



Universiteit
Leiden
The Netherlands

Franchising legal frameworks: a comparative study of the DCFR, US law and Australian law regarding franchise contracts

Sriporm, C.

Citation

Sriporm, C. (2023, June 22). *Franchising legal frameworks: a comparative study of the DCFR, US law and Australian law regarding franchise contracts*. Meijers-reeks. Retrieved from <https://hdl.handle.net/1887/3626652>

Version: Publisher's Version

License: [Licence agreement concerning inclusion of doctoral thesis in the Institutional Repository of the University of Leiden](#)

Downloaded from: <https://hdl.handle.net/1887/3626652>

Note: To cite this publication please use the final published version (if applicable).

Franchising Legal Frameworks

Franchising Legal Frameworks

A Comparative Study of the DCFR, US Law and
Australian Law Regarding Franchise Contracts

PROEFSCHRIFT

ter verkrijging van
de graad van doctor aan de Universiteit Leiden,
op gezag van rector magnificus prof.dr.ir. H. Bijl,
volgens besluit van het college voor promoties
te verdedigen op donderdag 22 juni 2023
klokke 11.15 uur

door

Chalermwut Sriporm

geboren te Udon Thani, Thailand

in 1986

Promotores: prof. dr. Jac. Hijma
Copromotor: dr. I.S.J. Houben
Promotiecommissie: dr. C.J.W. Baaij (Utrecht University)
prof. dr. J.M. Buchan (UNSW Sydney, Australia)
prof. dr. T.J. de Graaf
prof. dr. H.B. Krans
prof. dr. V. Mak

This research project was funded by a full scholarship from the Royal Thai Government in the period between 1 March 2017 and 17 January 2021.

Omslagontwerp: Primo!Studio, Delft
Opmaak binnenwerk: Anne-Marie Krens – Tekstbeeld – Oegstgeest
Drukwerk: Ipskamp Printing – Enschede

ISBN 978 94 6473 088 3

© 2023 C. Sriporm

Behoudens de in of krachtens de Auteurswet gestelde uitzonderingen mag niets uit deze uitgave worden verveelvoudigd, opgeslagen in een geautomatiseerd gegevensbestand, of openbaar gemaakt, in enige vorm of op enige wijze, hetzij elektronisch, mechanisch, door fotokopieën, opnamen of enige andere manier, zonder voorafgaande schriftelijke toestemming van de uitgever.

Voor zover het maken van reprografische verveelvoudigingen uit deze uitgave is toegestaan op grond van artikel 16h Auteurswet dient men de daarvoor wettelijk verschuldigde vergoedingen te voldoen aan de Stichting Reprorecht (Postbus 3051, 2130 KB Hoofddorp, www.reprorecht.nl). Voor het overnemen van (een) gedeelte(n) uit deze uitgave in bloemlezingen, readers en andere compilatiewerken (art. 16 Auteurswet) kan men zich wenden tot de Stichting PRO (Stichting Publicatie- en Reproductierechten Organisatie, Postbus 3060, 2130 KB Hoofddorp, www.stichting-pro.nl).

No part of this book may be reproduced in any form, by print, photoprint, microfilm or any other means without written permission from the publisher.

This PhD dissertation is dedicated to my beloved mother, *Payom Sriprom*, who was in the battle against terminal lung cancer for several years and departed her life in 2021. At that time, it was a grueling task for me to write this PhD dissertation because I was exhausted mentally and physically worrying about her serious illness. However, I never thought of relinquishing this doctoral project as my mother was longing for the publication of this book. The hope to see my book get published drove her fight against the deadly disease. Sadly, she could not make it. Therefore, I would like to dedicate this book to my dearest mother. I wish she looked down on me from heaven so I could tell her that: *I am so grateful for all you wholeheartedly made to cherish and support me. You are my wonderful mother forever. I love you.*

Acknowledgements

Writing this PhD dissertation is a long journey, taking my time half a decade. Undoubtedly, I have completed this journey, to a large extent, because of the tremendous assistance and support I received from many people. I am deeply indebted to the Royal Thai Government for a full scholarship granted to me from 1 March 2017 to 17 January 2021. This substantial funding enabled me to carry out my Ph.D. project without having to worry about the expense of so doing. Special thanks also go to the staff of Sanya Dharmasakti Library of Thammasat University for actively responding to my suggestions for acquiring copies of franchise law literature.

I am incredibly grateful to my supervisor and co-supervisor: Prof. dr. Jac. Hijma and Dr. I.S.J. Houben. Writing this dissertation was possible because they gave me a wonderful opportunity to pursue my Ph.D. project in the first place. Throughout the period of my Ph.D. studies, Prof. Hijma and Dr. Houben dedicated their valuable time and energy to provide me extremely helpful advice regarding how to conduct the PhD research, as well as offer unwavering support in professional and personal aspects. Sometimes, I experienced a miserable time, thereby making a slow research progress. Prof. Hijma and Dr. Houben never lost confidence in me and encouraged me to keep writing this dissertation steadily.

I am thankful to Prof. mr. M.E. Koppenol-Laforce and Prof. dr. J.I. van der Rest for their thought-provoking advice during an evaluation meeting held in the second year of the PhD studies. I am also grateful to members of the Doctorate committee: Dr. C.J.W. Baaij, Prof. dr. J.M. Buchan, Prof. dr. T.J. de Graaf, Prof. dr. H.B. Krans, and Prof. dr. V. Mak. Their suggestions for refining my dissertation were very constructive. Those suggestions also enabled me to make this dissertation the finest version.

I would have been remiss if I did not mention people who made my time in Leiden delightful and unforgettable. Special thanks go to Siriwan Thathong and her lovely family, Sungwan Klassen-Malaikhwan, Lalin Kovudhikulrungsri, Pimmanus Wibulsilp, Jin Choi, Shuai Guo, Jing Zhang, Weidong Zhang, Mikael Migu Soge and his wife, Diana Arias, Herra Pahasari and her family, Wilberdine Thoe Schwartzenberg, and Hetty ten Oever. I would also like to thank Surasak Boonrueang for regularly offering moral encouragement during my PhD studies. I thank Preeyaporn Ubonsawat for accompanying me to explore several cities in France, and Matika Vinichsorn for helping me find a much-needed book on franchising in the USA.

Above all, I would not have stood firm to finish this marathon journey without a terrific support from my beloved family. No amount of words would be sufficient to express my gratitude to my wonderful wife, Wannisa Panprom. My wife wholeheartedly endorsed my ambition to earn a doctoral degree at Leiden Law School. She also held my hand tight to get through hard times during the studies. Her endorsement and dedication are invaluable to me. Thank you for standing by me. I also would like to express my heartfelt appreciation to my father and sister: Kusol Sriprom and Phonsiri Sriprom, as well as Chamnan Panprom and Praphaisri Panprom, my father-in-law and mother-in-law. I had energy in writing this dissertation because they always gave me a happy home. Lastly, I sincerely thank Bualoy Ketrit (Pa Loy) for her amazing moral support.

Table of contents

1	INTRODUCTION	1
1.1	Introduction	1
1.2	Subject of the research	1
1.2.1	Introduction	1
1.2.2	Franchise as a contract-based marketing model	2
1.2.3	Asymmetrical relationship	4
1.2.4	Conclusions	5
1.3	Problems in a franchise life cycle	5
1.3.1	Introduction	6
1.3.2	Franchisor opportunism	6
1.3.3	Franchisor opportunism in a pre-contractual stage of a franchise relationship	7
1.3.4	Franchisor opportunism in an ongoing franchise relationship	8
1.3.4.1	Franchisor encroachment	8
1.3.4.2	Failure to provide adequate assistance and support	9
1.3.5	Franchisor opportunism related to an end of a franchise relationship	10
1.3.5.1	Transfer of a franchise contract	10
1.3.5.2	Non-renewal of a franchise contract	11
1.3.5.3	Termination of a franchise contract	12
1.3.6	Conclusions	13
1.4	Research objective	13
1.4.1	Introduction	13
1.4.2	Formulation of private law rules under franchise-specific law	14
1.4.2.1	Franchise-specific law	14
1.4.2.2	Private law rules	15
1.4.3	Conclusions	16
1.5	Research questions	16
1.5.1	Introduction	16
1.5.2	Sub-questions as regards a pre-contractual franchise relationship	17
1.5.3	Sub-questions as regards an ongoing franchise relationship	17
1.5.4	Sub-questions as regards an end of a franchise relationship	18
1.5.5	Conclusions	18
1.6	Research designs	19
1.6.1	Introduction	19
1.6.2	Doctrinal legal approach as a research methodology	19
1.6.3	Comparative law as a research method	20
1.6.3.1	Selection of the three legal systems	21
1.6.3.2	Documentation as an information collection method	29
1.6.4	Conclusions	30
1.7	Structure of the book	30

2	DEFINITION AND ESSENTIAL ELEMENTS OF A FRANCHISE	33
2.1	Introduction	33
2.2	The Draft Common Frame of Reference (DCFR)	34
2.2.1	Introduction	34
2.2.2	Contract	34
2.2.3	Right to conduct a franchise business	35
2.2.3.1	Control over a franchise business operation	36
2.2.3.2	Independence in a franchise business operation	36
2.2.4	Right to use the business package	37
2.2.5	Monetary considerations	37
2.2.6	Conclusions	38
2.3	The United States of America (USA)	38
2.3.1	Introduction	38
2.3.2	Contract, agreement, or arrangement	39
2.3.3	Right to conduct a franchise business	40
2.3.3.1	Significant control and assistance	40
2.3.3.2	Marketing plan or system	42
2.3.3.3	Community of interest	44
2.3.3.4	Substantial reliance	45
2.3.4	Use of the franchisor's marks	45
2.3.5	Monetary considerations	46
2.3.6	Conclusions	47
2.4	Australia	47
2.4.1	Introduction	47
2.4.2	Agreement	48
2.4.3	Right to conduct a franchise business	49
2.4.4	Use of a trademark, advertising or a commercial symbol	50
2.4.5	Monetary considerations	50
2.4.6	Conclusions	51
2.5	Comparative analysis	51
2.5.1	Introduction	51
2.5.2	Comparison and discussion	51
2.5.2.1	Similarity	51
2.5.2.2	Difference	53
2.5.2.3	Discussion	55
2.5.3	Conclusions	60
2.5.3.1	Concluding remarks	60
2.5.3.2	Key recommendations	61
2.6	Conclusions	62
3	REGULATION OF PRE-CONTRACTUAL INFORMATION OBLIGATIONS OF THE FRANCHISOR	63
3.1	Introduction	63
3.2	Duty of pre-contractual disclosure	64
3.2.1	Introduction	64
3.2.2	The Draft Common Frame of Reference (DCFR)	64

3.2.2.1	Introduction	64
3.2.2.2	Elements of a pre-contractual information duty	65
3.2.2.3	Conclusions	68
3.2.3	The United States of America (USA)	69
3.2.3.1	Introduction	69
3.2.3.2	Elements of a pre-contractual information duty	69
3.2.3.3	Conclusions	77
3.2.4	Australia	77
3.2.4.1	Introduction	77
3.2.4.2	Elements of a pre-contractual information duty	78
3.2.4.3	Conclusions	82
3.2.5	Comparative analysis	82
3.2.5.1	Introduction	82
3.2.5.2	Comparison and discussion	83
3.2.5.3	Conclusions	99
3.3	Duty to provide complete, current and accurate information	101
3.3.1	Introduction	101
3.3.2	The Draft Common Frame of Reference (DCFR)	101
3.3.2.1	Introduction	101
3.3.2.2	Disclosure rule	102
3.3.2.3	Rule relating to good faith and fair dealing	102
3.3.2.4	Conclusions	103
3.3.3	The United States of America (USA)	104
3.3.3.1	Introduction	104
3.3.3.2	Disclosure requirements	104
3.3.3.3	Updating requirements	105
3.3.3.4	Prohibition against misrepresentations	107
3.3.3.5	Conclusions	108
3.3.4	Australia	108
3.3.4.1	Introduction	108
3.3.4.2	Duty to maintain a disclosure document	108
3.3.4.3	Duty to act in good faith	109
3.3.4.4	Prohibition against misleading conduct	111
3.3.4.5	Conclusions	112
3.3.5	Comparative analysis	113
3.3.5.1	Introduction	113
3.3.5.2	Comparison and analysis	113
3.3.5.3	Conclusions	117
3.4	Private law remedies	118
3.4.1	Introduction	118
3.4.2	The Draft Common Frame of Reference (DCFR)	119
3.4.2.1	Introduction	119
3.4.2.2	Enforcement of performance	119
3.4.2.3	Monetary compensation	120
3.4.2.4	Cancellation of a contract	122
3.4.2.5	Conclusions	126
3.4.3	The United States of America (USA)	127
3.4.3.1	Introduction	127

3.4.3.2	Enforcement of performance	127
3.4.3.3	Monetary compensation	129
3.4.3.4	Cancellation of a contract	135
3.4.3.5	Conclusions	141
3.4.4	Australia	141
3.4.4.1	Introduction	141
3.4.4.2	Enforcement of performance	142
3.4.4.3	Monetary compensation	144
3.4.4.4	Cancellation of a contract	147
3.4.4.5	Conclusions	151
3.4.5	Comparative analysis	151
3.4.5.1	Introduction	151
3.4.5.2	Comparison and analysis	151
3.4.5.3	Conclusions	163
3.5	Conclusions	164
4	REGULATION OF THE FRANCHISOR'S ONGOING OBLIGATIONS	167
4.1	Introduction	167
4.2	Duty not to encroach	168
4.2.1	Introduction	168
4.2.2	The Draft Common Frame of Reference (DCFR) <i>cum annexis</i>	168
4.2.2.1	Introduction	168
4.2.2.2	Regulation by the express terms of a franchise contract	169
4.2.2.3	Regulation by the implied terms of a franchise contract	172
4.2.2.4	Conclusions	174
4.2.3	The United States of America (USA)	174
4.2.3.1	Introduction	174
4.2.3.2	Regulation by the rules of franchise relationship law	175
4.2.3.3	Regulation by the express terms of a franchise contract	177
4.2.3.4	Regulation by the implied terms of a franchise contract	180
4.2.3.5	Conclusions	182
4.2.4	Australia	183
4.2.4.1	Introduction	183
4.2.4.2	Regulation by the rule of the Franchising Code of Conduct	183
4.2.4.3	Regulation by the express terms of a franchise contract	184
4.2.4.4	Regulation by the implied terms of a franchise contract	185
4.2.4.5	Conclusions	187
4.2.5	Comparative analysis	187
4.2.5.1	Introduction	187
4.2.5.2	Comparison and analysis	187
4.2.5.3	Conclusions	200
4.3	Duty to assist	201
4.3.1	Introduction	201
4.3.2	The Draft Common Frame of Reference (DCFR)	202
4.3.2.1	Introduction	202
4.3.2.2	Regulation by the express terms of a franchise contract	202

4.3.2.3	Regulation by the terms generated by the rule of the DCFR	203
4.3.2.4	Conclusions	204
4.3.3	The United States of America (USA)	205
4.3.3.1	Introduction	205
4.3.3.2	Regulation by the express terms of a franchise contract	205
4.3.3.3	Conclusions	207
4.3.4	Australia	207
4.3.4.1	Introduction	207
4.3.4.2	Regulation by the express terms of a franchise contract	208
4.3.4.3	Conclusions	209
4.3.5	Comparative analysis	209
4.3.5.1	Introduction	209
4.3.5.2	Comparison and analysis	209
4.3.5.3	Conclusions	215
4.4	Private law remedies	217
4.4.1	Introduction	217
4.4.2	The Draft Common Frame of Reference (DCFR)	217
4.4.2.1	Introduction	217
4.4.2.2	Enforcement of performance	217
4.4.2.3	Monetary compensation	219
4.4.2.4	Cancellation of a franchise contract	220
4.4.2.5	Conclusions	223
4.4.3	The United States of America (USA)	223
4.4.3.1	Introduction	223
4.4.3.2	Enforcement of performance	224
4.4.3.3	Monetary compensation	226
4.4.3.4	Cancellation of a franchise contract	229
4.4.3.5	Conclusions	234
4.4.4	Australia	235
4.4.4.1	Introduction	235
4.4.4.2	Enforcement of performance	235
4.4.4.3	Monetary compensation	238
4.4.4.4	Cancellation of a franchise contract	241
4.4.4.5	Conclusions	245
4.4.5	Comparative analysis	246
4.4.5.1	Introduction	246
4.4.5.2	Comparison and analysis	246
4.4.5.3	Conclusions	255
4.5	Conclusions	257
5	REGULATION OF TRANSFER, NON-RENEWAL, AND TERMINATION OF A FRANCHISE CONTRACT	259
5.1	Introduction	259
5.2	Transfer of a franchise contract	260
5.2.1	Introduction	260
5.2.2	The Draft Common Frame of Reference (DCFR)	260
5.2.2.1	Introduction	260

5.2.2.2	Regulation of transfer by the rules of the DCFR	260
5.2.2.3	Regulation of transfer by the terms of a franchise contract	262
5.2.2.4	Conclusions	263
5.2.3	The United States of America (USA)	264
5.2.3.1	Introduction	264
5.2.3.2	Regulation of transfer by the rules of franchise relationship law	264
5.2.3.3	Regulation of transfer by the terms of a franchise contract	266
5.2.3.4	Conclusions	268
5.2.4	Australia	269
5.2.4.1	Introduction	269
5.2.4.2	Regulation of transfer by the transfer rules	269
5.2.4.3	Regulation of transfer by the terms of a franchise contract	271
5.2.4.4	Conclusions	272
5.2.5	Comparative analysis	272
5.2.5.1	Introduction	272
5.2.5.2	Comparison and discussion	273
5.2.5.3	Conclusions	283
5.3	Non-renewal of a franchise contract	284
5.3.1	Introduction	284
5.3.2	The Draft Common Frame of Reference (DCFR)	285
5.3.2.1	Introduction	285
5.3.2.2	Regulation of non-renewal by the rules of the DCFR	285
5.3.2.3	Regulation of non-renewal by the terms of a franchise contract	286
5.3.2.4	Conclusions	287
5.3.3	The United States of America (USA)	287
5.3.3.1	Introduction	287
5.3.3.2	Regulation of non-renewal by the rules of franchise relationship law	288
5.3.3.3	Regulation of non-renewal by the terms of a franchise contract	290
5.3.3.4	Conclusions	291
5.3.4	Australia	291
5.3.4.1	Introduction	291
5.3.4.2	Regulation of non-renewal by the rules of the Franchising Code of Conduct	291
5.3.4.3	Regulation of non-renewal by the terms of a franchise contract	292
5.3.4.4	Conclusions	293
5.3.5	Comparative analysis	293
5.3.5.1	Introduction	293
5.3.5.2	Comparison and discussion	294
5.3.5.3	Conclusions	299
5.4	Termination of a franchise contract	300
5.4.1	Introduction	300
5.4.2	The Draft Common Frame of Reference (DCFR)	301
5.4.2.1	Introduction	301

5.4.2.2	Regulation of termination by the rules of the DCFR	301
5.4.2.3	Regulation of termination by the terms of a franchise contract	303
5.4.2.4	Conclusions	305
5.4.3	The United States of America (USA)	305
5.4.3.1	Introduction	305
5.4.3.2	Regulation of termination by the rules of franchise relationship law	306
5.4.3.3	Regulation of termination by the rules of common law	310
5.4.3.4	Regulation of termination by the terms of a franchise contract	313
5.4.3.5	Conclusions	314
5.4.4	Australia	314
5.4.4.1	Introduction	314
5.4.4.2	Regulation of termination by the rules of the Franchising Code of Conduct	315
5.4.4.3	Regulation of termination by the rules of common law	317
5.4.4.4	Regulation of termination by the terms of a franchise contract	318
5.4.4.5	Conclusions	319
5.4.5	Comparative analysis	319
5.4.5.1	Introduction	319
5.4.5.2	Comparison and discussion	320
5.4.5.3	Conclusions	335
5.5	Private law remedies	337
5.5.1	Introduction	337
5.5.2	The Draft Common Frame of Reference (DCFR)	338
5.5.2.1	Introduction	338
5.5.2.2	Enforcement of performance	338
5.5.2.3	Monetary compensation	339
5.5.2.4	Cancellation of a contract	341
5.5.2.5	Specific remedies	344
5.5.2.6	Conclusions	347
5.5.3	The United States of America (USA)	347
5.5.3.1	Introduction	347
5.5.3.2	Enforcement of performance	348
5.5.3.3	Monetary compensation	351
5.5.3.4	Cancellation of a contract	354
5.5.3.5	Specific remedies	356
5.5.3.6	Conclusions	359
5.5.4	Australia	360
5.5.4.1	Introduction	360
5.5.4.2	Enforcement of performance	360
5.5.4.3	Monetary compensation	362
5.5.4.4	Cancellation of a contract	365
5.5.4.5	Specific remedies	368
5.5.4.6	Conclusions	370

5.5.5	Comparative analysis	371
5.5.5.1	Introduction	371
5.5.5.2	Comparison and discussion	371
5.5.5.3	Conclusions	386
5.6	Conclusions	388
6	CONCLUSION	389
6.1	Introduction	389
6.2	Definition of a franchise	390
6.2.1	Research findings	390
6.2.2	Recommendation	391
6.2.3	Limitation	391
6.3	Regulation of pre-contractual information obligations of the franchisor	392
6.3.1	Duty of pre-contractual disclosure	392
6.3.1.1	Research findings	392
6.3.1.2	Recommendation	392
6.3.1.3	Limitation	393
6.3.2	Duty to provide complete, current and accurate information	394
6.3.2.1	Research findings	394
6.3.2.2	Recommendation	395
6.3.2.3	Limitation	395
6.3.3	Private law remedies	396
6.3.3.1	Research findings	396
6.3.3.2	Recommendation	396
6.3.3.3	Limitation	397
6.4	Regulation of the franchisor's ongoing obligations	398
6.4.1	Duty not to encroach	398
6.4.1.1	Research findings	398
6.4.1.2	Recommendation	398
6.4.1.3	Limitation	399
6.4.2	Duty to assist	399
6.4.2.1	Research findings	399
6.4.2.2	Recommendation	400
6.4.2.3	Limitation	400
6.4.3	Private law remedies	401
6.4.3.1	Research findings	401
6.4.3.2	Recommendation	401
6.4.3.3	Limitation	402
6.5	Regulation of transfer, non-renewal, and termination of a franchise contract	402
6.5.1	Transfer of a franchise contract	402
6.5.1.1	Research findings	402
6.5.1.2	Recommendation	403
6.5.1.3	Limitation	403
6.5.2	Non-renewal of a franchise contract	404
6.5.2.1	Research findings	404

6.5.2.2 Recommendation	404
6.5.2.3 Limitation	405
6.5.3 Termination of a franchise contract	405
6.5.3.1 Research findings	405
6.5.3.2 Recommendation	406
6.5.3.3 Limitation	407
6.5.4 Private law remedies	408
6.5.4.1 Research findings	408
6.5.4.2 Recommendation	408
6.5.4.3 Limitation	409
6.6 Conclusions and epilogue	409
SUMMARY	415
SAMENVATTING (DUTCH SUMMARY)	419
SELECTED BIBLIOGRAPHY	425
CURRICULUM VITAE	435

1 Introduction

1.1 INTRODUCTION

This doctoral thesis undertakes a comparative study of the franchise legal framework of the European Draft Common Frame of Reference (DCFR), the United States of America (USA), and Australia, regulating franchisor opportunism in a franchise life cycle. This comparative legal study aims to propose guidelines for drafting private law rules in comprehensive franchise law regulating a franchise contractual relationship. The principal purpose of the franchise regulation to be recommended is to provide a weaker franchisee with legal protection against the franchisor's opportunistic conduct during the three stages of a franchise life cycle, from a pre-contractual stage of a franchise relationship to an end of a franchise relationship. Ultimately, this research study intends to offer a source of inspiration for legal systems that aim to introduce franchise-specific legislation regulating a franchise contractual relationship at the national level.

Chapter one is an introductory chapter; it outlines the framework of the doctoral thesis. The structure of the first chapter is as follows. Apart from this section, section 1.2 will acquaint readers with a general understanding of a franchise as the subject matter of this research study. This section will also point out the very nature of a franchise relationship. Then, section 1.3 will identify particular relational problems caused by franchisor opportunism in a franchise life cycle. After that, section 1.4 will set the ultimate research goal based on the problems identified in the preceding section. Section 1.5 will develop an overarching research question and sub-research questions to form a foundation for carrying out the research to achieve the study's prime objective. Section 1.6 will elaborate on the chosen research methodology, research method, and information collection method. In the end, section 1.7 will summarize the structure of this book.

1.2 SUBJECT OF THE RESEARCH

1.2.1 Introduction

In distributing goods or services, producers of the products may employ various marketing strategies. Some business owners may bring their products to the market without intermediaries through face-to-face selling, online selling, and telemarketing, to name a few. Nevertheless, these direct marketing methods may not be a good choice if the producers intend to expand their market extensively. With this marketing concern, many business owners frequently create indirect marketing channels to distribute their goods or

services to the market. Among other indirect channels, some producers choose a franchise model to dispense their products to customers residing in various market areas. Section 1.2.2 will explain how a franchise model functions in a distribution system and why it is increasing a popular model from a business owner's viewpoint. Section 1.2.3 will identify the intrinsic nature of a franchise relationship, which is a source of some relational problems. Section 1.2.4 will sum up the character of a franchise apprehended in this thesis.

1.2.2 Franchise as a contract-based marketing model

From a marketing perspective, a franchise model creates an indirect distribution channel. In the distribution context, producers of goods or services may assign the task of selling or distributing goods or services to some selected channel partners who operate businesses independently from the producers. These channel partners may include retailers, wholesalers, brokers, and agents.¹ In this respect, the role of the channel partners will vary depending upon the types of channel partners and, particularly, the marketing system organized by a business owner. In designing a distributing system, some producers select a vertical marketing system (VMS) to dispense their products to the market. According to Armstrong and others, VMS is a unified marketing system consisting of producers, wholesalers, and retailers. VMS can be divided into three types: corporate, administered, and contractual VMS.²

Of the three VMS types, business owners may choose a franchise model as a distribution system. From a marketing viewpoint, a franchise is a contract-based arrangement in which the producer (franchisor) who owns the right to brand and business model licenses independent partners (franchisees) to use the producer's trademark and operate a franchised business. A franchise model is said to be categorized into three types: (1) a manufacturer-sponsored retailer franchise, (2) a manufacturer-sponsored wholesaler franchise, and (3) a service firm-sponsored retailer franchise.³ In practice, a franchise model has been employed in various industries.⁴ According to Seid, a franchise business model has been adopted by approximately 120 sectors, including restaurants, hotels, education, and medical services.⁵

Nowadays, franchise businesses have increasingly been commonplace. Many countries around the world have seen the growth of businesses employ-

1 Gary Armstrong, Philip Kotler, and Marc Oliver Opresnik, *Marketing: An Introduction* (7th global edn, Pearson Education Limited 2023) 331-32.

2 Ibid 334-35.

3 Ibid 335.

4 William G Nickels, James M McHugh and Susan M McHugh, *Understanding Business* (12th edn, The McGraw-Hill Companies 2018) 134.

5 Michael Seid, 'Product and Trade Name Franchising' *The Balance* (15 August 2019), <<https://bit.ly/3dThSGP>> accessed 17 February 2023.

ing a franchise model. Some businesses enjoy success because of a franchise model. An example of a successful franchise business is McDonald's, the US-based franchise company with over 38,000 franchised outlets worldwide.⁶ From the experiences of many people, therefore, a franchise is seemingly a popular marketing model. However, there should be some justifications for that assumption. Several pieces of literature provide that business owners employ a franchise model to distribute their goods or services because of the following three advantages.⁷

First, the producers can acquire additional capital from selling their franchise business. In joining a franchise organization, business partners or purchasers of a franchise will be required to pay fees in the form of upfront franchise fees and ongoing fees, such as royalties. The collection of these fees would enable the franchise owners to acquire funding for expanding their business without heavily depending upon loans from financial institutions, such as commercial banks.

The second benefit is informational; business owners can obtain information about geographical locations and local communities through the members of a franchise organization. This local information shared by the business partners would help the producers effectively market their products in dispersed areas about which the producers know very little. In this case, the franchise owners can make an informed decision if their goods or services are distributed in particular markets.

The third advantage is concerned with staff management; producers can shift responsibility for labor supply to the members of a franchise system. In the franchising context, thus, franchise partners will be responsible for hiring their employees. In other words, the franchise partners need to employ their staff themselves. The shift in this managerial responsibility would reduce the producers' payroll costs as the producers will not have to recruit employees for their business partners.

However, no business model has 100-percent-advantages. Thus, it should be mentioned that a franchise model may have some drawbacks for business owners. For example, a franchise owner may encounter a loss of control over its brand and system. In particular, the franchise owner may not control the day-to-day operation of its business partners. Moreover, the franchise owner

6 McDonald's, 'Franchising Overview' <<https://bit.ly/3EcMVgE>> accessed 17 February 2023.

7 Warren S Grimes, 'When Do Franchisors Have Market Power – Antitrust Remedies for Franchisor Opportunism' (1996) 65(1) *Antitrust Law Journal* 105, 108; Steven C Michael, 'First mover advantage through franchising' (2003) 18 *Journal of Business Venturing* 61, 64; Rajiv P Dant and Patrick Kaufmann, 'Structural and strategic dynamics in franchising' (2003) 79 *Journal of Retailing* 63, 64-65; Anna Watson and others, 'Retail franchising: an intellectual capital perspective' (2005) 12 *Journal of Retailing and Consumer Services* 25, 25-26; Arto Lindblom and Henriikki Tikkanen, 'Knowledge creation and business format franchising' (2010) 48 *Management Decision* 179, 180.

may not gain a high revenue from franchising as it would have received from the company-owned branches.⁸

1.2.3 Asymmetrical relationship

The preceding section illustrates that a franchise is a marketing model based on a contractual arrangement between a franchisor and a franchisee. A franchise is a business contract because the contract is ordinarily concluded by business persons, who are enterprises that typically aim to make profits in the course of the agreement. One commentator figuratively says that a franchise is a business marriage between a franchisor and a franchisee.⁹ Despite the fact that a franchise is a commercial relationship, many individual franchisees may not confront franchisors on an equal footing.¹⁰ Thus, in many senses, a franchise relationship is normally regarded as an asymmetrical relationship.¹¹ One scholar even claims that franchise asymmetry is a distinguishing nature or *sine qua non* of franchise relationships.¹²

In the franchising context, franchise asymmetries may take the form of information and power asymmetries.¹³ In the former case, it is explained that a prospective franchisee usually lacks balanced and reliable information about a franchise in general and a franchise system in particular. This situation results from the fact that a franchisor exclusively possesses the material information, which is not easily accessible to the prospective franchisee.¹⁴ In the latter case,

8 Dennis E Wieczorek and Max J Schott II, 'Chapter 2: Structuring the Franchise Relationship' in Rupert M Barkoff and others (eds), *Fundamentals of Franchising* (4th edn, American Bar Association 2016) 63.

9 William L Killion, 'Chapter 1: The History of Franchising' in Alexander M Meiklejohn (ed), *Franchising: Cases, Materials, & Problems* (American Bar Association 2013) 2.

10 Paul Steinberg and Gerald Lescatre, 'Beguiling Heresy: Regulating the Franchise Relationship' (2004) 109(1) Penn State Law Review 105, 174.

11 Nirmalya Kumar, Lisa K Scheer, and Jan-Benedict E M Steenkamp, 'The Effects of Supplier Fairness on Vulnerable Resellers' (1995) 32 Journal of Marketing Research 54, 54; Jenny Buchan, 'Deconstructing the Franchise as a Legal Entity: Practice and Research in International Franchise Law' (2014) 21 Journal of Marketing Channels 143, 148; Jennifer L L Gant and Jenny Buchan, 'Moral Hazard, Path Dependency and Failing Franchisors: Mitigating Franchisee Risk Through Participation' (2019) 47(2) Federal Law Review 261, 266.

12 Tibor Tajti, 'Franchise and Contract Asymmetry: A Common Trans-Atlantic Agenda' (2015) 37 Loyola of Los Angeles International and Comparative Law Review 245, 248.

13 Other scholars may categorize franchise asymmetries differently. For example, Buchan divides asymmetries in franchising into information asymmetry, adviser asymmetry, education and regulator asymmetry, risk and reward asymmetry, resource asymmetry, contract asymmetry, and regulatory asymmetry. See Jenny Buchan, *Franchisees as Consumers: Benchmarks, Perspectives and Consequences* (Springer 2013) 85-100.

14 Elizabeth Crawford Spencer, *The Regulation of Franchising in the New Global Economy* (Edward Elgar Publishing Limited 2010) 64-65; Lorelle Frazer and others, 'Pre-contractual Due Diligence by Franchisees and Independent Small Business Buyers' (2018) 46 Australian Business Law Review 157, 159.

a franchisor is commonly more powerful than a franchisee.¹⁵ In particular, the franchisor usually holds greater bargaining power than the franchisee.¹⁶ A vivid example is that the franchisor typically offers a franchise contract as a standard form contract in which the franchisee barely negotiates the terms of the contract.¹⁷ Besides, a franchisor is usually more sophisticated than a franchisee in terms of business experiences.¹⁸ Some empirical studies affirm this phenomenon; they show that a franchisee usually has no prior business experience. Thus, the franchisee typically joins a franchise system to seek assistance, training, and operational manuals from the franchisor. From a franchisor's perspective, these inexperienced franchisees are more preferred as they are easily controllable.¹⁹

1.2.4 Conclusions

This doctoral thesis takes a franchise relationship as the subject matter of the research. In this research study, a franchise is perceived as a marketing relationship created by a franchise contract concluded between a franchisor and a franchisee. More importantly, a franchise relationship, perceived in this research study, is considered an asymmetrical franchise relationship because of the fact that the franchisor exclusively possesses essential information about a franchise system and holds superior bargaining power over the franchisee. As will be seen in the following section, this asymmetrical character of a franchise relationship can be the source of particular relational problems that need a certain degree of regulation by law.

1.3 PROBLEMS IN A FRANCHISE LIFE CYCLE

15 In the marketing context, the term 'power' is understood as the ability to influence perceptions, behaviors, and decision-making of other channel partners. Thus, a person who holds power will have a dominant influence over the channel members. See Erin Anderson, Leonard M Lodish and Barton A Weitz, 'Resource Allocation Behavior in Conventional Channels' (1987) 24(1) *Journal of Marketing Research* 85, 87.

16 David Gurnick and Steve Vieux, 'Case History of the American Business Franchise' (1999) 24 *Oklahoma City University Law Review* 37, 40; Jenny Buchan, 'Challenges that franchisees of insolvent franchisors pose for liquidator' (2008) 16 *Insolvency Law Journal* 26, 30; Ateeque Shaikh, 'Conceptualizing fairness in franchisor-franchisee relationship: Dimensions, definitions and preliminary construction of scale' (2016) 28 *Journal of Retailing and Consumer Services* 28, 28.

17 Buchan, *Franchisees as Consumers: Benchmarks, Perspectives and Consequences* (n 13) 72-75.

18 Gillian K Hadfield, 'Problematic Relations: Franchising and the Law of Incomplete Contracts' (1990) 42(4) *Stanford Law Review* 927, 991.

19 Robert W Emerson and Uri Benoliel, 'Are Franchisees Well-Informed: Revisiting the Debate over Franchise Relationship Laws' (2012) 76 *Albany Law Review* 193, 203-09.

1.3.1 Introduction

There is always the likelihood of franchisor opportunism in an asymmetrical franchise relationship.²⁰ In this kind of relationship, it is likely that a superior franchisor behaves opportunistically towards a franchisee.²¹ In some cases, franchisor opportunism inflicts financial loss or damage to an aggrieved franchisee.²² This doctoral thesis intends to work on the potential relational problems generated by franchisor opportunism. Since the expression 'franchisor opportunism' may sound unclear to several readers, this section will elaborate on this expression in section 1.3.2. Then, this section will identify practices of franchisor opportunism that could manifest in the three stages of a franchise life cycle in sections 1.3.3, 1.3.4, and 1.3.5, respectively. Section 1.3.6 will conclude on the main reason why the problems identified in this section are significant for this research study.

1.3.2 Franchisor opportunism

Explaining how the expression 'franchisor opportunism' is understood in this research study would be wise to clearly illustrate the source of the relational problems in an asymmetric franchise relationship. In this research study, the term 'opportunism' has an economic sense. From an economic perspective, Williamson provides that the word 'opportunism' refers to self-interest seeking with guile. Williamson also elaborates on the word 'guile'; he defines 'guile' as 'lying, stealing, cheating, and calculated efforts to mislead, distort, disguise, obfuscate, or otherwise confuse.'²³ This thesis takes the meaning of 'opportunism' defined by Williamson and understands 'franchisor opportunism' as the franchisor's unfair conduct, practice, and treatment toward a franchisee.

However, defining the term 'fairness' is a daunting task because the notion of fairness is broad and complicated. According to Murphy, the concept of fairness can be perceived differently in different contexts.²⁴ This doctoral thesis agrees with Murphy and anticipates that conceptualizing fairness requires a

20 Kumar, Scheer, and Steenkamp (n 11) 54.

21 Grimes (n 7) 112.

22 It is said that opportunism is the source of business failure. See Courtenay Atwell and Jenny Buchan, 'The Franchise Fulcrum: The Legal System's Contributions to Research about Power and Control in Business Format Franchising' (2014) 21 *Journal of Marketing Channels* 180, 181.

23 Oliver E Williamson, 'The Economics of Organization: The Transaction Cost Approach' (1981) 87 *American Journal of Sociology* 548, 554; Kenneth H Wathne and Jan B Heide, 'Opportunism in Interfirm Relationships: Forms, Outcomes, and Solutions' (2000) 64 *Journal of Marketing* 36, 38, citing Oliver E Williamson, *The Economic Institutions of Capitalism* (The Free Press 1985) 47.

24 Susan P Murphy, 'Fairness' in Deen K Chatterjee (ed), *Encyclopedia of Global Justice* (Springer 2011) 336.

lengthy philosophical discussion. Thus, this thesis will refer to the definition offered by Black Law's Dictionary for the sake of specificity. According to the Dictionary, the term 'fairness' is defined to mean the quality of treating people equally or in a reasonable way and the quality of impartiality and honesty.²⁵ In sum, this research study intends the expression 'franchisor opportunism' to capture any franchisor's unequal, unreasonable, partial, and dishonest conduct towards a franchisee.

Despite the recognition of franchisor opportunism, this doctoral thesis by no means excludes the likelihood of 'franchisee opportunism' in a franchise relationship. In the context of franchisee opportunism, some franchisees may behave opportunistically in the form of free-riding. That is, opportunistic franchisees may increase short-term profitability by failing to observe quality standards, under-investing in advertising, or failing to supervise their staff properly.²⁶ Nevertheless, the scale of franchisee opportunism in franchising is ordinarily trivial. It is argued that a franchisor has the power to limit the risk of franchisee opportunism. According to Spencer, the franchisor may use contractual terms to restrain a franchisee's opportunistic behaviors. Spencer exemplifies that the franchisor may impose reporting and minimum performance requirements on the franchisee. In this case, a breach of duties by a franchisee would allow the franchisor to resort to remedies for the breach.²⁷ This research study agrees with Spencer and, therefore, will not focus on relational problems connected with franchisee opportunism.

1.3.3 Franchisor opportunism in a pre-contractual stage of a franchise relationship

As mentioned in the preceding section, a franchisor usually holds substantial and confidential information pertaining to a franchise, such as information about the franchisor, the franchise system, and the franchise business. When a prospective franchisee approaches a franchisor for a license of a franchise, an opportunistic franchisor may withhold or distort essential information.²⁸ First, the franchisor may not provide the prospective franchisee with material information or select certain informational items to disclose to the franchisee. Second, the franchisor may provide a potential franchisee with modified and

25 Bryan A Garner (ed), *Black's Law Dictionary* (11th edn, Thomson West (US) 2019).

26 Jérôme Barthélemy, 'Agency and institutional influences on franchising decisions' (2011) 26(1) *Journal of Business Venturing* 93, 95.

27 Spencer (n 14) 72.

28 Jakki J Mohr and Ravipreet S Sohi, 'Communication Flows in Distribution Channels: Impact on Assessments of Communication Quality and Satisfaction' (1995) 71(4) *Journal of Retailing* 393, 395-96.

transformed information that turns out to be untrue or inaccurate.²⁹ The franchisor may engage in these unfair practices without legitimate reasons. In other words, the franchisor's conduct may be done opportunistically. For example, the franchisor may not disclose that the franchisor has been involved in civil or criminal lawsuits against it to increase franchise sales for economic incentives, such as collecting up-front franchise fees as much as possible.³⁰ This franchisor's conduct would cause financial harm to a prospective franchisee; a prospective franchisee will be susceptible to making an ill-advised decision because of the lack of substantial and candid information about a franchise. A wrong investment decision would result in the franchisee's business failure soon after opening a franchised business.

1.3.4 Franchisor opportunism in an ongoing franchise relationship

After a franchise contract is concluded, a franchise relationship is established and continues. In this stage of the relationship, however, the practice of franchisor opportunism can be manifold.³¹ According to Grimes, a franchisor's opportunistic behaviors typically include encroachment, misuse of franchisees' money, forcing a franchisee to bear certain risks, and limiting a franchisee's certain marketing discretions.³² For the sake of specificity, a choice of franchisor's opportunistic conduct will be made because it would not be feasible for this doctoral thesis to identify and discuss all the franchisor's potential misbehaviors in the course of an ongoing franchise relationship. In this research study, attention will be paid to franchisor opportunism in the form of franchisor encroachment and failure to provide adequate assistance and support.

1.3.4.1 Franchisor encroachment

Franchisor encroachment is claimed to be a form of franchisor opportunism.³³ During an ongoing relationship, an opportunistic franchisor may encroach upon an existing franchisee's business in three forms: territorial encroachment, product or service encroachment, and trademark encroachment. However, for specificity's sake, this research study will focus on the first form of franchisor encroachment. According to Vincent, territorial encroachment is a situation when

29 See eg *Federal Trade Commission v American Entertainment Distributors Inc* 2012 WL 12964783 (SD Fla, 2012) 8.

30 Grimes (n 7) 123-24.

31 Hadfield (n 18) 952.

32 Grimes (n 7) 125-26.

33 Uri Benoliel and Jenny Buchan, 'Franchisees' Optimism Bias and the Inefficiency of the FTC Franchise Rule' (2015) 13 *DePaul Business & Commercial Law Journal* 411, 415.

'[a] franchisor approves a new location, whether company-owned or franchised, which is close enough to an existing location so that the new location draws away some of the customers from the existing location, resulting in a reduction of sales for the older location.'³⁴

Besides, the franchisor encroachment can take traditional and non-traditional forms.³⁵

First, a franchisor may engage in traditional encroachment by opening a new company-own franchise unit or authorizing other new franchisees to operate a franchised outlet in close proximity to an incumbent franchisee's store.

Second, a franchisor may engage in non-traditional encroachment by distributing its goods or services through other alternative distribution channels, such as internet sales, which would result in competition with an existing franchisee's business.³⁶ In either case, the franchisor encroachment may contribute to a substantial decrease in the incumbent franchisee's sales volume, leading to the franchisee's business failure.³⁷

1.3.4.2 Failure to provide adequate assistance and support

The second relational issue to be discussed in this thesis is the franchisor's failure to provide assistance and support. In franchising, the viability of a franchised business is said to rely upon the franchisor's assistance, which typically includes site selection, training, provision of operational manuals, provision of ongoing advice, and other specific forms.³⁸ However, a franchisee may not receive proper assistance and support from a franchisor. On the one

34 William Slater Vincent, 'Encroachment: Legal Restrictions on Retail Franchise Expansion' (1998) 13 *Journal of Business Venturing* 29, 30.

35 It is said that an opportunistic franchisor may strategically utilize an encroachment for several purposes. For example, the franchisor may want to maximize sales of a franchise by establishing as many franchised units as possible. In increasing sales, the franchisor can collect more sale-based royalty fees from its franchisees. The franchisor may desire to avoid paying damages to a franchisee upon the termination of a franchise contract. In doing so, the franchisor may encroach upon the franchisee's territory, leading to the franchisee's surrender of operating a franchised business. See Roger D Blair and Francine Lafontaine, *The Economics of Franchising* (2nd edn, Cambridge University Press 2010) 214; Uri Benoliel, 'Criticizing the Economic Analysis of Franchise Encroachment Law' (2011) 75(1) *Albany Law Review* 205, 214.

36 Blair and Lafontaine, *ibid* 202.

37 Marc A Wites, 'The Franchisor as Predator: Encroachment and the Implied Covenant of Good Faith' (1996) 7 *University of Florida Journal of Law and Public Policy* 305, 306; Benoliel (n 35) 215-20.

38 Paul H Rubin, 'The Theory of the Firm and the Structure of the Franchise Contract' (1978) 21(1) *The Journal of Law and Economics* 223, 224; Craig Tractenberg, Jean-Philippe Turgeon, and Stéphanie Destrempes, 'The Franchisor's Duty to Police the Franchise System' (2016) 36 *Franchise Law Journal* 87, 87.

hand, a franchisor may not even commit itself to providing a franchisee with adequate assistance and support.³⁹ On the other hand, a franchisor may retain discretion in providing a franchisee with assistance and support.⁴⁰ In the latter case, the right of retention would open room for the franchisor to behave opportunistically toward the franchisee. For example, an opportunistic franchisor may choose to provide an inferior quality of support with the aim of cutting costs incurred to the franchisor. In either case, the lack of the franchisor's adequate assistance and support could reduce the franchisee's ability to make profits from operating a franchised business.⁴¹

1.3.5 Franchisor opportunism related to an end of a franchise relationship

In franchising, a franchisor may behave opportunistically toward a franchisee when a franchise relationship is approaching cessation of the relationship. Forms of franchisor opportunism related to an end of a franchise relationship may vary. For specificity's sake, this doctoral thesis will focus on the franchisor's opportunistic conduct in relation to transfer, non-renewal, and termination of a franchise contract.

1.3.5.1 *Transfer of a franchise contract*

In the course of a franchise relationship, a franchisee may desire to transfer a franchise to a third person. In general, a transfer of a franchise means a situation in which a franchisee chooses to sell or assign any portion of a franchise contract, ownership interests in the business entity that owns the franchise, the assets of the franchised business and/or the business itself before the expiry of the franchise agreement.⁴² For the sake of specificity, this research study understands a transfer of a franchise as a complete assignment of a franchise agreement, resulting in a transfer of the incumbent franchisee's rights and duties under the current franchise contract to the third person.

In reality, a franchisee may want to transfer a franchise contract for several reasons. For example, a franchisee may have successfully developed local goodwill attached to a franchised store, thereby resorting to redeeming the

39 Rubin (n 38) 224 and 230.

40 W Michael Garner, 'Editor's Column' (1991) 11 Franchise Law Journal 2, 26.

41 Marko Grünhagen, Xu (Vivian) Zheng, and Jeff Jianfeng Wang, 'When the Music Stops Playing: Post-litigation Relationship Dissolution in Franchising' (2017) 2 Journal of Retailing 138, 149.

42 Craig Tractenberg, 'Assignment, Termination, and Renewal' in Kenneth R Costello (ed), *Collateral Issues in Franchising: Beyond Registration and Disclosure* (American Bar Association 2015) 555.

value of goodwill by transferring a franchise contract to other parties.⁴³ In this case, a transfer of a franchise contract is an exit strategy for a transferring franchisee that allows the franchisee to recoup its investment. In transferring a franchise contract, it is said that a franchisor usually controls a franchisee's transfer by requiring the franchisee to obtain the franchisor's prior consent.⁴⁴ In many cases, a franchisor may withhold consent for good reasons. For instance, a franchisor may withhold its consent because a transferee fails to meet the franchisor's standard for recruiting a new franchisee. In some exceptional cases, a franchisor may withhold its consent opportunistically.⁴⁵ For example, a franchisor may withhold its consent to compel the franchisee's concessions or introduce a new franchise contract.⁴⁶ Apparently, these practices are unfair to the franchisee.⁴⁷

1.3.5.2 Non-renewal of a franchise contract

In practice, franchise contracts are typically concluded for a fixed term.⁴⁸ In many cases, a franchisee operates a franchised business until expiration. In this case, some franchisees may expect another successive term of a franchise contract that would permit them to recover the investments and earn profits.⁴⁹ A franchisor may decide not to renew an expiring franchise contract in contrast to the franchisee's expectation. Generally, the franchisor's non-renewal of a franchise contract is allowed since the franchisor customarily has no duty to renew the contract. The franchisor's non-renewal is justified as one of the sanctions that penalize unsatisfactory franchisees.⁵⁰

43 Jerome L Withered, 'The No-Assignment-without-Consent Clause in Franchise Agreements' (1984) 4 Franchise Law Journal 1, 14.

44 Jerrold G Van Cise, 'A Franchise Contract' (1969) 14 Antitrust Bulletin 325, 342; Withered, *ibid* 1; Steinberg and Lescatre (n 10) 210; Ronald K Gardner, Jr and Mary Kellerman DesCombaz, 'Chapter 11: Relationship and Termination Laws' in Alexander M Meiklejohn (ed), *Franchising: Cases, Materials, & Problems* (American Bar Association 2013) 568.

45 This situation normally occurs when a franchise contract provides unlimited or sole discretion to a franchisor, or the contract does not provide any standard for the franchisor to decide. Those contractual arrangements are said to be common in the franchising context. See Terrence M Dunn, 'The Franchisor's Control over the Transfer of a Franchise' (2008) 27 Franchise Law Journal 233, 233.

46 Antony W Dnes, 'A Case-Study Analysis of Franchise Contracts' (1993) 22 Journal of Legal Studies 367, 381, citing Ozanne and Hunt, *The Economic Effects of Franchising, Report Prepared for the United States Senate Small Business Administration* (1971) 272.

47 Peter C Lagarias and Edward Kushell, 'Fair Franchise Agreements from the Franchise Perspective' (2013) 33 Franchise Law Journal 3, 22.

48 Charles S Modell and Genevieve A Beck, 'Franchise Renewals – You Want Me to Do What' (2002) 22 Franchise Law Journal 4, 4; Blair and Lafontaine (n 35) 258.

49 Spencer (n 14) 292.

50 Antony W Dnes, 'Franchise Contracts, Opportunism and the Quality of Law' (2009) 3 Entrepreneurial Business Law Journal 257, 272.

In some cases, the franchisor's non-renewal of a franchise contract may be considered unfair to a franchisee. For example, it may be obvious from circumstances that an extension of the initial term of a franchise contract would allow an existing franchisee to realize the value of its goodwill in a franchised business.⁵¹ However, an opportunistic franchisor may intend to deprive the franchisee's goodwill by deciding not to renew a franchise contract.⁵² In this case, the franchisee will not fairly be compensated for the value of its goodwill.

1.3.5.3 Termination of a franchise contract

In practice, a franchise contract is usually a standardized and non-negotiable contract drafted by a franchisor.⁵³ Ordinarily, a franchisor prepares a franchise contract to reflect its interests. Thus, it is not uncommon that the franchisor reserves the right to terminate a franchise contract unilaterally. In some cases, a franchisor may hold the right to terminate a franchise agreement at any time without any cause.⁵⁴ Generally, a franchisor may terminate a franchise contract for justifiable reasons that a franchisee has to endure. For example, the franchisor may terminate a franchise contract to discontinue a relationship with franchisees whose substandard behaviors harm the entire franchise system.⁵⁵

In several instances, a franchisor may terminate a franchise contract opportunistically.⁵⁶ For instance, a franchisor may engage in 'churning' practices by terminating a franchise contract to appropriate the franchisee's lucrative outlet.⁵⁷ According to Benoliel and Buchan, the franchisor may terminate a franchise contract to sell a successful franchised unit to other franchisees for a higher price. Alternatively, the franchisor may terminate a franchise contract to operate a successful outlet itself.⁵⁸ In either case, the terminated

51 Lewis G Rudnick, 'Structuring a Franchise Relationship' (1980) 1 *Journal of the Forum Committee on Franchising* 9, 11.

52 Caroline B Fichter, Andrew M Malzahn, and Adam Matheson, 'Don't Tread on Me: A Defense of State Franchise Regulation' (2018) 38 *Franchise Law Journal* 23, 37.

53 Jenny Buchan, 'Consumer Protection for Franchisees of Failed Franchisors: Is There a Need for Statutory Intervention?' (2009) 9(2) *Queensland University of Technology Law and Justice Journal* 232, 234; Jenny Buchan and Rob Nicholls, 'The Challenges of Navigating the COVID-19 Pandemic for Australia's Franchise Sector' (2020) *Australian Business Law Review* 126, 127; Jenny Buchan, 'Franchisees as externalities of insolvent franchisors: a windfall gain for employees?' in Paul J Omar and Jennifer L L Gant (eds), *Research Handbook on Corporate Restructuring* (Edward Elgar 2021) 261.

54 Benjamin Klein, 'Transaction Cost Determinants of "Unfair" Contractual Arrangements' (1980) 70(2) *The American Economic Review* 356, 359; Blair and Lafontaine (n 35) 269.

55 Richard A Epstein, 'Unconscionability: A Critical Reappraisal' (1975) 18 *Journal of Law & Economics* 293, 315; Benjamin Klein, 'The economics of franchise contracts' (1995) 2 *Journal of Corporate Finance* 9, 18.

56 Emerson and Benoliel (n 19) 197.

57 Blair and Lafontaine (n 35) 271.

58 Benoliel and Buchan (n 33) 415-16.

franchisee will inevitably suffer financial damage, such as failing to redeem the value of its goodwill.⁵⁹ Additionally, the franchisor may terminate a franchise agreement to claim franchise fees and buy the franchisee's initial investment at a distress price.⁶⁰ Also, the franchisee's economic loss will unavoidably be realized.

1.3.6 Conclusions

An asymmetrical franchise relationship likely opens room for a franchisor to behave opportunistically toward a franchisee. This section shows that certain forms of franchisor opportunism may manifest themselves during the three stages of a franchise relationship, from the pre-contractual stage to the end of the relationship. Undoubtedly, a franchisor's opportunistic behaviors will victimize vulnerable franchisees and cause them economic loss or damage, which is hardly avoidable. In this respect, regulating franchisor opportunism by franchise-specific legislation may be needed to suppress franchisor opportunism in a franchise life cycle. The following section will set the main research goal of this doctoral thesis with regard to the legal regulation of franchisor opportunism.

1.4 RESEARCH OBJECTIVE

1.4.1 Introduction

The likelihood of franchisor opportunism in the three stages of a franchise relationship identified in the preceding section signifies the need to provide a vulnerable franchisee with legal protection against the franchisor's opportunistic conduct. In practice, there are several approaches to preventing a franchisor from utilizing its superior informational and economic power to behave opportunistically toward a franchisee in a franchise life cycle. Some countries may take a regulatory approach; that is to say, they may introduce

59 Hartlief and Baeck examined whether a franchisee can claim reimbursement for the value of goodwill on the basis of unjustified enrichment in seven European countries, namely, Belgium, Estonia, Germany, Ireland and the UK, Italy, and the Netherlands. In the comparative study, the authors concluded that the examined jurisdictions are reluctant to permit the claim for the loss of goodwill. Moreover, no selected country has specific legislation that allows the franchisee to be compensated for goodwill. *See* Ton Hartlief and Joke Baeck, 'Goodwill Compensation after Termination of a Franchise Contract: Comparative Perspective on Cour de Cassation 23 October 2012 (No. 11-21.978)' (2014) 22(6) *European Review of Private Law* 955, 957-58.

60 Klein (n 54) 359.

franchise-specific law regulating the franchisor's opportunistic conduct.⁶¹ This section will set the principal objective of the doctoral thesis that facilitates legal systems with an aim to take this regulatory approach in section 1.4.2. Section 1.4.3 will recapitulate the ultimate goal of this research study.

1.4.2 Formulation of private law rules under franchise-specific law

The main goal of this research study is to offer guidelines for formulating private law rules of franchise-specific law regulating franchisor opportunism in the three stages of a franchise life cycle. The following subsections 1.4.2.1 and 1.4.2.2 will elaborate on the terms 'franchise-specific law' and 'private law rules' for the purpose of this research study.

1.4.2.1 Franchise-specific law

This research study presupposes that franchise-specific law better protects a franchisee against franchisor opportunism because of two reasons.

First, this thesis believes that general contract law cannot satisfactorily protect a weaker franchisee. In legal literature, some legal scholars have claimed that a franchisee will not be able to protect itself under the system of contract law. For example, Buchan mentions that contract law is not an appropriate regulatory tool in franchising.⁶² That is, contract law relies on the principle of freedom of contract, which suggests that contracting parties will bargain to protect their own interests. Thus, it is not uncommon that a franchisor will draft a franchise contract to protect its own interests. Buchan also points out that the franchisor will not be interested in protecting the franchisee from the franchisor's damaging conduct.⁶³ In sum, contract law

61 One reason is that contract law, as a general legal framework governing a franchise relationship, may not protect a weaker franchisee appropriately. Some legal scholars have claimed that a franchisee cannot protect itself under the realm of contract law since contract law principles, such as contractual freedom, assume that the parties must bargain to protect their own interests. In reality, the franchisee hardly protects itself because it is inexperienced and has less bargaining power. Moreover, the franchisor will not be interested in protecting the franchisee from the franchisor's unfair conduct. See Tanya Woker, 'Franchising – The Need for legislation' (2005) 17 South African Mercantile Law Journal 49, 49-56; Buchan, *Franchisees as Consumers: Benchmarks, Perspectives and Consequences* (n 13) 79-84. Thus, some commentators have argued for the statutory protection of a franchisee under the realm of franchise-specific law because the franchisee may not protect itself. See Caroline B Fitchter, Andrew M Malzahn, and Adam Matheson, 'Don't Tread on Me: A Defense of State Franchise Regulation' (2018) 38(1) Franchise Law Journal 23, 34.

62 Buchan, 'Deconstructing the Franchise as a Legal Entity: Practice and Research in International Franchise Law' (n 11) 148, 151-52.

63 Buchan, *Franchisees as Consumers: Benchmarks, Perspectives and Consequences* (n 13) 69-72, 79.

will not allow an inexperienced franchisee with lesser bargaining power to protect itself against an exploitative franchisor.

Second, franchise-specific legislation is regulatory. Some commentators have argued for the legal protection of a franchisee under the realm of franchise-specific law.⁶⁴ According to Emerson and Benoliel, franchise law can correct a perceived inequality in bargaining power between a franchisor and a franchisee and protect franchisees against franchisor opportunism.⁶⁵ By its nature, franchise-specific law contains provisions establishing mandatory rules to provide a franchisee with *ex-ante* and *ex-post* protection. In the former case, franchise-specific law rules can take an action-based approach in requiring a franchisor to act affirmatively or negatively that will not jeopardize the franchisee's legitimate interests. In the latter case, franchise-specific law rules can adopt a sanction-based approach in offering a system of private law remedies that permit an aggrieved franchisee to remedy the actual and anticipated loss or damage arising from the franchisor's damaging conduct. Thus, this research study aims to facilitate the adoption of this regulatory intervention.

It should be noted that this doctoral thesis intends franchise-specific law to be 'comprehensive franchise law'. In this thesis, comprehensive franchise law will be referred to as statutory law containing a set of mandatory rules regulating franchisor opportunism in the whole franchise life cycle, from a pre-contractual to a contractual franchise relationship. Nevertheless, this thesis does not intend comprehensive franchise law to take any specific form. Accordingly, legal systems may propose franchise-specific law, as comprehensive franchise law, in various forms. For example, legal systems may introduce comprehensive franchise law as a piecemeal franchise statute or an administrative franchise regulation. Civil law jurisdictions may include in their civil code a special part of contract law governing a franchise contract. For example, the Netherlands has recently amended Book 7 of the Dutch Civil Code to contain a set of specific contract law provisions establishing rules regulating pre-contractual and contractual franchise relationships.⁶⁶

1.4.2.2 Private law rules

Comprehensive franchise law may contain provisions that offer private and public law rules regulating a franchise relationship. Nevertheless, this doctoral thesis will not deal with public law aspects of comprehensive franchise law. For instance, this thesis will not discuss problems related to registering a franchise business and filling documents, such as filling a disclosure document.

64 Fitchter, Malzahn, and Matheson (n 61) 34.

65 Robert W Emerson and Uri Benoliel, 'Can Franchisee Associations Serve as a Substitute for Franchisee Protection Laws?' (2013) 118(1) Penn State Law Review 99, 105.

66 Book 7, title 16, articles 911-922.

In other words, this research study will focus on suggesting the formation of private law rules as rules regulating the rights and duties of the parties to a contract.⁶⁷

The primary objective of the research study is to develop guidelines for formulating civil law rules regulating the franchisor's opportunistic conduct in a franchise relationship. Strictly speaking, this thesis intends to develop the rules that regulate the rights and duties of the parties to a franchise contract to ensure adequate legal protection of a franchisee. In order to create a complete picture of franchise regulation, this research study also aims to suggest the construction of a remedial system that will redress the franchisee's loss or damage in the case of violation of the franchise regulation under comprehensive franchise law. Nonetheless, this book has a limit in length; it is inevitable to study those two aspects of franchise regulation in detail. Thus, it should be mentioned that this research study will pay more attention to substantive law rules regulating the rights and obligations of the franchisor and the franchisee than the remedial system.

1.4.3 Conclusions

The ultimate goal of this doctoral thesis is practical; it aims to offer a source of inspiration for any legal systems that intend to introduce franchise-specific law to regulate a franchisor's opportunistic conduct to protect a weaker franchisee. Specifically speaking, this thesis will develop guidelines for formulating private law rules under comprehensive franchise law regulating the franchisor's opportunistic conduct in a franchise life cycle and private law remedies for the franchisor's violation of the rules. In this respect, a benchmark for comprehensive franchise law rules is the protection of the franchisee's legitimate interests against the franchisor's opportunistic conduct. Private law rules can be introduced to address several private law aspects of a franchise relationship. The following section will formulate an umbrella research question and sub-research questions to set an analytical framework for the research study that enables the achievement of the main research objective.

1.5 RESEARCH QUESTIONS

1.5.1 Introduction

This section will develop explorative research questions to form the backbone of the research study. These research questions will be divided into one over-

⁶⁷ John C P Goldberg, 'Pragmatism and Private Law' (2012) 125 Harvard Law Review 1640, 1640.

arching research question and sub-research questions. Based on the problems identified in section 1.3 and the main research goal set in section 1.4, this doctoral thesis supposes that comprehensive franchise law is introduced to regulate franchisor opportunism in the three stages of a franchise life cycle in order to protect a franchisee. Then, this thesis formulates an overarching research question: “Which franchise-specific law rules should be formulated to regulate the franchisor’s opportunistic conduct?” In responding to this central research question, this section will develop a series of ten sub-research questions to be answered in this thesis. Ten sub-research questions pertaining to the three stages of a franchise relationship will be formulated in sections 1.5.2, 1.5.3, and 1.5.4, respectively. Section 1.5.5 will conclude on the pivotal role of the formulated overarching research question and ten sub-research questions.

1.5.2 Sub-questions as regards a pre-contractual franchise relationship

Three sub-research questions pertinent to a pre-contractual stage of a franchise life cycle are formulated as follows.

How is a franchisor required to provide the prospective franchisee with material information about a franchise business before the conclusion of a franchise contract? What are the franchise-specific law rules that should be made to establish the franchisor’s pre-disclosure duty?

How is a franchisor required to ensure that pre-contractual information to be disclosed is current and candid? What are the franchise-specific law rules that should be made to constitute the franchisor’s duty of truthfulness?

Can an aggrieved franchisee seek private law remedies to compel the franchisor’s performance, claim monetary compensation, and cancel a franchise contract if a franchisor fails to comply with the franchise rules?

These three sub-research questions will be investigated in chapter three of the book.

1.5.3 Sub-questions as regards an ongoing franchise relationship

Three sub-research questions connected with an ongoing franchise relationship are formulated as follows.

How is a franchisor required to refrain from engaging in traditional and non-traditional encroachment in the vicinity of the franchisee’s marketing area? What are the franchise-specific law rules that should be made to regulate the franchisor encroachment?

How is a franchisor required to assist the franchisee in the opening and operation of a franchise business? What are the franchise-specific law rules that should be made to govern the franchisor's assistance?

Can an aggrieved franchisee seek private law remedies to compel the franchisor's performance, claim monetary compensation, and cancel a franchise contract if a franchisor fails to comply with the franchise rules?

These three sub-research questions will be investigated in chapter four of the book.

1.5.4 Sub-questions as regards an end of a franchise relationship

Four sub-research questions in relation to the end of a franchise relationship are formulated as follows.

How is a franchisor required not to withhold consent to a transfer by the franchisee unreasonably? What are the franchise-specific law rules that should be made to regulate the franchisor's withholding consent to the transfer?

How is a franchisor prevented from refusing to renew an expiring franchise contract for a definite period? What are the franchise-specific law rules that should be made to regulate the franchisor's non-renewal of a franchise contract?

How is a franchisor prevented from terminating a franchise contract for an indefinite and definite period without justifiable grounds? What are the franchise-specific law rules that should be made to regulate the franchisor's termination of a franchise contract?

Can an aggrieved franchisee seek private law remedies to compel the franchisor's performance, claim monetary compensation, and cancel a franchise contract if a franchisor fails to comply with the franchise rules? Can an aggrieved franchisee be reimbursed for the value of tangible and intangible assets upon the cessation of a franchise relationship, and, if it can, what are the assets whose value can be reimbursed?

These four sub-research questions will be investigated in chapter five of the book.

1.5.5 Conclusions

This section sets an overarching research question to be answered in this research study. This central question concerns franchise-specific law rules that should be formulated under comprehensive franchise law to regulate franchisor opportunism in the three stages of a franchise life cycle. Answering this central research question will not be successful unless the core of the research study is formed. Thus, this section also develops the accompanying ten sub-research

questions to form the basis for the research study. Before the developed research questions are investigated later in the book, it is crucial to design methodological aspects of the research study to ensure that all the research questions are answered in a scholarly-sound manner. This designing task will be undertaken in the following section.

1.6 RESEARCH DESIGNS

1.6.1 Introduction

This section is devoted to selecting a research methodology and a research method to be employed in this research study.⁶⁸ The proper selection of the research methodology and method will ensure that this doctoral thesis answers the research questions developed in the preceding section and formulates thesis proposals to achieve the research objective. In terms of methodology, this research study will take the position of a legal doctrinal approach. Concerning the research method, this research will employ a comparative law method to examine the franchise legal framework of the DCFR, the USA, and Australia regulating franchisor opportunism in the three stages of a franchise life cycle. This section will elaborate on a choice of legal doctrinal research and a comparative law method in sections 1.6.2 and 1.6.3, respectively. Section 1.6.4 will conclude on the central theme of this research study.

1.6.2 Doctrinal legal approach as a research methodology

As mentioned in section 1.4, this research study will propose guidelines for formulating private law rules of franchise-specific law regulating franchisor opportunism in the three stages of a franchise life cycle. Thus, it is inevitable that this research study examines 'law' as a normative framework regulating persons' conduct. With this reason in mind, a proper research methodology is normative or doctrinal legal research since this methodology involves the systematic description of legal materials.⁶⁹ This thesis believes that a descript-

68 A research methodology and a research method will be addressed separately because this doctoral thesis perceives that the research methodology and research method differ in terms of terminology. According to Mills, a research methodology is understood as a researcher's position concerning a research study. In contrast, a research method is defined as a strategy that the researcher employs to answer the research questions. See Jane Mills, 'Chapter 3: Methodology and Methods' in Jane Mills and Melanie Birks, *Qualitative Methodology: A Practical Guide* (SAGE Publications 2014) 32.

69 Jan M Smits, 'What Is Legal Doctrine?: On The Aims and Methods of Legal-Dogmatic Research' in Rob van Gestel, Hans-W Micklitz, and Edward L Rubin (eds), *Rethinking Legal Scholarship: A Transatlantic Dialogue* (Cambridge University Press 2017) 213-21.

ive legal approach will help answer the overarching research question and ten sub-research questions from a legal standpoint to formulate guidelines for enacting comprehensive franchise law rules regulating the franchisor's opportunistic conduct.

This research study will employ doctrinal legal research to study the extent to which the DCFR, the USA, and Australia provide the franchise legal framework to regulate franchisor opportunism in the three stages of a franchise relationship. Apparently, the franchise legal framework of the chosen legal systems will be the object of the study in this thesis. In this respect, it would be wise to explain the meaning of the expression 'franchise legal framework' that is understood in this research study.

For this research study, the franchise legal framework refers to the following two types of legal framework that this thesis considers most relevant to the regulation of franchisor opportunism in a franchise relationship.

The first type of legal framework is the rules of private law. This research study will examine well-established legal rules that lay down normative standards or principles regulating a franchise relationship. It should be noted that these legal rules can be established by franchise-specific law and contract law.

The second type of legal framework is the terms of a franchise contract. This research study perceives the franchise legal framework in the broadest sense to include agreements between the franchisor and the franchisee under a franchise contract. The reason for taking this view is that a franchise contract is a principal instrument outlining a franchise relationship.⁷⁰ In many cases, the terms of a franchise contract articulate minimum requirements that could protect a franchisee against a franchisor's opportunistic practices.

1.6.3 Comparative law as a research method

This doctoral thesis will conduct doctrinal legal research by employing a comparative law method. In comparative law research, a comparison of multiple legal systems is said to be a process of the study. According to Örüçü, the comparison method includes juxtaposing, contrasting, and comparing legal systems.⁷¹ Because of this particular trait, a comparative law method will help extract widely-adopted legal solutions to specific problems. This benefit of a comparative law method will enhance the possibility of widespread adoption of research proposals among legal systems around the globe. Thus,

70 Jenny Buchan, 'Ex ante information and ex post reality for franchisees: The case of franchisor failure' (2008) 36 *Australian Business Law Review* 407, 422; Atwell and Buchan (n 22) 187.

71 Esin Örüçü, 'Methodology of comparative law' in Jan M Smits (ed), *Elgar Encyclopedia of Comparative Law* (2nd edn, Edward Elgar 2012) 573.

this thesis believes that a comparative law method fits the purpose of this research study.

However, a challenging question arises: what legal systems are chosen to compare? For specificity's sake, this doctoral thesis aims to conduct multilateral comparative law research in the sense that more than two legal systems will be chosen to compare. Furthermore, this research study will utilize a multilateral comparative law method to juxtapose the franchise legal framework of the DCFR, the USA, and Australia. This research study aims to extract similarities and differences in the legal approaches adopted by the three legal systems to regulate the franchisor's opportunistic conduct in the three stages of a franchise life cycle. The findings from the comparative examinations will be discussed to propose guidelines for formulating private law rules regulating franchisor opportunism in a franchise life cycle. The following subsections 1.6.3.1 and 1.6.3.2 will elaborate on the selection of the three legal systems and the information collection method to be employed in this comparative law study.

1.6.3.1 Selection of the three legal systems

As mentioned in the preceding section, this doctoral thesis chooses the DCFR, the USA, and Australia as comparison units. These legal systems are chosen because of the comprehensiveness of their franchise legal framework; the DCFR, the USA, and Australia offer the franchise legal framework that regulates a franchise relationship from its birth to its end.⁷² This comprehensiveness will ensure that this research study satisfactorily answers the central question and sub-research questions. Moreover, the comprehensiveness establishes *tertium comparationis* or the common denominator, making a comparative legal analysis in this research study possible. Metaphorically speaking, comparing the franchise legal framework of the DCFR, which is a mere academic text, with those of the USA and Australia will not lead to a comparison between apples and oranges.⁷³

72 Employing the comprehensiveness of the franchise legal framework as a criterion means the choice of legal systems to compare is not based on the Roman root of legal systems. In other words, choosing the DCFR, the USA, and Australia for the research study is not based on the division of civil law and common law legal systems.

73 Nowadays, contemporary comparatists have not confined themselves to comparatively examining the positive laws of nations. In some comparative law research, the researcher may select model law to compare with other national legal systems. For example, in Díaz's doctoral research, the Principles of European Law on Commercial Agency, Franchise and Distribution Contracts (PEL CAFDC) was chosen to compare with French and Spanish legal systems. See Odavia Bueno Díaz, *Franchising in European Contract Law: A comparison between the main obligations of the contracting parties in the Principles of European Law on Commercial Agency, Franchise and Distribution Contracts (PEL CAFDC), French and Spanish law* (seller: european law publisher 2008).

As can be seen, the franchise legal framework of the DCFR, the USA, and Australia is the object of this research study. In this respect, it would be wise to identify main sources of the franchise legal framework of the chosen legal systems. The identification of the legal sources will be made in the following three italicized headings.

– *The Draft Common Frame of Reference (DCFR)*

This doctoral thesis takes the Draft Common Frame of Reference (DCFR) to represent the European legal framework, which is the first comparison unit. In Europe, franchises are claimed to be flourishing businesses that significantly contribute to the GDP of many European countries.⁷⁴ Currently, the European Franchise Association's website has estimated over 14,900 franchise systems operating across the continent.⁷⁵ In this respect, studying the European legal framework regulating franchise relationships would be appealing for this thesis. Unfortunately, European countries have no uniformity in regulating a franchise relationship. In other words, the legal framework regulating a franchise relationship varies from country to country. Some countries, such as Italy, France, Spain, Belgium, and Lithuania, have enacted franchise-specific legislation regulating some aspects of a franchise relationship. Other countries, such as Germany and the UK, utilize general contract law rules to govern a franchise relationship as a contractual relationship. Thus, it would not be viable for this research study to find a single national legal framework that represents the European system in regulating a franchise relationship.

Because of the restraint mentioned above, this research study finds that the DCFR is a perfect choice for representing a European perspective on regulating a franchise relationship. According to the drafters of the DCFR, this instrument is drafted by European scholars. Besides, model rules in the DCFR are derived mainly from thirty legal systems in Europe, as well as the overarching European law.⁷⁶ More importantly, some commentators claim that the DCFR is the first complete set of systematized rules of franchise contracts in Europe.⁷⁷ This thesis agrees with this acclamation because the DCFR makes a franchise contract one of the specific contracts.⁷⁸ The DCFR provides model

74 Mark Abell, *The Law and Regulation of Franchising in the EU* (Edward Elgar Publishing 2013) 1-2.

75 <https://eff-franchise.com/>

76 Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.1, Oxford University Press 2010) 1.

77 Christian von Bar, 'The Draft Common Frame of Reference: Scope and Purpose,' in Vincent Sagar, Matthias Storme and Evelyne Terryn (eds), *The Draft Common Frame of Reference: national and comparative perspectives* (Intersentia 2012) 5; Tajti (n 12) 249-50.

78 It should be noted that the drafters present the DCFR in a civil code-like instrument that covers broad subjects, including specific contracts. See Lucinda Miller, *The Emergence of EU Contract Law: Exploring Europeanization* (Oxford University Press 2011) 132.

rules in Book IV regulating both pre-contractual and contractual franchise relationships.⁷⁹ Unlike other model franchise laws, the DCFR offers a comprehensive franchise legal framework regulating a franchise relationship.⁸⁰ Therefore, it would not be exaggerated to say that the DCFR is the most suitable choice that could represent the European legal framework regulating a franchise relationship.

The selection of the DCFR as a comparison unit may be questioned in the following two aspects.

First, one may argue that this academic text lacks a practical dimension because European countries have not adopted the DCFR as existing law yet. Despite this, the DCFR by no means loses any connection to the real legal world. First, it should be borne in mind that model rules of the DCFR derive from the extensive comparative law studies of existing laws in Europe.⁸¹ Furthermore, some provisions of the DCFR are cited by court decisions. For instance, in Scotland, Lord Malcolm in *Phil Wills v Strategic Procurement (UK) Limited* referred to II. – 7:201(1) of the DCFR when discussing an error issue in contract law.⁸² This Scottish case law demonstrates that the DCFR is not a mere academic text and can really be utilized in courts.

Second, one may argue that the DCFR is incomplete as it does not offer model rules governing some specific areas of law. In remedying this incompleteness, this thesis will examine the rules of other legal frameworks as appurtenances (*cum annexis*). For example, the DCFR does not contain model competition law rules, which are customarily relevant in franchising. In this respect, this thesis will examine the rules of the Treaty on the Functioning of the European Union (TFEU) when it comes to the effects of competition law rules on competition issues in a franchise relationship. This gap-filling solution is not unusual in the view of the drafters of the DCFR since they acknowledge that European competition law rules may affect certain provisions in a franchise agreement.⁸³ Thus, in some parts of the comparative examination, this research study will explore the DCFR *cum annexis*.

79 The DCFR also offers general contract law rules in Book I, II, and III that will be applied to a franchise contract in the absence of special rules in Book IV. These rules primarily deal with private law remedies for a non-performance of an obligation under a franchise agreement.

80 Compared to the UNIDROIT Model Franchise Disclosure Law 2002, this model law contains ten articles focusing on the franchisor's pre-disclosure duty in a franchise relationship. In other words, the instrument does not deal with contractual issues in a franchise relationship, such as franchisor encroachment and franchisor assistance. In this respect, the UNIDROIT model law is a less interesting choice for this thesis because it does not offer comprehensive franchise law rules like the DCFR.

81 Bar and Clive (n 76) 1.

82 *Wills v Strategic Procurement (UK) Ltd*, 2016 SC 367 [10].

83 Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.3, Oxford University Press 2010) 2384.

Since this doctoral thesis will examine the terms of a franchise contract, one may question where to find contract drafting practices when examining the DCFR in this thesis. For the sake of specificity, this research study will utilize the ICC Model International Franchising Contract (the ICC Model Contract) to exemplify a franchise contract's terms representing a European viewpoint. According to the authors of the ICC Model Contract, this publication offers the most commonly encountered clauses in franchise contracts. Those clauses are intended to be adopted domestically and internationally.⁸⁴ In addition, the ICC Model Contract could well represent a European perspective on drafting a franchise contract because of several references to regional and domestic laws of the European Union. For example, the authors of the ICC Model Contract refer to European competition law rules when it comes to antitrust issues. Furthermore, the authors mention German and Austrian laws to demonstrate how the national laws protect a franchisee in a pre-contractual stage through general contract law rules.⁸⁵

– *The United States of America (USA)*⁸⁶

The United States of America (USA) is chosen as the second comparison unit because this legal system has a long history of regulating a franchise.⁸⁷ Nowadays, the USA has regulated franchise relationships through several types of franchise-specific legislation. The US legal system regulates a pre-contractual franchise relationship through franchise sales or disclosure laws. At the national level, the Federal Trade Commission's Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity (FTC Rule) has been legislated to regulate pre-sale disclosures.⁸⁸ At the state level, sixteen US states (franchise sale states) have enacted franchise sale law, which is not

84 International Chamber of Commerce, *ICC Model International Franchising Contract* (ICC Publications 2011) 3-4.

85 Ibid 13-15.

86 In terms of statistics, in 2021, around 774,965 local franchise businesses were operating in the USA. These businesses created around 8.2 million jobs and generated 787.7 billion US dollars for the US economy. In 2022, it is expected that the number of franchise businesses will increase by 2.2% to 792,014 establishments. These stats derive from the report '2022 Franchising Economic Outlook' prepared by FRANData for the International Franchise Association. This report can be accessed at <<https://bit.ly/3l56qh6>>.

87 The USA is said to be the home of modern franchising. A franchise, as a marketing model, is claimed to have been developed in this country. Furthermore, the USA is said to be the first country that introduces franchise-specific legislation to regulate franchise relationships. See Killion (n 9) 8-19; John R F Baer and Susan Grueneberg, 'United States' in Andrew P Loewinger and Michael K Lindsey (eds), *International Franchise Sale Laws* (2nd edn, American Bar Association 2016) 502.

88 The electronic version of the FTC Rule can be found on the Federal Trade Commission's website at <<https://bit.ly/3coWutM>>.

preempted by the FTC Rule, to regulate franchise sales in their jurisdictions.⁸⁹ In the case of concurrence, this thesis will primarily examine the FTC Rule since it is a primary legislative instrument regulating pre-sale disclosures throughout the country. However, this research study will highlight aspects of the state disclosure laws in case of distinct deviations from the FTC Rule.

The USA also regulates contractual franchise relationships through general franchise relationship laws. Nowadays, there is no federal franchise relationship law. According to Emerson and Benoliel, several federal franchise relationship bills were introduced in the past but all the bills were rejected.⁹⁰ Consequently, franchise relationship legislation is a matter of state law.⁹¹ Currently, eighteen US states (relationship states) have enacted franchise relationship statutes to regulate several matters with regard to ongoing franchise relationships.⁹² In this research study, the rules of state franchise relationship law will primarily be examined. In the rest of the country, contract law will be utilized to govern franchise relationships. However, contract law rules are exclusively state law doctrines that may vary from jurisdiction to jurisdiction.⁹³ Thus, this study will not examine state contract law doctrines thoroughly. Instead, this study will focus on examining contract law rules utilized

89 Those states are California, Florida, Hawaii, Illinois, Indiana, Maryland, Michigan, Minnesota, New York, North Dakota, Oregon, Rhode Island, South Dakota, Virginia, Washington, and Wisconsin. It should be noted that some other states have their business opportunities law, which may apply to pre-contractual franchise relationships. See *Peltier v Spaghetti Tree, Inc.*, 451 NEn2d 1219, 1221, 6 Ohio St 3d 194, 196 (Ohio, 1983). For example, Alaska has the sale of business opportunities statute that requires the disclosure of pre-contractual information. See AK ST § 45.66.080. Arizona has trade and commerce law requiring the pre-sale disclosure. See AZ ST § 44-1276.01. Nevertheless, this doctoral thesis specifically focuses on the state franchise disclosure statutes.

90 Emerson and Benoliel (n 65) 106-07.

91 It should be noted that a new Bill cited as 'Fair Franchise Act of 2017' has presently been introduced and sponsored by Keith Ellison, the US Representative, since 2017. This Act is to be enacted as federal franchise legislation establishing minimum standards of fair conduct in franchise sales and franchise business relationships. One of the declared purposes of the Act is to protect franchisees against unfair treatment by franchisors, who inherently have superior economic power and bargaining power in the negotiation of the terms and conditions of the franchise relationship. If Congress passes the Bill, pre-contractual and contractual franchise relationships will uniformly be regulated by the Act throughout the USA. The text of the Bill can be retrieved at <<https://bit.ly/3i5xNE0>>.

92 Those relationship states are Arkansas, California, Connecticut, Delaware, Hawaii, Illinois, Indiana, Iowa, Michigan, Minnesota, Mississippi, Missouri, Nebraska, New Jersey, Rhode Island, Virginia, Washington, and Wisconsin. Besides the US states, Virgin Island, an unincorporated US territory, has its franchised businesses law, which governs part of an ongoing franchise relationship. See 12A V.I.C. § 130-139.

93 Alexander M Meiklejohn, 'Chapter 13: Common Law Doctrine' in Alexander M Meiklejohn (ed), *Franchising: Cases, Materials, & Problems* (American Bar Association 2013) 663.

by courts to protect franchisees against franchisor opportunism in a franchise relationship.⁹⁴

Apart from the rules of law, the USA offers contracting practices that enable the collection of a franchise contract's terms to illustrate how a franchise agreement deals with franchisor opportunism. In some states, such as California, samples of a real-life franchise agreement can be searched through the website of California's Department of Financial Protection and Innovation.⁹⁵ However, it would be a burdensome task to collect all samples of a franchise contract to examine its terms. For the sake of exemplification, some sources of the terms of a franchise contract will be referred to in this research study. For example, this thesis will take samples of contractual clauses offered by some national franchise associations, including the American Association of Franchisees and Dealers (AAFD) and the Coalition of Franchisee Associations (CFA). Furthermore, this research study will resort to the book entitled 'the Annotated Franchise Agreement' published by the American Bar Association (ABA) because it offers terms and conditions that are said to be common among typical franchise agreements in the USA.⁹⁶

– *Australia*

Australia is chosen as the third comparison unit. For a general view, franchising set foot in Australia around the 1960s.⁹⁷ Now, it is said to be a flourishing business that forms an essential part of the nation's economy.⁹⁸ According to Buchan, the franchise sector in the country is big, diverse, and complicated.⁹⁹ Accordingly, Australia has a specific legal environment for this business sector; that is to say, it regulates a franchise through several Common-

94 For example, attention will be paid to the implied duty of good faith and fair dealing, which is said to be an important contract law doctrine applicable to franchising. See W Michael Garner, 'Good-faith dealing—In general, 2 Franch & Distr Law & Prac, Westlaw, (November 2019) at § 8:25.

95 The website can be accessed at <<https://docqnet.dfpi.ca.gov/search/>>.

96 Nina Greene, Dawn Newton, and Kerry Olson (eds), *The Annotated Franchise Agreement* (2nd edn, American Bar Association 2021) at xxi-xxvi.

97 Jenny Buchan, 'Australia's Franchising Code of Conduct Review – A Continuation Down the Path of Jamming a Square Peg into a Round Hole?' (2019) 47 *Australian Business Law Review* 393, 393.

98 Kanchana Kariyawasam and Lisa Samarkovski, 'Legal Issues in Franchising in Australia: Is the Current Regulatory Environment for the Franchise Sectoradequate' (2012) 9 *Macquarie Journal of Business Law* 179, 179-181; Michael T Schaper, 'Franchising Regulation in Australia: Recent Trends and Current Issues' (2013) 11(1) *International Journal of Franchising Law* 3, 4.

99 Jenny Buchan, 'The 2018 Review of the Franchising Code of Conduct: Epicentre of a Year of Scrutiny for Australian Franchising' (2019) 47 *Australian Business Law Review* 101, 102.

wealth statutes, including franchise-specific legislation.¹⁰⁰ Furthermore, it is claimed that Australia well regulates franchising businesses.¹⁰¹ The Australian legal system is, therefore, an enticing legal system to compare in this research study.

The principal legislation regulating a franchise relationship is the mandatory industry code established under the Competition and Consumer Act 2010 (CCA), known as the Franchising Code of Conduct (the Code).¹⁰² This Australian Code is attractive because of two reasons. First, the Code is a legislative instrument that systematically and comprehensively regulates the whole life of a franchise relationship, from the initial phase of contracting, the operation of a franchise agreement, to the termination of the agreement.¹⁰³ Second, the Code is one of the most improved franchise-specific laws in the world. This assumption is based on the fact that Australia regularly reviews the effects of the Code on franchise industries.¹⁰⁴ Besides reviewing the Code's effectiveness, Australia has carried out a series of amendments to the Code since its inception so that the Code is an improved version.¹⁰⁵ Therefore, the Code will be the primary object of the study.

This research study will also explore other legal frameworks regulating a franchise relationship.

First, this research study will examine the rules of the CCA as the Code is incomplete; that is to say, the Code does not contain provisions offering remedial rules for any contravention of the Code's provisions. In this case, this research study will have to find applicable rules from other sources. Since the Code is a mandatory industry code enacted under the CCA, any violation of the Code will permit an aggrieved party to resort to the remedies made

100 Robert W Emerson, 'Directing the Disjointed: A Call to Harmonize EU Franchise Law' (2014) 12 *International Journal of Franchising Law* 41, 41; Buchan, *ibid* 102; Stephen Giles, *Annotated Franchising Code of Conduct* (2nd edn, LexisNexis Butterworths 2021) 6.

101 Buchan, 'Ex ante information and ex post reality for franchisees: The case of franchisor failure' (n 70) 407.

102 The Competition and Consumer (Industry Codes- Franchising) Regulation 2014.

103 Schaper (n 98) 6; Natalie Sears, 'Australia's Updated Franchise Code of Conduct: Does an Express Obligation of Good Faith Benefit the Franchisor and Franchisee' (2014) 20 *Law and Business Review of the Americas* 121, 121.

104 The latest review of the Code was done by the Parliamentary Joint Committee on Corporations and Financial Services. In 2019, the Committee inquired into the operation and effectiveness of the Code and published the report to offer recommendations for amending the Code. The electronic version of the report can be downloaded at <<https://bit.ly/2SadgDD>>.

105 For example, Australia has recently amended the Code through Regulation 2021 – the Competition and Consumer (Industrial Codes- Franchising) Amendment (Fairness in Franchising) Regulation 2021. A list of all amendments to the Code can be found at <<https://www.legislation.gov.au/Series/F2014L01472>>

available under that statutory law.¹⁰⁶ Thus, the CCA will also be studied in this thesis.

Second, this research study will examine general contract law rules because contract law is claimed to be one of the legal frameworks applying to a franchise relationship.¹⁰⁷ In Australia, common law, as the body of judge-made law, including equity and admiralty, is the principal source of Australian contract law.¹⁰⁸ However, Australia is a federal country.¹⁰⁹ Thus, it is claimed that there can be different approaches to contract law issues among the Australian states and territories.¹¹⁰ Despite the divergence, this thesis will focus on widely-accepted doctrines or principles in contract law pointed out by some authoritative contract law textbooks.

This research study will also collect a franchise contract's terms to examine how the terms regulate franchisor opportunism. In this thesis, the collection of the terms of a franchise agreement will be selective since it is not feasible to acquire all franchise contracts in the country for examination. In this regard, this research study will collect examples of a franchise contract's terms from accessible sources, including Australian courts' decisions that mention the terms in a franchise agreement under dispute, as well as the Precedent to Franchise agreement (Precedent) that offers model basic franchise agreements.¹¹¹ This research study will also examine guidelines for drafting a franchise contract offered by the Franchise Council of Australia (FCA) to see recommended agreements under the contract.

Other jurisdictions may offer a comprehensive franchise legal framework as the selected legal systems do. In 2012, Sotos pointed out that some jurisdictions, such as Canada, South Africa, South Korea, Malaysia, and Russia, also offer comprehensive franchise regulatory regimes governing franchise relationships.¹¹² Presently, the number of jurisdictions could be multiplied. For example, Thailand has regulated parts of a franchise relationship by the Notification of the Trade Competition Commission prescribed by virtue of

106 Penny Ward, 'Australia' in Andrew P Loewinger and Michael K Lindsey (eds), *International Franchise Sales Laws* (American Bar Association 2016) 4.

107 Tony D'Aloisio, 'Franchising in Australia' (1989) 58 *Antitrust Law Journal* 949, 953.

108 Mark Leeming, 'Theories and Principles Underlying the Development of the Common Law – The Statutory Elephant in the Room' (2013) 36 *University of New South Wales Law Journal* 1002, 1004.

109 It remains debatable whether common law in Australia is primarily state law or federal law. See Leslie Zines, 'The Common Law in Australia: Its Nature and Constitutional Significance' (2004) 32 *Federal Law Review* 337, 337-56; Liam Boyle, 'An Australian August Corpus: Why There Is Only One Common Law in Australia' (2015) 27 *Bond Law Review* 27, 27-56.

110 Dan Svantesson, 'Codifying Australia's Contract Law – Time for a Stocktake in the Common Law Factory' (2008) 20(2) *Bond Law Review* 1, 9.

111 The Precedent is prepared by Perrott, Churley, and Giles and updated by Carkeet and Mitchell. A copy of the Precedent is in the author's storage.

112 John Sotos, 'Recent Trends in Franchise Relationship Laws' (2012) 10(1) *International Journal of Franchising Law* 3, 7.

the Trade Competition Act, B.E. 2560 (2017) since 2019. In this respect, there may be a question of why those jurisdictions are not selected for examination. There are two reasons for the choice of the three legal systems as follows. First, this doctoral dissertation does not intend to conduct comparative law research at a global scale, meaning the franchise legal framework of all legal systems will be taken into account. Instead, it aims to limit the number of legal systems to compare to three legal systems to focus on the actual comparison.¹¹³ Second, as can be seen, the volume of franchise practices in Europe, the USA, and Australia is said to be enormous. The immensity of franchise businesses in these continents would ensure an abundance of cases and legal instruments for the research study.¹¹⁴ In other words, the DCFR, the USA, and Australia offer an example of how to construct comprehensive franchise law rules that other jurisdictions will follow.

1.6.3.2 Documentation as an information collection method

This doctoral thesis is a documentary research study. In this thesis, information about the legal framework of the DCFR, the USA, and Australia, will be collected through documentation. This research study selects documentation as an information collection method for two reasons.

First, a documentary method suits the sources of information. In general, information about the franchise legal framework of the chosen legal systems, such as legal rules, illustrative cases, and text commentaries, will primarily be documentary evidence. In other words, these sources are usually documented. Thus, it is inevitable that this thesis collects documents for the study.

The second reason is that a documentary method removes geographical constraints when collecting the information. As can be seen, this research study chooses to examine three legal systems from different regions. Collecting information through documentation would help reduce traveling costs of the compilation of information at all places in the world. In this case, a documentation method will allow conducting the research study from home, university offices, and libraries.¹¹⁵

In conducting this research study, the information about the franchise legal framework of the DCFR, the USA, and Australia will be collected from physical and online documents. Most physical documents will be taken from books and academic papers, such as articles in academic journals. For example, this research study will resort to the text of the DCFR and its commentaries through

113 Mathias Siems, *Comparative Law* (3rd edn, Cambridge University Press 2022) 17.

114 This assumption does not imply that other countries have a small scale of franchise practices or are not considered worth studying. In any case, the choice of legal systems in this doctoral research is the choice of appropriateness.

115 This freedom is claimed to be one of the advantages of documentary research. See Malcolm Tight, *Documentary Research in the Social Sciences* (SAGE Publications Ltd 2019) 14.

a compilation of the books – Principles, Definitions and Model Rules of European Private Law – edited by Christian von Bar and Eric Clive. These printed materials will be gathered by self-acquisition and through library services. This thesis will collect electronic documents from various reliable legal websites and databases, including Westlaw, HeinOnline, and LexisNexis databases. Using these e-databases will enable the collection of the text of statutes and case law originated from the US and Australian legal systems.

1.6.4 Conclusions

This section affirms that this doctoral thesis will answer the overarching research question and its ten sub-research questions in a scholarly manner. This thesis will conduct the study employing a doctrinal legal approach with a functional comparative law method. This research study will examine and juxtapose the franchise legal framework of the DCFR, the USA, and Australia collected through documentation to extract common and distinct legal solutions to the questions. These extracted legal solutions will be discussed in chapters of the book to formulate guidelines for enacting private law rules regulating franchisor opportunism in the three stages of a franchise life cycle.

1.7 STRUCTURE OF THE BOOK

This doctoral thesis consists of six chapters. Apart from this introductory chapter, chapter two will explore the definition and essential elements of a franchise under the franchise legal framework of the DCFR, the USA, and Australia. This second chapter will also formulate the definition of a franchise for comprehensive franchise law. The reason for incorporating this chapter into the book is practical. In regulating a franchise, a franchise relationship should be defined to exclude other similar relationships. In other words, defining a franchise will help identify a legal relationship that franchise-specific law rules aim to regulate.

Chapter three will answer the three sub-research questions pertinent to a pre-contractual franchise relationship.¹¹⁶ This third chapter will examine the franchise legal framework of the DCFR, the USA, and Australia to explore the extent to which the franchise legal framework of the selected legal systems requires a franchisor to provide a prospective franchisee with essential information about a franchisor and a franchise system before the conclusion of a franchise contract. This chapter will also examine the extent to which the franchise legal framework of the chosen legal systems requires the franchisor to ensure that the pre-contractual information is current, complete, and accu-

¹¹⁶ See section 1.5.2.

rate. The findings will be discussed to propose guidelines for formulating comprehensive franchise law rules regulating the franchisor's pre-contractual information duties. Additionally, chapter three will examine the private law remedies for a breach of the duties to see if an aggrieved franchisee can enforce the franchisor's performance, claim damages, and cancel a franchise contract. The findings will be discussed to suggest the establishment of the remedial system under comprehensive franchise law.

Chapter four will answer the three sub-research questions connected with an ongoing franchise relationship.¹¹⁷ This fourth chapter will describe and juxtapose the franchise legal framework of the DCFR, the USA, and Australia regulating franchisor encroachment and franchisor assistance to examine how the selected legal systems' franchise legal framework requires the franchisor to refrain from engaging in traditional and non-traditional encroachment in the vicinity of the franchisee's marketing area and assist the franchisee in opening and operating a franchised business. The findings will be discussed to propose guidelines for formulating comprehensive franchise law rules regulating the franchisor's duty not to encroach and the duty to assist. This fourth chapter will also examine if an aggrieved franchisee can seek private law remedies to enforce the franchisor's performance, claim damages, and cancel a franchise contract to advise the construction of the remedial regime.

Chapter five will answer the four sub-research questions pertinent to the end of a franchise relationship.¹¹⁸ This fifth chapter will examine the franchise legal framework of the DCFR, the USA, and Australia to explore how the franchise legal frameworks prevent the franchisor from withholding consent to a transfer, refusing to renew a definite franchise contract, and terminating a franchise contract without justifiable grounds. The findings will be discussed to propose guidelines for formulating comprehensive franchise law rules regulating the franchisor's conduct with regard to transfer, non-renewal, and termination of a franchise contract. Chapter five will also explore if an aggrieved franchisee can enforce the franchisor's performance, claim damages, and cancel a franchise contract and if the franchisee can seek special remedies to reimburse for the value of certain assets upon the cessation of a franchise relationship. The findings will be discussed to suggest the establishment of the remedial system under comprehensive franchise law.

Chapter six is the conclusion chapter. This sixth chapter will formulate the thesis proposal by summarizing answers to an overarching research question and its ten sub-research questions. In this chapter, a summary of the answers to the research questions will be given by way of recapitulating the research findings and practical recommendations with the proposed provisions of comprehensive franchise law regulating franchisor opportunism in a franchise life cycle made in chapters two, three, four, and five. Caveats regarding

¹¹⁷ See section 1.5.3.

¹¹⁸ See section 1.5.4.

the recommendations and the proposed provisions will also be mentioned to remind legal systems of limitations when implementing the thesis proposal in reality. In the end, this chapter will offer model provisions of comprehensive franchise law based on the thesis's recommendations and highlight a specific issue for future research on the regulation of franchisor opportunism in a franchise relationship.

2 | Definition and essential elements of a franchise

2.1 INTRODUCTION

There are various models for a producer and its partners to construct a marketing relationship. A franchise seems to be a popular model utilized to create a distribution relationship in the business world. From a legal perspective, many legal systems allow the formation of this commercial relationship in light of the contractual freedom recognized by general contract law. Some legal systems may regulate the construction of a franchise relationship through franchise-specific law. In this respect, it will practically be important to distinguish the elements of a franchise that constitute a franchise relationship. Demonstrating a franchise's components is vital to protect a weaker franchisee because courts will not utilize protective franchise rules unless a legal relationship is regarded as a franchise relationship under the franchise regulation.¹ Thus, the definition of a franchise should be examined at the beginning of the research study.

Chapter two will explore how the franchise legal framework of the Draft Common Frame of Reference (DCFR), the United States of America (USA), and Australia define a franchise. Strictly speaking, this second chapter will examine how the franchise legal framework of the chosen legal systems particularizes the essential elements of a franchise constituting a franchise relationship for the purpose of regulation. The descriptive examination of a franchise definition under the three legal systems will be conducted in sections 2.2, 2.3, and 2.4, respectively. After the examination, section 2.5 will compare and discuss the definition and the essential elements of a franchise to suggest characterizing a franchise under comprehensive franchise law. Section 2.6 will conclude on the findings of chapter two.

¹ The following US court's decision can exemplify this statement. See *Implement Service Inc v Tecumseh Products Co* 726 F Supp 1171 (SD Ind, 1989) 1179–180.

2.2 THE DRAFT COMMON FRAME OF REFERENCE (DCFR)

2.2.1 Introduction

Under the DCFR, a franchise relationship is created by a franchise contract. The DCFR treats a franchise contract as a marketing contract, regulated by provisions in Part E of Book IV. In particular, this Part devotes chapter 4, from IV.E. – 4:101 to IV.E. – 4:304, to dealing with a franchise relationship. In this fourth chapter, IV.E. – 4:101 defines a franchise contract. According to IV.E. – 4:101, a franchise contract is considered a specific contract with the following three elements: (1) a grant of the right to conduct a franchise business, (2) a grant of the right to use the business package, and (3) the payment of remuneration.² This section will examine these four core elements in sections 2.2.2, 2.2.3, 2.2.4, and 2.2.5, respectively. Section 2.2.6 will conclude on the principal characteristics of a franchise contract under the DCFR.

2.2.2 Contract

As mentioned in the introduction, a franchise is a legal relationship created by a contract.³ In this respect, a franchise must be created by an agreement intended to give rise to a binding legal relationship or to have some other legal effect.⁴ For the sake of categorization, a franchise contract is a two-party contract concluded by a franchisor and a franchisee. However, IV.E. – 4:101 does not define the expressions ‘franchisor’ and ‘franchisee’. Despite the lack of a definition, it could be inferred from the text of IV.E. – 4:101 that the franchisor is a party who grants the other party – the franchisee – the right to conduct a franchise business and the right to use the franchisor’s intellectual property rights, know-how, and business method. In this case, the franchisee is a party who is entitled to the grant of the rights and has an obligation to pay remuneration to the franchisor.

In terms of formality, IV.E. – 4:101 imposes no formal requirement for concluding a franchise contract. Thus, the franchisor and the franchisee are

2 IV.E. – 4:101 states as follows: ‘[T]his Chapter applies to contracts under which one party (the franchisor) grants the other party (the franchisee), in exchange for remuneration, the right to conduct a business (franchise business) within the franchisor’s network for the purposes of supplying certain products on the franchisee’s behalf and in the franchisee’s name, and under which the franchisee has the right and obligation to use the franchisor’s tradename or trademark or other intellectual property rights, know-how and business method.’

3 According to the drafters of the DCFR, a franchise contract is a contract that has the economic function of establishing and regulating a marketing relationship. See Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.3, Oxford University Press 2010) 2281.

4 The DCFR, II. – 1:101(1).

not required to conclude a franchise contract in writing. Nor do the parties have to conclude a franchise contract in other specific forms.⁵ For example, the franchisor and franchisee are not required to ask a notary to authenticate a franchise contract or register a franchise contract with the public authorities.⁶ In theory, the franchisor and the franchisee may enter into a franchise agreement verbally. Despite this, the franchisor or the franchisee may request a statement in textual form on a durable medium setting out the terms of the contract.⁷ In any event, in practice, a franchise contract usually is concluded in writing as a standard-form contract.⁸

2.2.3 Right to conduct a franchise business

A franchise contract is a marketing contract with particular elements included by IV.E. – 4:101. The first component of a franchise contract is a grant of the right to conduct a franchise business.⁹ Under a franchise contract, the franchisor will grant the franchisee the right to conduct a franchise business in the franchise network to dispense certain goods or services onto the market.¹⁰ IV.E. – 4:101 implies the following two additional elements concerning the conduct of a franchise business: the control over a franchise business operation and the independence in a franchise business operation.

5 The DCFR, II. – 1:106(1).

6 Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.1, Oxford University Press 2010) 149. In some European countries, such as Italy, a franchise contract is required to be made in writing. The failure to follow the formal requirement will render the agreement void. See Bar and Clive (n 3) 2387.

7 The DCFR, IV.E. – 2:402(1).

8 John Velentzas and Georgia Broni, 'The Business Franchise Contract As A Distribution Marketing System: Free Competition And Consumer's Protection' (2013) 5 *Procedia Economics and Finance* 763, 767. In the case of a standard form contract, the DCFR contains some provisions that will regulate the unfairness of a franchise contract's terms. According to II. – 9:405, the franchisee may argue that the term of a standard-form franchise contract supplied by the franchisor is unfair in that its use grossly deviated from good commercial practice, contrary to good faith and fair dealing. In this case, the unfair term will not bind the franchisee as a result of II. – 9:408(1).

9 According to the drafters of the DCFR, a franchise business can be divided into three main types: industrial, distribution, and service franchises. First, in industrial franchising, a franchisee will produce goods following the franchisor's instructions and sell the goods under the franchisor's intellectual property rights. Second, in a distribution franchise, the franchisee will distribute goods in an outlet that bears the franchisor's business name or symbol. Third, the franchisee will provide services under the franchisor's business name, symbol, or intellectual property rights in service franchising. See Bar and Clive (n 3) 2384.

10 In this respect, a franchise contract is a contract in the network. This network consists of the franchisor and its franchisees operating the same business method and communicating with others. See Bar and Clive (n 3) 2384.

2.2.3.1 *Control over a franchise business operation*

A franchise contract is a contract by which a franchisee conducts a franchise business under the franchisor's method. Inferred from IV.E. – 4:101, the franchisee has an obligation to use the franchisor's business method. According to the drafters of the DCFR, a franchise business method includes a general explanation of the franchise system, the characteristics of the know-how, the assistance that the franchisor will offer, and an estimate of the investments and expenses that are necessary for operating a business.¹¹ As can be seen, the franchisee is required to use the franchisor's business method. In this respect, IV.E. – 4:303(1) to (3) elaborates on the manners in which the franchisee performs this obligation.¹² According to paragraphs (1) to (3), the franchisee must make reasonable efforts to utilize the franchisor's business method; the franchisee must follow the franchisor's reasonable instructions concerning the method and the maintenance of the reputation of a franchise network, and the franchisee must take reasonable care not to damage the franchise network.

2.2.3.2 *Independence in a franchise business operation*

A franchise contract is a contract by which a franchisee independently conducts a franchise business. The concept of the franchisee independence can be extracted from IV.E. – 1:101(1), in conjunction with IV.E. – 4:101. Paragraph (1) of IV.E. – 1:101 acknowledges that distributors, including franchisees, are engaged in the business independently. The commentaries to this article explain that a franchise relationship is not an employment relationship in which the franchisee is under the command and control of the franchisor. IV.E. – 4:101 seems to affirm the independent nature of a franchise relationship because this article provides that the franchisee will operate a franchise business on the franchisee's behalf and in the franchisee's name.¹³ Nevertheless, those two provisions by no means suggest that the franchisee is contractually independent of the franchisor. As can be seen in the preceding subsection, the franchisee is required to follow the franchisor's business method in operating a franchised business.

¹¹ Ibid 2389.

¹² The drafters of the DCFR argue that these requirements are imposed to ensure the uniformity of a franchise network. *See* *ibid* 2419.

¹³ This element suggests that the franchisor will not be liable for any loss or damage caused by the franchisee's conduct in operating franchised units. Furthermore, the franchisee will solely be responsible for any financial loss incurred from the operation of the franchised outlet.

2.2.4 Right to use the business package

The second element of a franchise contract is the franchisee's right and obligation to use the franchisor's business package. In operating a franchise business, a franchisee is licensed and required to use the franchisor's intellectual property rights and know-how. According to the drafters of the DCFR, intellectual property rights encompass industrial and intellectual property rights regarding trademarks, trade names, shop signs, logos, insignia, utility models, designs, copyrights and related rights, software, drawings, plan, and patents held by the franchisor.¹⁴ Know-how is understood as a package of non-patented practical information, resulting from experience and testing by the supplier, which is secret, substantial, and identified.¹⁵

As mentioned above, the franchisee will have the right to use the franchisor's business package. In this case, the franchisor has to grant the franchisee the right to use the intellectual property rights and know-how that are necessary for the franchisee to operate the franchise business. Nevertheless, the DCFR does not contain model rules governing licensing intellectual property rights and authorizing the use of know-how. In this case, the drafters of the DCFR suggest that national law of European countries will apply.¹⁶ These domestic laws vary from country to country. For example, in the Netherlands, the Benelux Convention on Intellectual Property (BCIP) specifically governs the rights pertinent to trademarks and designs.¹⁷ However, the BCIP imposes no formality for licensing those intellectual property rights. In any case, the franchisee's right to use the franchisor's business package cannot be agreed otherwise, pursuant to IV.E. – 4:201(3) and 4:202(2). Thus, it could be said that the grant of the business package is an integral part of a franchise contract.

2.2.5 Monetary considerations

The third element of a franchise contract is monetary considerations. According to IV.E. – 4:101, a franchisee is required to make remuneration to a franchisor in exchange for a grant of a franchise.¹⁸ IV.E. – 4:301(1) provides that the remuneration may take the form of initial franchise fees, royalties, and other

¹⁴ Bar and Clive (n 3) 2395.

¹⁵ The drafters refer to the definition of know-how offered by article 1(f) of the Commission Regulation (EC) No 2790/1999 of 22 December 1999 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices. *See* *ibid* 2397-398.

¹⁶ *Ibid* 2395.

¹⁷ The English text of the BCIP can be accessed at <<https://bit.ly/3m6tIs0>>.

¹⁸ The DCFR, IV.E. – 4:101.

periodical payments agreed by the parties under the contract.¹⁹ Although the franchisor is generally free to determine the amount of payment, the DCFR protects the franchisee against the franchisor's abuse of this discretionary power in some cases.²⁰ According to IV.E. – 4:301(2), in conjunction with II. – 9:105, the franchisee may make reasonable payment to the franchisor, provided that the franchisor unilaterally holds discretion in determining payment, and the franchisor's determination of the payment is unreasonable. In these cases, the franchisee may pay reasonable fees even though the franchisor requires otherwise.

2.2.6 Conclusions

A franchise is a specific contract. The DCFR differentiates a franchise contract from other nominate contracts by regulating the constituent elements of the contract and providing model rules regulating the relationship in Part E of Book IV. Essentially, a franchise contract is a contract by which a franchisor grants a franchisee the right to conduct a franchise business in the franchise network. In conducting a franchised business, the franchisee can operate the business independently under the franchisor's control over the business method. A franchise contract is a contract by which the franchisor grants the franchisee the right to use the franchisor's intellectual property rights, know-how, and business method. In exchange for the grant of these rights, the franchisee is required to remunerate the franchisor in the form of agreed initial franchise fees, royalties, and other periodical payments.

2.3 THE UNITED STATES OF AMERICA (USA)

2.3.1 Introduction

The FTC Rule is the federal franchise sale law that applies throughout the USA. At the state level, twenty-four states (franchise-regulating states) have franchise-specific legislation regulating a franchise in their own jurisdictions.²¹ Both federal and state franchise-specific laws define a franchise. However, it is

19 Neither IV.E. – 4:301 nor the drafters of the DCFR exemplify the expression 'other periodical payments'. In franchising practice, an additional periodical payment may take the form of a marketing fee that the franchisee is required to pay to the franchisor periodically during a franchise relationship.

20 Bar and Clive (n 3) 2416.

21 Those twenty-three franchise-regulating states are Arkansas, California, Connecticut, Delaware, Florida, Hawaii, Illinois, Indiana, Iowa, Maryland, Michigan, Minnesota, Mississippi, Missouri, Nebraska, New Jersey, New York, North Dakota, Oregon, Rhode Island, South Dakota, Virginia, Washington, and Wisconsin.

claimed that there is no uniform definition of a franchise in the country.²² Despite no uniformity in defining a franchise, a franchise is commonly understood as a contract, agreement, or arrangement between the franchisor and franchisee with the following three essential elements: (1) the grant of the right to conduct a franchise business, (2) the use of the franchisor's marks, and (3) the payment of monetary consideration. This section will examine all the franchise components in sections 2.3.2, 2.3.3, 2.3.4, and 2.3.5, respectively. Section 2.3.6 will conclude on the essential elements of a franchise under the US legal system.

2.3.2 Contract, agreement, or arrangement

Under the FTC Rule and the state franchise-specific laws, a franchise relationship is a legal relationship created by a contract, agreement, or arrangement between a franchisor and a franchisee.²³ Under the federal and state statutes, a franchisor is ordinarily a person who grants a franchise and participates in the franchise relationship.²⁴ A franchisee is a person who is granted a franchise.²⁵ In sum, a franchise requires an agreement made by the franchisor and the franchisee.²⁶

In terms of formality, the formal requirement may vary. Some franchise-specific statutes explicitly mention the format of a franchise agreement. The FTC Rule and some state franchise-specific laws, such as the franchise statute

22 Joseph J Fittante, Jr, "Community of Interest": Clarity or Confusion? (2003) 22 Franchise Law Journal 160, 160; John R F Baer and Susan Grueneberg, 'United States' in Andrew P Loewinger and Michael K Lindsey (eds), *International Franchise Sales Laws* (American Bar Association 2016) 503. Thus, this section will not thoroughly examine a franchise definition under the federal and state franchise-specific statutes. Instead, this section pays attention to the elements of a franchise that are common among the selected franchise-specific laws.

23 The FTC Rule: 16 CFR, § 436.1(h); Arkansas: AR ST, § 4-72-202(1)(A); California: CA CORP, § 31005(a)(1) and CA BUS & PROF, § 20003(a); Connecticut: CT ST, § 42-133e(b); Delaware: DE ST TI 6, § 2551(1); Florida: FL ST § 817.416(1)(b); Hawaii: HI ST, § 482E-2; Illinois: IL ST CH 815, § 705/3(1)(a); Indiana: IN ST, 23-2-2.5-1(a) and IN ST, 23-2-2.7-5; Iowa: IA ST, § 523H.1(3.a)(1)(a) and IA ST, § 537A.10(c.1)(a)(i); Maryland: MD BUS REG, § 14-201(e)(1)(i); Michigan: MI ST, 445.1502(3)(a); Minnesota: MN ST, § 80C.01(Subd. 4)(a)(1)(i); Mississippi: MS ST, § 75-24-51(c); Missouri: MO ST, 407.400(1); Nebraska: NE ST, § 87-402(1)(a); New Jersey: NJ ST, 56:10-3(a); New York: NY GEN BUS, § 681(3)(a); North Dakota: ND ST, 51-19-02(5a)(1); Oregon: OR ST, § 650.005(4)(a); Rhode Island: RI ST, § 6-50-2(16)(3)(i) and RI ST, § 19-28.1-3(7)(i)(A); South Dakota: SD ST, § 37-5B-1(11); Virginia: VA ST, § 13.1-559(1); Washington: WA ST, 19.100.010(6)(a)(i); Wisconsin: WI ST, 135.02(3)(a) and WI ST, 553.03(4)(a)(1).

24 16 CFR, § 436.1(k) and SD ST, § 37-5B-1(14).

25 16 CFR, § 436.1(i) and SD ST, § 37-5B-1(12).

26 W Michael Garner, Contract principles and franchise relationship, 2 Franch & Distr Law & Prac, Westlaw (November 2020) at § 8:1. According to the Restatement (Second) of Contracts, an agreement is a manifestation of mutual assent on the part of two or more persons. See Restatement (Second) of Contracts, § 3.

of Florida, provide that a franchise agreement can take the form of an oral or written agreement.²⁷ Conversely, in Mississippi, Nebraska, New Jersey, and Virginia, the state franchise legislation requires a franchise contract to be made only in a written form. In these states, an oral franchise agreement is claimed to be unenforceable.²⁸ It should be mentioned that some franchise-specific statutes do not address the format of a franchise agreement. For example, in Delaware and Indiana, the franchise statutes are silent on the formal requirement of a franchise contract.²⁹ Accordingly, one commentator provides that it is not certain that a franchise agreement is required to take a written form.³⁰

2.3.3 Right to conduct a franchise business

A franchise is a contractual relationship in which a franchisor grants a franchisee the right to conduct a franchise business. Under federal and state laws, a franchise business is typically understood as the business of offering, selling, or distributing goods or services.³¹ Some franchise-specific legislation includes in the definition of a franchise an additional element demonstrating the franchisor's control or assistance concerning the operation of the franchise business. This component is added to maintain uniformity in a franchise network. The following four subsections will survey the elements suggesting the franchisor's control or assistance adopted under the federal and state franchise statutes.

2.3.3.1 Significant control and assistance

The FTC Rule and South Dakota franchise-specific law similarly require that the franchisor exerts a significant degree of control over the franchisee's

27 16 CFR, § 436.1(h) and FL ST § 817.416(1)(b).

28 Nicole S Zellweger, 'Enforceability of Oral Franchise Agreement' (2009) 28 Franchise Law Journal 136, 136.

29 Delaware: DE ST TI 6, § 2551(1); Indiana: IN ST, 23-2-2.5-1(a) and IN ST, 23-2-2.7-5.

30 Zellweger (n 28) 136.

31 The FTC Rule: 16 CFR, § 436.1(h)(1); Arkansas: AR ST, § 4-72-202(1)(A); California: CA CORP, § 31005(a)(1) and CA BUS & PROF, § 20003(a); Connecticut: CT ST, § 42-133e(b); Delaware: DE ST TI 6, § 2551(2); Florida: FL ST § 817.416(1)(b)(2); Hawaii: HI ST, § 482E-2; Illinois: IL ST CH 815, § 705/3(1)(a); Indiana: IN ST, 23-2-2.5-1(a)(1); Iowa: IA ST, § 523H.1(3.a)(1)(a) and IA ST, § 537A.10(c.1)(a)(i); Maryland: MD BUS REG, § 14-201(e)(1)(i); Michigan: MI ST, 445.1502(3)(a); Minnesota: MN ST, § 80C.01(Subd. 4)(a)(1)(i); Mississippi: MS ST, § 75-24-51(c); Missouri: MO ST, 407.400(1); Nebraska: NE ST, § 87-402(1)(a); New Jersey: NJ ST, 56:10-3(a); New York: NY GEN BUS, § 681(3)(a); North Dakota: ND ST, 51-19-02(5a)(1); Oregon: OR ST, § 650.005(4)(a); Rhode Island: RI ST, § 6-50-2(16)(3)(i) and RI ST, § 19-28.1-3(7)(i)(A); South Dakota: SD ST, § 37-5B-1(11)(a); Virginia: VA ST, § 13.1-559(1); Washington: WA ST, 19.100.010(6)(a)(i), and Wisconsin: WI ST, 135.02(3)(a) and WI ST, 553.03(4)(a)(1).

method of operation or provides significant assistance in the franchisee's method of operation.³² However, the FTC Rule and the South Dakota statute do not offer criteria for determining this element. Despite the lack of statutory criteria, the Franchise Rule Compliance Guide (Compliance Guide) provides some helpful guidelines in this regard.³³ First of all, the Compliance Guide offers general considerations that the franchisor's significant control or assistance must relate to the franchisee's overall business operation. In other words, the franchisor's significant control or assistance must not have a marginal effect on the franchisee's operating method. Besides, the franchisor's significant control or assistance must correlate with the franchisee's reliance upon the franchisor's control or assistance. The indication is that the more the franchisee reasonably relies upon the franchisor's control or assistance, the more the franchisor's control or assistance is considered significant.³⁴

In addition to general considerations, the Compliance Guide exemplifies types of the franchisor's significant control and assistance. For instance, the franchisor has significant control over the franchisee's franchise business operation if the franchisor has the power to approve the site for unestablished businesses; impose design or appearance requirements; set hours of operation; control production techniques, to name a few. Additionally, the franchisor provides significant assistance if the franchisor establishes formal sales, repair, and business training programs; offers accounting systems; helps select site locations; furnishes a detailed operating manual, to name a few. As a matter of policy, some factors will not establish the franchisor's significant control and assistance. These factors include trademark controls designed solely to protect the trademark owner under state and federal trademark laws and health or safety restrictions required by federal or state law and regulations.³⁵

32 16 CFR, § 436.1(h)(2) and SD ST, § 37-5B-1(11)(b). Nevertheless, Grueneberg claims that the laws merely require the franchisor to retain the right to do so under a franchise agreement. In other words, the franchisor may not have to actually exercise significant control over the franchisee's franchise business operation or provide significant assistance to the franchisee in operating a franchise business. See Susan Grueneberg, 'Chapter 8: The FTC Rule' in Alexander M Meiklejohn (ed), *Franchising: Cases, Materials, & Problems* (American Bar Association 2013) 27.

33 The Compliance Guide is introduced to facilitate the franchisor's compliance with the FTC Rule. The text of the Compliance Guide can be accessed at <<https://bit.ly/31JyyNE>>.

34 The Compliance Guide, at 2.

35 Ibid, at 3 – 4.

2.3.3.2 Marketing plan or system

Some state franchise-specific statutes require the franchisee to engage in a franchise business under a marketing plan or system.³⁶ Nevertheless, the state laws differ in contemplating the expression 'a marketing plan or system'. Some franchise-specific statutes define the phrase explicitly. For example, Iowa's franchise-specific statutes define the term 'marketing plan' to mean a plan or system concerning a material aspect of conducting business. In addition, the Iowa laws provide a non-exhaustive list of indicators of the marketing plan. These indicators include price specification, special pricing systems or discount plans, sales or display equipment or merchandising devices, sales techniques, promotional or advertising materials or cooperative advertising, training regarding the promotion, operation, or management of the business, and operational, managerial, technical, or financial guidelines or assistance.³⁷

Some state franchise laws may not elaborate on the term marketing plan or system. In this respect, state courts play a vital role in clarifying the expression. For example, in Indiana, the court in *Master Abrasives v Williams* enumerated the factors indicating the existence of a marketing plan in a franchise contract. According to the court, the marketing plan exists if the franchise contract (1) divides the state into marketing areas; (2) authorizes the franchisor to establish sales quotas; (3) gives the franchisor the right of approval of sales personnel employed by the franchisee; (4) establishes mandatory sales training by the franchisor for the franchisee's sales personnel, and (5) requires the franchisee's sales personnel to elicit information from customers as to the use each customer would make of the franchisor's products.³⁸ However, the court in *RWJ Companies Inc v Equilon Enterprises* provided that those factors were not intended to be exhaustive. Instead, attention must be paid to the nature of obligations in the agreement, with special regard to the franchisor's mandates regarding the sales of goods and services.³⁹

In addition to the element of a marketing plan or system, the state franchise-specific statutes also require an element of a substantial prescription. That is, the laws require a marketing plan or system to be prescribed in substantial

36 California: CA CORP, § 31005(a)(1) and CA BUS & PROF, § 20003(a); Connecticut: CT ST, § 42-133e(b); Illinois: IL ST CH 815, § 705/3(1)(a); Indiana: IN ST, 23-2-2.5-1(a)(1); Iowa: IA ST, § 523H.1(3.a)(1)(a) and IA ST, § 537A.10(c.1)(a)(i); Maryland: MD BUS REG, § 14-201(e)(1)(i); Michigan: MI ST, 445.1502(3)(a); New York: NY GEN BUS, § 681(3)(a); North Dakota: ND ST, 51-19-02(5a)(1); Oregon: OR ST, § 650.005(4)(a); Rhode Island: RI ST, § 19-28.1-3(7)(i)(A); Virginia: VA ST, § 13.1-559(1); Washington: WA ST, 19.100.010(6)(a)(i), and Wisconsin: WI ST, 553.03(4)(a)(1).

37 IA ST, § 523H.1(7) and IA ST, § 537A.10(g).

38 *Master Abrasives Corp v Williams*, 469 NE 2d 1196 (Ind App 4 Dist, 1984) 1200. The indicators enumerated in the case *Master Abrasives Corp* were cited in the case *Horner v Tilton*, 650 NE 2d 759 (Ind App, 1995) 762.

39 *RWJ Companies Inc v Equilon Enterprises LLC*, 2005 WL 3544295 (SD Ind, 2005) 4, citing *Horner v Tilton*, 650 NE 2d 759 (Ind App, 1995) 762.

part by the franchisor. Despite the lack of the definition under the franchise statutes, some franchise-regulating states explain this component through their administrative regulations and guidelines.⁴⁰ For example, in Michigan, the administrative regulation exemplifies four factors indicating that a marketing plan or system is prescribed in substantial part by the franchisor.⁴¹ Alternatively, in California, the administrative guidance, Commissioner's Release 3-F (the Release), offers guidelines for determining whether an agreement constitutes a franchise in light of the Californian franchise investment law.⁴² According to the Release, the prescription of a marketing plan exists if the franchisee's right to engage in a franchise business is subject to some restrictions regarding a marketing plan or system imposed by the franchisor. In any case, a question of whether the restrictions are substantial must be determined on a case-by-case basis, considering all provisions in a franchise agreement.⁴³

40 Moreover, state courts may play a role in deciding if the prescription of a marketing plan exists. In practice, a number of court decisions have addressed the issue concerning a marketing system or plan prescribed in substantial part by the franchisor. For example, the Michigan court in *Vaughn v Digital Message Systems* held that the franchisor prescribed in substantial part a marketing plan for the franchisee because the franchisor laid down sales, marketing, and training guidelines for the franchisee in a franchise agreement. See *Vaughn v Digital Message Systems Corp*, 1997 WL 115821 (ED Mich, 1997) 6.

41 MI ADC, R 445.101 states those four factors as follows:

'(1) Representations by, or requirements of, the franchisor that the franchisee operates a business which can purchase a substantial portion of its goods solely from sources designated or approved by the franchisor.

(2) Representations by, or requirements of, the franchisor that the franchisee follows an operating plan, standard procedure, training manual, or its substantial equivalent promulgated by the franchisor in the operation of the franchise, violations of which may, under the terms of the agreement, permit the franchisor to terminate or refuse to renew the agreement.

(3) Representations by, or requirements of, the franchisor that the franchisee is limited as to type, quantity, or quality of any product or service the franchisee may sell, or that limit the franchisee as to the persons or accounts to which he may sell the franchisor's product or service.

(4) Representations by, or requirements of, the franchisor that the franchisor aids or assists the franchisee in training or in obtaining locations or facilities for operation of the franchisee's business, or in marketing the franchisor's product or service.'

42 The Release can be accessed at <<https://bit.ly/3mktvvc>>.

43 The Release offers examples of a prescribed marketing plan or systems as follows: prescribing or limiting resale prices, restrictions on use of advertising or mail order, requiring display racks, giving detailed directions and advice concerning operating techniques, assigning exclusive territory, providing training sessions, assigning contract, use of manual, and providing trade secrets. The Release mentions that any of those examples alone may not constitute the prescription of a marketing plan or system by the franchisor. However, a combination of the exemplified restrictions may amount to a marketing system or plan prescribed in substantial part by the franchisor.

2.3.3.3 Community of interest

Other states adopt the concept of a community of interest instead of a marketing plan or system. In these jurisdictions, the franchise-specific statute requires that there is an element of a community of interest in the franchise business.⁴⁴ Some states define the expression 'community of interest'. In Hawaii, Rhode Island, and Wisconsin, the law defines the expression to mean a continuing financial interest between the franchisor and the franchisee in the operation of the franchise business or the marketing of goods or services.⁴⁵ Nevertheless, the definition provided by the statutes is ambiguous. Thus, some state courts have tried listing factors for determining if there is a community of interest between the franchisor and the franchisee in a franchise relationship. For example, in Wisconsin, the Supreme Court in *Ziegler v Rexnord* enumerated ten non-exclusive indicators of a business relationship with continuing financial interest.⁴⁶

Other states do not define the concept of a community of interest. In this respect, courts have played a pivotal role in enumerating indicators of a 'community of interest'. However, the indicators listed by the courts vary from case to case. For example, in New Jersey, the court in *Orologio of Short Hills v The Swatch Group (US)* employed a balancing test in that the court takes into account the following four indicators: (1) the purported franchisor's control over the purported franchisee, (2) the purported franchisee's economic dependence on the purported franchisor, (3) disparity in bargaining power, and (4) the presence of a franchise-specific investment by the purported franchisee.⁴⁷ Conversely, in Minnesota, the court in *Martin Investors v Vander Bie* embraced

44 Hawaii: HI ST, § 482E-2; Minnesota: MN ST, § 80C.01(Subd. 4)(a)(1)(ii); Mississippi: MS ST, § 75-24-51(c); Missouri: MO ST, 407.400(1); Nebraska: NE ST, § 87-402(1)(a); New Jersey: NJ ST, 56:10-3(a); Rhode Island: RI ST, § 6-50-2(16)(3)(i), and Wisconsin: WI ST, 135.02(3)(a).

45 Hawaii: HI ST, § 482E-2 Rhode Island: RI ST, § 6-50-2(1), and Wisconsin: WI ST, 135.02(1).

46 The Supreme Court enumerated ten factors as follows:

'(1) how long the parties have dealt with each other; (2) the extent and nature of the obligations imposed on the parties in the contract or agreement between them; (3) what percentage of time or revenue the alleged dealer devotes to the alleged grantor's products or services; (4) what percentage of the gross proceeds or profits of the alleged dealer derives from the alleged grantor's products or services; (5) the extent and nature of the alleged grantor's grant of territory to the alleged dealer; (6) the extent and nature of the alleged dealer's uses of the alleged grantor's proprietary marks (such as trademarks or logos); (7) the extent and nature of the alleged dealer's financial investment in inventory, facilities, and goodwill of the alleged dealership; (8) the personnel which the alleged dealer devotes to the alleged dealership; (9) how much the alleged dealer spends on advertising or promotional expenditures for the alleged grantor's products or services; (10) the extent and nature of any supplementary services provided by the alleged dealer to consumers of the alleged grantor's products or services.'

See *Ziegler Co Inc v Rexnord Inc*, 407 NW 2d 873 (Wis, 1987) 879-80.

47 *Orologio of Short Hills Inc v The Swatch Group (US) Inc*, 653 Fed Appx 134 (CA3 (NJ), 2016) 139.

the shared-profit test when explaining a community of interest. According to the court, a community of interest is constituted if the putative franchisor and franchisee share in fees from a common source of the service provided by the franchisor and franchisee.⁴⁸

2.3.3.4 Substantial reliance

Florida is the only franchise-regulating state that adopts the concept of substantial reliance. According to the Florida franchise misrepresentation law, the operation of the franchisee's business must be substantially reliant on a franchisor for the basic supply of goods.⁴⁹ However, the law does not define the term 'substantially reliant'. There is one court decision that addresses the concept of substantial reliance. In *International Dairy Queen*, the court decided that the operation of the franchisee's business was substantially reliant on the franchisor if the franchisee was required to buy the products bought from the franchisor's approved suppliers.⁵⁰

2.3.4 Use of the franchisor's marks

The use of the franchisor's marks is the second element that is common among federal and state franchise-specific laws. At the national level, the FTC Rule provides that the franchisee will obtain the right to operate a franchise business that is identified or associated with the franchisor's trademark or the right to offer, sell, or distribute goods, services, or commodities that are identified or associated with the franchisor's trademark.⁵¹ In this case, the FTC Rule assigns a special meaning to the term 'trademark'. Under the Rule, a 'trademark' is defined to include trademarks, service marks, names, logos, and other commercial symbols.⁵²

At the state level, all state franchise-specific laws, except Florida's, include the element of the use of the franchisor's marks in the definition of a franchise. Some franchise statutes require the franchisee's business to be substantially associated with the franchisor's trademark, service mark, trade name, logotype, advertising, or other commercial symbol designating the franchisor or its

48 However, the court provided that there is no substantiality requirement for creating a community of interest. Thus, the franchisor's right to one percent of the proceeds of each loan placed by the franchisee in the marketing of the service suffices to indicate a community of interest between the franchisor and franchisee. See *Martin Investors, Inc v Vander Bie*, 269 NW 2d 868 (Minn, 1978) 875.

49 FL ST § 817.416(1)(b)(4).

50 *Boca Mara Properties, Inc v International Dairy Queen, Inc*, 732 F2d 1550 (CA Fla, 1984) 1552.

51 16 CFR, § 436.1(h)(1).

52 16 CFR, § 436.1(v).

affiliate.⁵³ Other state laws require the franchisor to license the franchisee to use a trade name, service mark, trademark, logotype, or related characteristic in a franchise business.⁵⁴ It should be noted that, under these statutes, no requirement of the substantial association with the franchisor's marks exists.⁵⁵

2.3.5 Monetary considerations

The franchisee's monetary consideration is the third crucial element of a franchise agreement. At the federal level, the FTC Rule provides that the franchisee shall make a required payment or commit to making a required payment to the franchisor or its affiliate.⁵⁶ At the state level, nineteen states' franchise-specific statutes impose the payment requirement.⁵⁷ Most state laws

53 California: CA BUS & PROF, § 20001(b) and CA CORP, § 31005(a)(2); Connecticut: CT ST, § 42-133e(b); Illinois: IL ST CH 815, § 705/3(1)(b); Indiana: IN ST, 23-2-2.5-1(a)(2); Iowa: IA ST, § 523H.1(3a)(1)(a) and IA ST, § 537A.10(c)(1)(a)(iii); Maryland: MD BUS REG, § 14-201(e)(1)(ii); Michigan: MI ST, 445.1502(3)(b); New York: NY GEN BUS, § 681(3)(b); North Dakota: ND ST, 51-19-02(5)(a)(2); Oregon: OR ST, § 650.005(4)(b); Virginia: VA ST, § 13.1-559(2), and Washington: WA ST, 19.100.010(6)(a)(ii). In some states, the expression 'substantially associated' is clarified by the administrative regulation. For example, under the Illinois administrative regulation, the franchisee's business will be considered substantially associated with the franchisor's marks if the franchisee uses the marks to identify its business to the customers or convey to the public that the franchisee's business is the franchisee's outlet. *See* 14 IL ADC, 200.103. Thus, marketing the product with the franchisor's name or mark alone does not sufficiently establish a franchise under the Illinois franchise disclosure law. *See Mechanical Rubber & Supply Co v American Saw and Mfg Co*, 810 F Supp 986 (CD Ill, 1990) 991.

54 Arkansas: AR ST, § 4-72-202(1)(A); Hawaii: HI ST, § 482E-2(5); Minnesota: MN ST, § 80C.01(sub.4)(i); Mississippi: MS ST § 75-24-51(c); Missouri: MO ST 407.400(1); Nebraska: NE ST § 87-402(1); New Jersey: NJ ST 56:10-3(a) Rhode Island: RI ST § 6-50-2(3)(i), and Wisconsin: WI ST 135.02(3)(a).

55 For instance, the Minnesota courts emphasized that this element only requires that the franchisee is granted the right to use the franchisor's mark or name, not that the franchisee is permitted to hold itself as the franchisor or an authorized representative of the franchisor. *See Martin Investors Inc v Vander Bie*, 269 NW 2d 868 (Minn, 1978) 874; *RJM Sales & Marketing Inc v Banfi Products Corp*, 546 F Supp 1368 (DC Minn, 1982) 1373.

56 16 CFR, § 436.1(h)(3). The phrase 'required payment' is defined to mean all consideration that the franchisee must pay to the franchisor, either by contract or by practical necessity, as a condition of obtaining or commencing the operation of the franchise. However, a required payment does not include payments for the purchase of reasonable amounts of inventory at bona fide wholesale prices for resale or lease. *See* 16 CFR, § 436.1(s). According to the Compliance Guide, the required payment broadly captures all sources of revenue, including the initial franchise fee, rent, advertising assistance, equipment and supplies, training, security deposits, escrow deposits, non-refundable bookkeeping charges, promotional literature, equipment rental, and continuing royalties on sales. *See* The Compliance Guide, at 5.

57 California: CA BUS & PROF, § 20001(c) and CA CORP, § 31005(a)(3); Delaware: DE ST TI 6, § 2551(1); Hawaii: HI ST, § 482E-2(5); Illinois: IL ST CH 815, § 705/3(1)(c); Indiana: IN ST, 23-2-2.5-1(a)(3); Iowa: IA ST, § 523H.1(3a)(1)(b) and IA ST, § 537A.10(c)(1)(a)(ii);

require that the franchisee pays consideration to the franchisor in the form of a franchise fee. Nevertheless, the state franchise statutes vary when it comes to defining the term 'franchise fee'. Despite the variation, a franchise fee is commonly understood as any fee or charge that the franchisee is directly or indirectly required to pay for the right to enter into a franchise business or to continue a franchise business.⁵⁸

2.3.6 Conclusions

This section explores some common characteristics of a franchise, although federal and state franchise-specific laws define it differently in detail. In the USA, a franchise is constituted by an agreement with a combination of the following three elements. First, a franchisor grants a franchisee the right to conduct a franchise business uniformly within a franchise system. Second, a franchisee uses a franchisor's marks in a franchise business operation. Third, a franchisee pays a franchisor monetary consideration for the right to operate a franchise business. These three elements are integral parts of a franchise agreement. Thus, an agreement that lacks one or all of these three components will not constitute a franchise relationship between the franchisor and the franchisee.

2.4 AUSTRALIA

2.4.1 Introduction

Australia regulates a franchise through the Franchising Code of Conduct (the Code). Under the Code, a franchise can be established in various ways.⁵⁹ Among other things, a franchise agreement can establish a franchise relationship.⁶⁰ In light of the Code, a franchise agreement is defined to mean an

Maryland: MD BUS REG, § 14-201(e)(1)(iii); Michigan: MI ST, 445.1502(3)(c); Minnesota: MN ST, § 80C.01(sub.4)(iii); Mississippi: MS ST § 75-24-51(c); Nebraska: NE ST § 87-402(1); New York: NY GEN BUS, § 681(3)(a); North Dakota: ND ST, 51-19-02(5)(a)(3); Oregon: OR ST, § 650.005(4)(c); Rhode Island: RI ST, § 19-28.1-3(7)(i)(b); South Dakota: SD ST, § 37-5B-1(11)(c); Virginia: VA ST, § 13.1-559(3); Washington: WA ST, 19.100.010(6)(a)(iii), and Wisconsin: WI ST, 553.03(4)(a)(3).

58 In Delaware, Illinois, Rhode Island, and Virginia, the law sets the minimum threshold of a franchise fee. For example, under the Virginia Retail Franchising Act, the franchisee is required to pay a franchise fee of 500 US dollars and more for the right to operate a franchise business. See VA ST, § 13.1-559(3).

59 *Subway Systems Australia Pty Ltd v Thorpe* [2000] QSC 099 [7].

60 It should be noted that the Code identifies certain contractual relationships that do not constitute a franchise agreement. For example, a partnership relationship is not a franchise relationship. See The Code, cl. 5(3).

agreement with the following three particular elements: (1) the right to conduct a franchise business, (2) the use of a trademark, advertising or a commercial symbol, and (3) monetary considerations.⁶¹ This section will examine all the components of a franchise agreement in sections 2.4.2, 2.4.3, 2.4.4, and 2.4.5, respectively. Section 2.4.6 will conclude on the principal characteristics of a franchise agreement under the Code.

2.4.2 Agreement

An agreement is essential to establish a franchise under the Code. Though, the Code does not define the term ‘agreement’. Neither does case law assign a special meaning to the phrase ‘agreement’ for the purpose of applying the Code. Despite the lack of a definition under the Code, Giles provides that the phrase ‘agreement’ can have a meaning under general contract law.⁶² In contract law, an agreement is understood as a meeting of the minds of the two parties that involves an exchange of promises.⁶³ In a franchise agreement, clause 5(1)(b) indicates that a franchisor and a franchisee are the parties to the agreement. In terms of definition, the Code defines the terms ‘franchisor’ and ‘franchisee’ in different ways. Among other things, a franchisor is defined to mean a person who grants a franchise. A franchisee is defined to mean a person to whom a franchise is granted.

In addition, a franchise agreement must be concluded in any of specific forms introduced by the Code. According to clause 5(1)(a), a franchise agreement is an agreement that takes the form, in whole or part, of any of the following three forms: a written agreement, an oral agreement, and an implied agreement.⁶⁴ As can be seen, a franchisor and a franchisee can conclude a franchise agreement more flexibly since the agreement is not necessarily established by a written agreement. Despite this, court decisions show that, in practice, a franchise agreement seems to be made in writing.⁶⁵

⁶¹ The Code, cl. 4.

⁶² Stephen Giles, *Annotated Franchising Code of Conduct* (2nd edn, LexisNexis Butterworths 2021) 29.

⁶³ Philip Clarke and Julie Clarke, *Contract Law: Commentaries, Cases, and Perspectives* (3rd edn, Oxford University Press 2016) 26. An agreement must be effective and enforceable at law. See eg *Fevia v Carmel-Fevia*, [2009] Fam CA 816 [121].

⁶⁴ The Code, cl. 5(1)(a)(i) – (iii).

⁶⁵ See eg *Agro Holdings Ltd v Flexi-Coil (Australia) Pty Ltd*, [1999] FCA 1658 [29]; *Capital Networks Pty Ltd v .au Domain Administration Ltd*, [2004] FCA 808 [96]; *Australian Competition and Consumer Commission v Kyloe Pty Ltd*, [2007] FCA 1522 [26]; *W Hoy Pty Ltd v W.T.H. Pty Ltd*, [2018] FCA 310 [25].

2.4.3 Right to conduct a franchise business

The first element of a franchise agreement is the right to conduct a franchise business. The Code provides that, under a franchise agreement, a franchisor grants a franchisee the right to conduct a business of offering, supplying, or distributing goods or services. The Code also requires the franchisee to conduct a franchise business under a system or marketing plan.⁶⁶ Although the Code does not define the phrase ‘system or marketing plan’, some Australian courts have clarified this expression. For example, the Federal Court in *Rafferty and Another v Madgwicks* suggested that the expression ‘system or marketing plan’ referred to a coordinated method, procedure, or scheme whereby goods or services are sold.⁶⁷ Bennet J in *Capital Networks v .au Domain Administration* derived some helpful indicators of a system or marketing plan from the selected American authorities. That is, the system or marketing plan may be established because of the fact that the franchisor provides the franchisee with a detailed compensation and bonus structure for franchisees selling the products, a centralized bookkeeping and record-keeping computer operation for franchisees, a prescribed scheme through which a person can become a franchisee, and a reservation of the right to screen and approve all promotional materials used by franchisees.⁶⁸

Additionally, the Code requires that the franchisee conducts a franchise business under a system or marketing plan that is substantially determined, controlled, or suggested by the franchisor or the franchisor’s associate.⁶⁹ In *Capital Networks*, Bennet J conceded that the word ‘control’ was determinative of this component. The judge defined the term ‘control’ to mean the power to direct or restrain the content of the business plan on any substantial issue. According to Bennet J, practical and commercial considerations will determine the existence of the franchisor’s control.⁷⁰ The Federal Court has partly spelled out these considerations in the case *Rafferty and Another*. According to the Court, the matters relating to the franchisor’s control over a system or marketing plan include the franchisee’s involvement in selling the franchisor’s products, the degree of the franchisor’s responsibility for some centralized management and for uniform standards concerning quality, and the imposition of the franchisee’s obligation regarding advertising and promotional campaigns, to name a few.⁷¹

⁶⁶ The Code, cl. 5(1)(b).

⁶⁷ *Rafferty and Another v Madgwicks* [2012] 203 FCR 1 [171].

⁶⁸ *Capital Networks* (n 65) [102] – [104].

⁶⁹ The Code, cl. 5(1)(b).

⁷⁰ *Workplace Safety Australia Pty Ltd v Simple OHS Solutions Pty Ltd* [2015] NSWCA 84 [105] – [106].

⁷¹ *Rafferty and Another* (n 67) [174].

2.4.4 Use of a trademark, advertising or a commercial symbol

The use of the brand is the second component of a franchise agreement.⁷² The Code requires a franchise business to be substantially or materially associated with a trademark, advertising, or a commercial symbol owned, used, licensed, or specified by the franchisor or an associate of the franchisor.⁷³ In this case, a mere license to sell products associated with, for example, a trademark does not suffice to establish a franchise.⁷⁴ As can be seen, the Code permits a franchise business to be associated with several possible symbols. Despite this, it is said that most franchised businesses are identified with the franchisor's trademark.⁷⁵ In this respect, the definition of a trademark is provided by the Trade Marks Act 1995 (Cth). According to section 17 of the Act 1995, a trademark means a sign used, or intended to be used, to distinguish goods or services dealt with or provided in the course of trade by a person from goods or services so dealt with or provided by any other person.⁷⁶

2.4.5 Monetary considerations

The last essential element of a franchise agreement is monetary considerations. In concluding a franchise agreement, the Code requires a franchisee to pay or agree to pay an amount to a franchisor or a franchisor's associate before starting or continuing a franchise business.⁷⁷ The Code clarifies the term 'amount' by providing a non-exhaustive list of the payment. Under the Code, the payable amount can take the form of an initial capital investment fee, a payment for goods or services, a fee based on a percentage of gross or net income whether or not called a royalty or franchise service fee, and a training fee or training school fee.⁷⁸ It should be noted that the Code excludes four types of payment that are not regarded as the payable amount.⁷⁹ For example, a payment for goods and services supplied on a genuine wholesale basis does not constitute the amount under a franchise agreement.⁸⁰

72 Peter Buberis, *Australian Franchising Code of Conduct: A Critical Analysis with Current Case law* (Emerald Publishing 2020) 13.

73 The Code, cl. 5(1)(c).

74 Giles (n 62) 30.

75 Ibid 30.

76 According to section 6 of the 1995 Act, a sign includes the following or any combination of the following, namely, any letter, word, name, signature, numeral, device, brand, heading, label, ticket, aspect of packaging, shape, color, sound or scent.

77 The Code, cl. 5(1)(d). *See also Apple Computer Australia Pty Ltd v George Mekrizis and Ors* [2003] NSWSC 126 [307].

78 The Code, cl. 5(1)(d)(i) to (iv).

79 The Code, cl. 5(1)(d)(v) to (viii).

80 The Code, cl. 5(1)(d)(v).

2.4.6 Conclusions

In Australia, a franchise agreement can establish a franchise relationship. In making a franchise agreement, the Franchising Code of Conduct regulates particular elements of a franchise agreement. Under the Code, a franchise agreement must be an agreement in which the franchisor grants the franchisee the right to conduct the franchise business under a system or marketing plan substantially to be determined, controlled, or suggested by the franchisor or the franchisor's associate. The franchisee's business operation must substantially or materially be associated with a trademark, advertising, or a commercial symbol owned, used, licensed, or specified by the franchisor or an associate of the franchisor. In exchange for the right to a franchise business, the franchisee must pay or agree to pay an amount of money to the franchisor or an associate of the franchisor. These elements are integral parts of a franchise agreement in the sense that, if one of these components is absent, there will not be a franchise agreement in light of the Code.⁸¹

2.5 COMPARATIVE ANALYSIS

2.5.1 Introduction

The description sections show that the DCFR, the USA, and Australia have the franchise legal framework that defines a franchise to mean an agreement or contract with particular components. This section will juxtapose and discuss the essential elements of a franchise agreement that constitute a franchise relationship under the chosen legal systems' franchise legal framework in section 2.5.2. Section 2.5.3 will recapitulate the fundamental components of a franchise and offer key recommendations for defining a franchise for the sake of regulating a franchise relationship under comprehensive franchise law.

2.5.2 Comparison and discussion

2.5.2.1 Similarity

The DCFR, the USA, and Australia are similar in that the rules of franchise-specific law provide that a franchise is primarily established by a legally enforceable agreement or contract between a franchisor and a franchisee.⁸² The franchise rules of the selected legal systems similarly require a franchise agreement or contract to have the following three fundamental elements: (1)

81 *Capital Networks* (n 65) [119].

82 See sections 2.2.2, 2.3.2, and 2.4.2.

the grant of the right to conduct a franchise business, (2) the license to use the franchisor's marks in the operation of a franchise business, and (3) the payment of monetary consideration. The lack of these three components will not constitute a franchise relationship for franchise regulation.

– *Right to conduct a franchised business*

Firstly, a franchise agreement is an agreement by which the franchisor grants the franchisee the right to carry on the business of offering, selling, or distributing the franchisor's goods or services onto the market.⁸³ Concerning this element, the franchise rules of the DCFR, the USA, and Australia imply the element of the franchisor's control over the franchisee's conduct to maintain uniformity in marketing the franchisor's products. In other words, the selected legal systems' franchise rules require the franchisee to follow the franchisor's specific methods of conducting the franchise business. Under the DCFR, the franchisee is obliged to follow the franchisor's business method and reasonable instructions concerning the method.⁸⁴ In the USA, the federal and some state franchise-specific laws require the franchisee to operate a franchise business under the franchisor's control or assistance and the franchisor's marketing plan or system.⁸⁵ In Australia, the franchisee has to conduct a franchise business under the franchisor's system or marketing plan.⁸⁶

– *Right to use a franchisor's marks*

Secondly, a franchise agreement is an agreement by which the franchisor authorizes the franchisee to use the franchisor's marks in operating a franchise business. The authorized marks may vary from legal system to legal system. Under the DCFR, the franchisor has the right to use the franchisor's intellectual property rights, including trademarks, trade names, shop signs, logos, insignia, utility models, designs, copyrights and related rights, software, drawings, plan, and patents.⁸⁷ The US federal and state franchise legislation provides that the franchisee operates a franchise business that is identified or associated with the franchisor's trademark, service mark, trade name, logo, or other commercial symbols.⁸⁸ In Australia, the Franchising Code of Conduct requires the franchisee to conduct a franchise business that is substantially or materially associated with the franchisor's trademark, advertising, or a commercial symbol.⁸⁹

⁸³ See sections 2.2.3, 2.3.3, and 2.4.3.

⁸⁴ See subsection 2.2.3.1.

⁸⁵ See subsections 2.3.3.1 and 2.3.3.2.

⁸⁶ See section 2.4.3.

⁸⁷ See section 2.2.4.

⁸⁸ See section 2.3.4.

⁸⁹ See section 2.4.4.

– *Monetary considerations*

Thirdly, a franchise agreement is an agreement by which the franchisee pays or agrees to pay the franchisor monetary considerations in exchange for the franchisor's grant of the rights mentioned in the preceding italicized headings. Under the franchise rules of the selected legal systems, the franchisee's payment can take several forms. Typically, the franchisee's payment includes the payment of two types of franchise fees: (1) upfront or initial franchise fees and (2) ongoing franchise fees or royalties.⁹⁰ Moreover, the chosen legal systems agree that the franchisee must intend the payment of monetary considerations to remunerate the franchisor for granting the right to conduct a franchise business and the right to use the franchisor's marks. In this respect, a franchise agreement or contract will be regarded as a reciprocal contract under the DCFR, the USA, and Australia.

2.5.2.2 *Difference*

The fundamental components of a franchise agreement under the DCFR, the USA, and Australia are similar. Nevertheless, there are some differences among the selected legal systems. To be precise, the selected legal systems seem to differ in terms of a formality for the conclusion of a franchise contract, the concept of franchisee independence, and a community of interest. Elaborations on these disparities are to be provided in the following three italicized headings.

– *Formality*

Firstly, the DCFR differs from the US and Australian legal systems in that the franchise rules do not impose a formal requirement for concluding a franchise contract.⁹¹ The lack of formality might attribute to the fact that the DCFR regards the principle of freedom of contract as one of the underlying principles. Accordingly, the DCFR tries not to impose formal restrictions that would lessen parties' capacity to enjoy that freedom in making legal transactions.⁹² This idea underlies the rule in II. – 1:106(1) that allows a contract or other juridical act to be concluded in any form. Since the franchise rules do not provide otherwise, II. – 1:106(1) will apply; the franchisor and the franchisee can conclude a franchise contract in any form, including a verbal agreement. In any case, the DCFR permits a party to request a written document for evidence of the contract.

⁹⁰ See sections 2.2.5, 2.3.5, and 2.4.5.

⁹¹ See section 2.2.2.

⁹² Bar and Clive (n 6) 38.

Conversely, the US and Australian laws regulate the format of a franchise agreement. In this case, the franchisor and the franchisee must follow the formal requirement imposed by franchise-specific law rules of the USA and Australia. Nevertheless, the formality of making a franchise contract varies from country to country. In America, most franchise-specific statutes provide that a franchise agreement may take the form of an oral or written agreement. In four franchise regulating states, however, a franchise agreement must be made in writing.⁹³ In Australia, the Code provides that a franchise agreement can take the form of a verbal and written agreement. In terms of formality, I believe that the divergence in the formal requirement of a franchise agreement between the DCFR, the USA, and Australia is insignificant. As can be seen, the selected legal systems would allow the franchisor and the franchisee to conclude a franchise agreement orally or in writing.

– *Independence concept*

Secondly, the DCFR differs from the USA and Australia in that the DCFR adopts the element of franchisee independence explicitly. Under the DCFR, the franchisee will conduct a franchised business independently, meaning the franchisee will not be regarded as the franchisor's employee. Besides, the franchisee will conduct a franchised business on the franchisee's behalf and in the franchisee's name.⁹⁴ Contrariwise, the USA and Australia do not obviously mention the franchisee's independence notion in their franchise legislation.⁹⁵

However, it cannot be concluded that the concept of franchisee independence does not exist in these countries. Under the US legal system, courts acknowledge that franchisee independence is an essence of a franchise relationship.⁹⁶ Furthermore, in Australia, the Franchising Code of Conduct impliedly embraces this independence concept by excluding particular relationships that would reflect mandate relationships. For example, an employment relationship does not constitute a franchise relationship in light of the Code.⁹⁷ Thus, it

⁹³ See section 2.3.3.

⁹⁴ See subsection 2.2.3.2.

⁹⁵ There is an exception in the US state of Florida. Under Florida franchise misrepresentation law, a franchise is a contract or agreement wherein the franchisee is an independent business in the franchisor's distribution system. This element suggests that the law expressly recognizes the concept of independence. Nevertheless, most franchise-specific statutes in America do not insert this element into the definition of a franchise.

⁹⁶ See eg *Neptune TV & Appliance Service, Inc v Litton Microwave Cooking Products Div, Litton Systems, Inc*, 462 A2d 595, 598, 190 NJ Super 153 (NJ Super AD, 1983) 159; *California ARCO Distributors, Inc v Atlantic Richfield Co*, 204 Cal Rptr 743, 752, 158 Cal App 3d 349 (Cal App 2 Dist, 1984) 361; *Bush v National School Studios, Inc*, 407 NW2d 883, 891, 139 Wis2d 635 (Wis, 1987) 653; *People ex rel Dept of Transportation v Acosta*, 100 Cal Rptr 3d 669, 673, 178 Cal App 4th 762 (Cal App 3 Dist, 2009) 769.

⁹⁷ The Code, cl. 5(3)(a).

could be said that the USA and Australia adopt the notion of franchisee independence as a concept underlying a franchise relationship too.

– *Community of interest*

Thirdly, a handful of the franchise regulating states in America differs from other legal systems because they insert into the definition of a franchise the requirement of a community of interest.⁹⁸ In these jurisdictions, there must be a community of interest between a franchisor and a franchisee in a franchise business. In general, the concept of a community of interest pays attention to a shared financial interest in a franchise relationship instead of the franchisor's control exerted over the franchisee's business operation. Nevertheless, the element of a community of interest seems to be conceptual. In this respect, the expression needs crystallization by the courts. In practice, some state courts have enumerated some indicators of a community of interest. Some factors adopted by courts indirectly reflect the franchisor's control over the conduct of a franchise business, which is typically accepted by the remaining legal systems.

2.5.2.3 Discussion

A clear definition of a franchise would help demarcate what commercial relationships fall within the ambit of franchise regulation. Thus, I suggest that legal systems that aim to regulate a franchise in comprehensive franchise law define a franchise that will be subject to franchise regulation. Defining a franchise would metaphorically mark an entrance into regulating a franchise relationship to protect franchisees. This defining task would benefit from the comparison carried out in the preceding subsections as the DCFR, the USA, and Australia, show the adoption of a similar definition of a franchise with relatively comparable components. Therefore, following the commonality in defining a franchise, I propose that the rules of comprehensive franchise law define a franchise as follows.

- '(1) A franchise is a legal relationship established by a franchise contract.
- (2) A franchise contract is a contract in which the franchisor grants the franchisee
 - (a) the right to conduct a franchise business independently, following the franchisor's business method, and
 - (b) the right to use the franchisor's marks, including trademarks and trade names, in the operation of a franchised business. The franchisee pays or agrees to pay the franchisor monetary considerations in exchange for granting the rights mentioned in (a) and (b).
- (3) A franchise contract must be evidenced in writing; otherwise, a franchise contract is unenforceable.'

⁹⁸ See subsection 2.3.3.3.

From the proposal, I suggest in paragraph (1) that a franchise is a legal relationship created by a franchise contract. In this respect, a franchise contract is the backbone of a franchise relationship. Thus, a franchise relationship will be created on the condition that a franchise contract is legally formed by two parties: a franchisor and a franchisee. In general, the formation of a franchise contract will be subject to contract law rules concerning the formation of a contract, which would differ across jurisdictions. However, the comparison of the franchise legal framework of the DCFR, the USA, and Australia, demonstrates that the contents of a franchise contract and the formality of the conclusion of a franchise contract can be regulated by franchise-specific law. In my opinion, comprehensive franchise law should contain the rules regulating these two aspects of a franchise. The following two italicized headings will discuss the formal requirement for concluding a legally enforceable franchise contract and the essential elements of a franchise contract, respectively.

– *Legally enforceable franchise contract*

In terms of formality, I propose in paragraph (3) that the franchise rules require a franchise contract to be evidenced in writing. In other words, a franchise contract should be made in a written format and signed by the franchisor and the franchisee. This written format of a franchise contract could help protect a franchisee from being exploited by a franchisor because of the following two functions.

First, a written format serves a cautionary function.⁹⁹ According to Smits, this formality can help warn the parties that they are concluding an important or financially risky transaction.¹⁰⁰ In my opinion, this warning function suits the franchising context because purchasing a franchise is typically regarded as an investment of considerable sums. To be precise, purchasing a franchise requires a franchisee to pay a lot of money, which would cause the franchisee personal financial destruction. Thus, requiring a franchise contract to be made in writing would remind a potential franchisee of the terms and conditions under a proposed franchise contract. This formal requirement would encourage the franchisee to consult legal or financial advisors before entering into a franchise contract. For example, the franchisee may advise a financial consultant about financial terms in a written franchise agreement.

Second, a written format also serves an evidentiary function.¹⁰¹ Smits provides that this function will create certainty about the existence and contents of the parties' obligations, thereby reducing future disputes over the parties' agreement.¹⁰² In franchising, a franchise contract's terms are ordinarily intri-

99 Lon L Fuller, 'Consideration and Form' (1941) 41 Columbia Law Review 799, 800.

100 Jan M Smits, *Contract Law: A Comparative Introduction* (3rd edn, Edward Elgar 2021) 102.

101 Fuller (n 99) 800.

102 Smits (n 100) 102 – 03.

cate and extended; it usually includes a large number of contractual provisions. For example, a 7-Eleven individual store franchise agreement is a 36-page document containing 31 provisions, some of which have elaborate sub-clauses.¹⁰³ Accordingly, I suggest that a franchise contract is made in writing because a document can record all the terms and conditions of a franchise contract for future reference.

Besides, I propose that the failure to comply with the formality results in the unenforceability of a franchise contract. In light of contract law principles, the consequence of failing to comply with the formality can be twofold. On the one hand, the failure renders an agreement or contract invalid (*ad validitatem*). On the other hand, an agreement or contract not made in conformity with the formality remains valid but unenforceable (*ad probationem*).¹⁰⁴ As a matter of policy, comprehensive franchise law should opt for an *ad probationem* effect. In my view, legal systems should respect the parties' autonomy and strive to maintain the contract's sanctity.¹⁰⁵ Maintaining the validity of a franchise contract would enable a franchise model to drive the country's economy more efficiently.

Thus, I suggest that legal systems do not nullify a franchise contract merely because of non-compliance with the required formality. In other words, I advise that legal systems offer the parties an opportunity to correct an error in fulfilling a formal requirement, thereby maintaining a valid franchise relationship. If the franchisor and the franchisee conclude a franchise contract orally, the rules of comprehensive franchise law should provide that the contract is unenforceable. In this case, the parties may correct this unenforceability by documenting a franchise contract so that the contract is evidenced in writing and legally enforceable.

– Essential elements of a franchise contract

From the proposal, I propose in paragraph (2) that the rules of comprehensive franchise law enumerate three components of a franchise contract, which are common among the selected legal systems, as follows.

¹⁰³ The text of the standard form 7-Eleven individual store franchise agreement can be accessed at <<https://bit.ly/3qx169j>>

¹⁰⁴ Hugh Beale and others, *Cases, Materials and Text on Contract Law* (3rd edn, Hart Publishing 2019) 215-16; Jan M Smits, *Contract Law: A Comparative Introduction* (3rd edn, Edward Elgar 2021) 108.

¹⁰⁵ This policy embraces the autonomy theories that focus on the choice of contracting parties. According to Bix, the autonomy-theories view that the parties should be able to establish legally enforceable rights and obligations. In this case, the law, particularly contract law, should respect and enforce what the parties have chosen. See Brian H Bix, 'Theories of contract law' in Pier Giuseppe Monateri (ed), *Comparative Contract Law* (Edward Elgar Publishing 2017) 11.

(1) *The right to conduct a franchise business*

First, a franchise contract is a contract in which the franchisor grants the franchisee the right to conduct a franchise business, which is a business that aims at dispensing, offering, or selling the franchisor's goods or services onto the market. An essential attribute of a franchise business is that the franchisee distributes the franchisor's products to the market in a uniform manner. In this respect, the franchisor's control over the uniformity in a franchise network is regarded as a key element of franchising.¹⁰⁶ From the comparison, the DCFR, the US, and Australian franchise laws seem to exert the element that implies the franchisor's control over the franchise business operation in the definition of a franchise agreement. Thus, for the sake of uniformity, the rules of comprehensive franchise law should be explicit in the sense that the franchisee cannot conduct a franchised business on its own. Instead, the rules should require the franchisee to operate a franchised business under the franchisor's control over marketing or business plans.

The element of the franchisor's control under the chosen legal systems seems to be elusive. For example, the DCFR requires the franchisee to follow the franchisor's business method. Some US state franchise legislation and the Australian Franchising Code of Conduct require the franchisee to conduct a franchise business under a system or marketing plan. From my perspective, the expressions 'business method' and 'a system or marketing plan' are far from certain. Accordingly, in practice, a franchise agreement usually contains the terms specifically instructing a franchisee in operating a franchise business. In this regard, I suggest that the rules of comprehensive franchise law do not elaborate on the requirement of the franchisor's control over the franchisee's business operation. In other words, the rules may establish the element of the franchisor's control conceptually, as seen in paragraph 2(a). This establishment would allow the parties to elaborate on the franchisor's control so as to suit individual franchise businesses.

Although a franchisor has the power to control a franchisee's business operation, the rules of comprehensive franchise law should explicitly include the element of franchisee independence into a definition of a franchise. Taking the DCFR as an example, IV.E. – 4:101 expressly provides that the franchisee operates a franchise business on the franchisee's behalf and in the franchisee's name. For the sake of clarification, I suggest that the franchisee's independence should be understood in the following two aspects.

The first aspect of franchisee independence is that a franchisee will not conduct a franchise business as the franchisor's employee, mandatary, or agent. From a theoretical viewpoint, this component will distinguish a franchise contract from an employment, mandate, or agency contract to safeguard the franchisee against the franchisor's command over the day-to-day operation.

¹⁰⁶ Gary R Batenhorst, 'Franchisee Marketing' in Kenneth R Costello (ed), *Collateral Issues in Franchising: Beyond Registration and Disclosure* (American Bar Association 2015) 213.

In practice, this inclusion of this concept in defining a franchise is not unusual. For instance, in Australia, the Franchising Code of Conduct explicitly excludes some relationships, such as employment and partnership relationships, from a franchise relationship.¹⁰⁷

The second aspect is that a franchisee will conduct a franchise business as an independent business owner. This component is vital to ensure that a franchised business is not treated as a subsidiary of the franchisor's company. In this respect, the franchisee will independently secure and obtain financing for the opening and operation of a franchised business. This independent element will also make sure that the franchisee will independently take care of financial gains and losses from the franchised business operation. In the end, the franchisee will be provided with a glimpse of owning a business that encourages the franchisee to devote a great deal of effort to running the business.

(2) *Use of the franchisor's marks*

Second, a franchise contract is a contract in which the franchisor grants the franchisee the right to use the franchisor's marks in the operation of a franchised business. This element is the peculiarity of franchising because it marks an individual franchise business by creating a uniform appearance of all the franchised units in an individual franchise network. In other words, a unique designation of franchised stores would help customers distinguish the appearance and quality of the franchisor's products in the market from the others'. For instance, customers who visit McDonald's franchised outlets would expect that McDonald's hamburgers differ from those sold in Burger King's stores. Thus, the rule of comprehensive franchise law should require a franchised business to be designated by the franchisor's marks.

Additionally, the comprehensive franchise law rules should exemplify the expression 'franchisor's marks'. In my view, the franchisor's marks should primarily cover intellectual property rights that are employed to differentiate the franchisor's franchise business, such as trademarks and tradenames. In many legal systems, these IP rights are essentially recognized to distinguish goods and services of one undertaking from others'.¹⁰⁸ Thus, the DCFR, the USA, and Australia accept that the franchisor's marks include a trademark and tradename that the franchisor owns or is authorized to license others to use. In this case, therefore, the comprehensive franchise law rule should, at the

¹⁰⁷ The Code, cl. 5(3)(a)(b).

¹⁰⁸ Mark J Davison, Ann L Monotti, and Leanne Wisman, *Australian Intellectual Property Law* (3rd edn, Cambridge University Press 2016) 7; Arthur R Miller and Michael H Davis, *Intellectual Property: Patents, Trademarks, and Copyright in a Nutshell* (6th edn, St. Paul Minn 2018) 154-155; Richard Davis, *Tritton on Intellectual Property in Europe* (5th edn, Thomson Reuters 2020) 355.

very least, require a franchised business to be designated by the franchisor's trademark and tradename.

Furthermore, I suggest that the differentiation of a franchise business by other symbols, which are not IP rights *per se*, should be acceptable under the rules of comprehensive franchise law. As can be seen, the selected legal systems do not require a franchise business to be associated only with the franchisor's trademark and tradename. Taking the DCFR as an illustration, the drafters of the model law exemplify that, in the context of distribution and service franchises, the franchisee's business may relate to the franchisor's business name or symbol.¹⁰⁹ Thus, the comprehensive franchise law rule should permit a franchise business to be symbolized by other commercial names or symbols, such as logos, even though they are not recognized as IP rights. However, I advise that legal systems should have general rules that help designate that a franchisor is the right holder of these names or symbols.¹¹⁰

(3) *Monetary considerations*

Third, a franchise contract should be understood as a reciprocal contract. Thus, a franchise contract is a contract in which the franchisee agrees to remunerate a franchisor for the right to conduct a franchise business under a marketing or business plan prescribed by the franchisor and the right to use the franchisor's marks. In general, the remuneration should be regarded as monetary considerations, including upfront or initial fees and ongoing fees or royalties. The franchisee's remuneration should also be interpreted to cover other types of the franchisee's payment made in exchange for the grant of the rights. For example, the Australian Franchising Code of Conduct regards the payment for goods or services, as well as a training fee or training school fee, as a payable amount. The underlying reason for requiring flexible types of monetary consideration is to prevent the franchisor from setting any payment scheme to escape the regulation of comprehensive franchise law, which aims to be franchisee-oriented.

2.5.3 Conclusions

2.5.3.1 *Concluding remarks*

This section has described and juxtaposed how the franchise legal framework of the DCFR, the USA, and Australia defines 'franchise'. There is no uniformity

¹⁰⁹ Bar and Clive (n 3) 2384.

¹¹⁰ For example, in Thailand, section 18 of the Civil and Commercial Code recognizes that a person can be entitled to use a name. This rule could help avoid conflict over whether a franchisor has the authority to grant a franchisee the right to use a commercial name or symbol.

in defining a franchise under the chosen legal systems. However, the franchise legal framework of the DCFR, the USA, and Australia contemplates a franchise similarly; a franchise is a marketing relationship created by a franchise contract with three common elements.¹¹¹ Summarily, a franchise contract is an agreement in which the franchisor grants the franchisee the right to conduct a franchise business and the right to use the franchisor's marks in exchange for the franchisee's payment of monetary considerations. Distinctions between the chosen legal systems are slight and related to detailed requirements of making a franchise contract. Therefore, it is fair to say that the essential elements of a franchise contract adopted by the chosen legal systems are common and offer helpful guidelines for defining a franchise under comprehensive franchise law.

2.5.3.2 Key recommendations

(1) *Establishing a franchise relationship*

Comprehensive franchise law should accentuate that a legally enforceable franchise contract between a franchisor and a franchisee establishes a franchise relationship. In addition, comprehensive franchise law should provide that a franchise contract consists of the following three elements: (1) the grant of the franchisee's right to conduct a franchise business independently, following the franchisor's business method, (2) the grant of the franchisee's right to use the franchisor's marks, and (3) monetary considerations paid by the franchisee.

(2) *Right to conduct a franchise business*

A franchise contract is a marketing contract in which the franchisor grants the franchisee the right to conduct a business of offering, dispensing, or distributing the franchisor's goods or services onto the market. In this respect, the law should assert the element of the franchisor's control over the franchisee's business method. The law should also ensure that the franchisee enjoys independence in operating a franchised business.

(3) *Right to use the franchisor's marks*

A franchise contract is a marketing contract in which the franchisor grants the franchisee the right to use the franchisor's marks in a franchised business operation. In terms of interpretation, the franchisor's marks should primarily include using the franchisor's intellectual property rights, such as a trademark and tradename. In designating a franchisor's franchise business, the franchisor

¹¹¹ These components reflect the four cornerstones of franchising. Webber suggests that any franchise system should be based on the following four cornerstones of franchising: the franchise agreement, licensing, brand ownership, and fee structure. See Robert Webber, *An Introduction to Franchising* (Palgrave Macmillan 2013) 13-14.

should be permitted to license the franchisee to use other commercial names or symbols, which are not regarded as IP rights *per se*.

(4) *Monetary considerations*

A franchise contract is a marketing contract in which the franchisee pays or agrees to pay the franchisor monetary considerations to obtain the right to operate a franchise business and the right to use the franchisor's marks. These considerations may take several forms, including upfront or initial franchise fees and ongoing fees or royalties. The franchisee's payment should have the purpose of reciprocating the franchisor for a grant of the right to a franchise business.

(5) *Formality*

Comprehensive franchise law should regulate the formality of a franchise contract. In terms of a formal requirement, the law should require a franchise contract to be evidenced in writing. Strictly speaking, a franchise contract should be made in a written format, signed by the franchisor and the franchisee. Failure to comply with this formal requirement should render a franchise contract unenforceable.

2.6 CONCLUSIONS

Chapter two has explored the definition of a franchise under the franchise legal framework of the DCFR, the USA, and Australia and found no universally agreed definition of a franchise. In other words, the franchise legal framework of the chosen legal systems defines a franchise differently in detail. This second chapter has discovered that the DCFR, the USA, and Australia, contemplate a franchise similarly in that a franchise is a marketing relationship created by a franchise contract. In this case, chapter two has extracted common elements of a franchise contract, concluded by a franchisor and a franchisee, under the selected legal systems. In general, a franchise contract has the following three particular elements: (1) the franchisor's grant of the right to conduct a franchise business, (2) the franchisor's license to use the franchisor's marks, and (3) the franchisee's payment of franchise fees. These three components are considered the backbone of a franchise contract and should be adopted when defining a franchise under comprehensive franchise law.

3 Regulation of pre-contractual information obligations of the franchisor

3.1 INTRODUCTION

Contract law's operation usually does not reach the pre-contractual sphere. Accordingly, the parties in a contract negotiation typically incur no obligation to the other, particularly the duty to provide pre-contractual information.¹ This assumption holds true in the context of making a franchise contract. However, purchasing a franchise requires a considerable investment from a franchise purchaser. In this case, it would be imperative for a prospective franchisee to be provided with material and qualified information to make a well-informed decision on whether to enter into a franchise contract with a franchisor. As will be seen, the Draft Common Frame of Reference (DCFR), the United States of America (USA), and Australia have established the franchise legal framework regulating a pre-contractual relationship between a franchisor and a prospective franchisee. One of the most intriguing features of these legal frameworks is the regulation of the franchisor's pre-contractual information duties. This regulatory aspect will be the subject of the examination of chapter three.

The third chapter will examine the franchise legal framework of the DCFR, the USA, and Australia to answer the three sub-research questions developed in chapter one.² Section 3.2 will explore the chosen legal systems' franchise legal framework to explore how a franchisor is required to provide a prospective franchisee with material information about a franchise before concluding a franchise contract. Then, section 3.3 will examine how the franchise legal framework of the chosen legal systems requires a franchisor to ensure the currency and truthfulness of the pre-contractual information. Next, section 3.4 will explore the potential private law remedies that permit an aggrieved franchisee to compel the franchisor's performance, claim monetary compensation, and cancel a franchise contract in the case of contravention of the regula-

1 For the sake of clarity, this chapter will synonymously use the terms 'obligation' and 'duty'. In other words, these two terms will be used interchangeably, meaning action or inaction that a person is legally bound to perform towards the other person.

2 See section 1.5.2 in chapter one.

tion of the franchisor's pre-contractual information duties.³ In the end, section 3.5 will conclude on the findings of chapter three.

3.2 DUTY OF PRE-CONTRACTUAL DISCLOSURE

3.2.1 Introduction

As mentioned in the introduction, the DCFR, the USA, and Australia have the franchise legal framework regulating the franchisor's pre-contractual duties. Among other things, these legal frameworks regulate the franchisor's pre-contractual disclosure obligation. In this chapter, a disclosure obligation should be understood as an obligation to provide information before the conclusion of a franchise contract. Section 3.2 will focus on the construction of the franchisor's pre-contractual duty of disclosure. This section will examine franchise-specific law rules regulating the franchisor's duty of pre-sale disclosure under the three legal systems in sections 3.2.2, 3.2.3, and 3.2.4, respectively. Section 3.2.5 then juxtaposes and discusses the chosen legal systems' approaches to regulating the pre-contractual disclosure obligation to develop guidelines for formulating franchise rules regulating the franchisor's disclosure duty under comprehensive franchise law.

3.2.2 The Draft Common Frame of Reference (DCFR)

3.2.2.1 Introduction

The DCFR regulates the franchisor's disclosure duty through two model rules on pre-contractual information duties in Part E of Book IV. According to IV.E. – 2:101, in conjunction with IV.E. – 4:102(1), a franchisor has an obligation to provide a prospective franchisee with specific pre-contractual information items a reasonable time before a franchise contract is concluded. This requirement aims to enable the prospective franchisee to enter into the contract with full knowledge of all relevant facts.⁴ Consequently, this pre-contractual obligation is mandatory and cannot be excluded by agreement.⁵ This section will break down the franchisor's obligation into six elements and examine all the com-

3 For the sake of clarity, this chapter intends the phrase 'cancelling a franchise contract' to mean putting an end to a franchise relationship utilizing certain legal mechanisms. After a franchise contract is legally canceled, a franchise relationship will be dissolved or annulled.

4 Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.3, Oxford University Press 2010) 2387.

5 The DCFR, IV.E. – 4:102(3).

ponents of the obligation in subsection 3.2.2.2. Subsection 3.2.2.3 will conclude on the contents and nature of the franchisor's pre-sale disclosure duty.

3.2.2.2 Elements of the pre-contractual information duty

– Provider of pre-contractual information

According to IV.E. – 4:102(1), the franchisor is obliged to provide the prospective franchisee with pre-contractual information enumerated in this article. Thus, the franchisor is a pre-contractual information provider in light of IV.E. – 4:102. As examined in chapter two, the DCFR does not explicitly define the term 'franchisor'.⁶ In this case, the franchisor can impliedly be defined to mean a party to a franchise contract who grants the franchisee the right to conduct a franchise business and the right to use the franchisor's intellectual property rights, know-how, and business method, in exchange for remuneration.

Although the franchisor assumes the obligation to provide pre-contractual information under IV.E. – 4:102, the franchisor is not obliged to perform the obligation in person. In other words, this pre-contractual information duty may be performed by a third person. Under the DCFR, III. – 2:107 permits the performance of a non-personal obligation by a third person. In my view, the duty of disclosure in the pre-contractual phase is inherently not a personal obligation and is assignable. Thus, according to paragraph (1)(a) of III. – 2:107, the franchisor may assign other persons, such as the franchisor's representative, agent, and employee, to act on its behalf in providing the prospective franchisee with the required pre-contractual information. In this case, the franchisor's pre-contractual information duty will be discharged by the due performance of those third persons by virtue of III. – 2:107(2).

– Contents of pre-contractual information

As can be seen, the DCFR requires the franchisor to provide qualified information peculiar to a franchise business.⁷ In this case, IV.E. – 4:102(1) delineates the qualified information by enumerating a list of eight disclosure items. These eight disclosure items are items of information concerning (1) the franchisor's company and experience, (2) the relevant intellectual property rights, (3) the characteristics of the relevant know-how, (4) the commercial sector and the market conditions, (5) the particular franchise method and its operations, (6) the structure and extent of the franchise network, (7) the fees, royalties or any other periodical payments, and (8) the terms of the franchise contract. The scope of each item of information is further elaborated by the drafters of the DCFR in Comment C to IV.E. – 4:102. For example, the drafters provide that

⁶ See section 2.2.2 in chapter two.

⁷ Bar and Clive (n 4) 2388.

information about the terms of the contract should include the rights and obligations of the respective parties, the duration of the agreement, the fee system, the conditions for termination and the renewal of the contract, economic considerations, exclusivity arrangements, and restriction on the free disposal of the business by the franchisee.⁸

It should be noted that the disclosure of the eight pre-contractual information items is a minimum requirement. This statement has three implications. First, the franchisor cannot provide less information than that required by IV.E. – 4:102(1).⁹ Second, the franchisor may be required to provide the prospective franchisee with more information. According to IV.E. – 2:101, the franchisor may be required to provide additional information items, provided that good commercial practice requires the franchisor to do so.¹⁰ For example, the franchisor may have to furnish the franchisee with information about litigation history. The reason is that the franchisor's involvement in any legal proceeding can substantially influence the franchisee's investment decision.¹¹ Third, the franchisor may, by its initiative, give the prospective franchisee additional information items that reasonably inform the franchisee about a franchise. This assertion can be deduced from IV.E. – 2:101, providing that a party who is engaged in negotiation for a franchise contract has a duty to provide the other party with information that is sufficient to enable the other party to decide to enter into the contract on a reasonably informed basis.

– *Format of pre-contractual information*

The DCFR imposes no formality in disclosing pre-contractual information. Neither IV.E. – 2:101 nor IV.E. – 4:102 requires any specific format of the franchisor's disclosure of pre-sale information. Additionally, the drafters of the DCFR do not mention the formality of the disclosure in the pre-contractual phase. According to III. – 2:105(1), therefore, the franchisor may choose to provide the franchisee with the required pre-contractual information orally or in writing.¹² For example, the franchisor may decide to provide the

⁸ Ibid 2390.

⁹ Ibid 2388.

¹⁰ Neither IV.E. – 2:101 nor its commentaries define 'good commercial practice'. Thus, this phrase opens room for courts to construct on a case-by-case basis, taking into account the usages in particular businesses.

¹¹ If considering some European franchise regulations, it is not unusual for a franchisor to be obliged to disclose a history of legal proceedings. For instance, the Italian franchise law requires the franchisor to provide a short description of any final court or arbitration proceedings concerning the franchise system commenced against the franchisor and concluded during the last three years. See The Law No.129/2004, article 4(f).

¹² Notes IV to IV.E. – 4:102 show that the DCFR differs from the UNIDROIT Model Law, as well as franchise-specific law of some European countries, such as France, Italy, and Spain, in that those legal systems require the franchisor to furnish the information in writing. See Bar and Clive (n 4) 2392-393.

prospective franchisee with a disclosure document containing the required items of pre-contractual information. The franchisor may choose to give the franchisee the disclosure document in a paper or digitized format.

– *Delivery of pre-contractual information*

Neither the model rules of the DCFR nor their commentaries specify a method for delivering pre-contractual informational items to a prospective franchisee. In this case, it could be said that the franchisor has discretion in selecting a means for furnishing the prospective franchisee with the required items of pre-contractual information. Thus, the delivery methods can be manifold, which ordinarily relates to the disclosure format chosen by the franchisor. Assume that the franchisor chooses to give the franchisee a digitized disclosure document containing pre-contractual information items. In this case, the franchisor may decide to deliver the digitized document to the franchisee via email. Alternatively, the franchisor may ask the franchisee to download the digital file of a disclosure document through the franchisor's website.¹³ In other cases, the franchisor may choose to provide the franchisee with pre-contractual information verbally if it is plausible to do so. In this case, the franchisor may disseminate the information by phone or at an in-person meeting with the franchisee.

– *Timing for disclosing pre-contractual information*

The DCFR sets an indefinite period for disclosing the required pre-contractual information. According to IV.E. – 2:101, the franchisor shall perform a pre-contractual information obligation within a reasonable time before concluding a franchise contract. Since the reasonableness is indiscernible, the drafters of the DCFR provide that a court can decide if the franchisor provides pre-contractual information in a reasonable time by considering the circumstances of the case or any applicable usage.¹⁴ More importantly, the franchisor should allow the franchisee to have sufficient time to process the information given and decide whether to enter into a franchise contract. However, whether the timing is sufficient must be decided on a case-by-case basis. In European countries that regulate a franchise, the time frame for the disclosure of pre-contractual information ranges from 20 days to one month. For example, Italy adopts a period of 30-day, while France and Spain opt for a 20-day period.

13 It should be mentioned that the DCFR does not contain model rules regulating the electronic transmission of information.

14 Bar and Clive (n 4) 2287.

Belgium requires a one-month period for the disclosure.¹⁵ Additionally, the UNIDROIT Model Law sets a 14-day period for the disclosure timing.¹⁶

– *Recipient of pre-contractual information*

According to IV.E. – 4:102(1), a franchisee is a person with whom a franchisor must provide the required pre-contractual information. Although IV.E. – 4:102(1) uses the word ‘franchisee’, the term should not be taken literally because no franchise agreement has been concluded at the time of the disclosure of pre-sale information. The term ‘franchisee’ should be understood as a prospective franchisee, not as an actual franchisee. Nevertheless, IV.E. – 4:102 does not define the word ‘prospective franchisee’. Despite the lack of definition, the drafters of the DCFR seem to conceive a ‘prospective franchisee’ as a person who approaches a franchisor for the right to conduct a franchise business and will conclude a franchise contract with the franchisor.¹⁷ However, the drafters of the DCFR do not provide criteria for determining the point at which a prospective franchisee legally exists in light of IV.E. – 4:102(1). The lack of criteria will pose several questions. For example, a question arises whether the franchisor has to provide pre-contractual information to a person who reaches the franchisor by phone for information about a franchise.

3.2.2.3 Conclusions

Under the DCFR, Part E of Book IV is the legal framework that establishes the franchisor’s duty to provide pre-contractual information. This disclosure duty is mandatory and aims to ensure that a prospective franchisee has full knowledge of facts before entering into a franchise contract. In Part E, the franchisor is required to provide the prospective franchisee with a minimum of eight information items at a reasonable time prior to the conclusion of a franchise contract. These informational items are essentially pieces of information relevant to a franchisor and a franchise business. The DCFR does not impose formality in disclosing the required pre-contractual information. Therefore, the franchisor is free to choose the disclosure format and a means for disseminating the information.

15 Mark Abell, ‘The regulation of franchising in EU Member States’ (2012) 10(2) International Journal of Franchising Law 17, 19-24.

16 The UNIDROIT Model Law, Art. 3.

17 Bar and Clive (n 4) 2387-390.

3.2.3 The United States of America (USA)

3.2.3.1 Introduction

In America, federal and state franchise sale laws regulate the initial phase of a franchise relationship. At the national level, the Federal Trade Commission promulgates the Disclosure Requirements and Prohibitions Concerning Franchising (FTC Rule) as the federal legislation applying throughout the country. At the state level, sixteen states (franchise sale states) have enacted state franchise sale law to regulate pre-sale conduct in franchising.¹⁸ These state statutes apply in the states on the condition that the laws are inconsistent with the FTC Rule. In case of inconsistency, it must afford franchisees equal or greater protection.¹⁹ As will be seen, the federal and franchise sale legislation of fifteen franchise sale states imposes on the franchisor the duty of disclosure.²⁰ This section will break down the franchisor's obligation under the federal and state franchise sale laws into six elements and examine all the elements in subsection 3.2.3.2. Subsection 3.2.3.3 will summarize the contents and nature of the franchisor's pre-contractual information duty under the US legal system.

3.2.3.2 Elements of the pre-contractual information duty

– Provider of pre-contractual information

(1) Federal Law

The FTC Rule requires a franchisor to prepare and disclose pre-contractual information to a prospective franchisee. The federal regulation defines the term 'franchisor' to mean a person who grants a franchise and participates in the franchise relationship. Thus, the franchisor's employee, representative, agent, and broker are generally not regarded as franchisors and not required to prepare and provide pre-sale disclosures to the potential franchisee.²¹ Nevertheless, the FTC Rule requires these third persons to give the prospective franchisee pre-sale information in exceptional cases. Under the FTC Rule, section

18 Those states are: California, Florida, Hawaii, Illinois, Indiana, Maryland, Michigan, Minnesota, New York, North Dakota, Oregon, Rhode Island, South Dakota, Virginia, Washington, and Wisconsin.

19 72 FR 15462 (March 30, 2007). It should be noted that twenty-five states have their business opportunities law that may apply to pre-contractual franchise relationship. For example, Alaska has the sale of business opportunities statute that require the disclosure of pre-contractual information. See AK ST § 45.66.080. Arizona has the trade and commerce law requiring the pre-sale disclosure. See AZ ST § 44-1276.01.

20 Franchise sale law of Florida does not contain disclosure rules because it only regulates misrepresentation in selling a franchise. See FL ST § 817.416.

21 72 FR 15462 (March 30, 2007).

436.9(e) provides that a franchise seller has to provide a prospective franchisee with the franchisor's copy of a disclosure document earlier in the sales process than required under the Rule, upon reasonable request. Section 436.1(j) defines the 'franchise seller' to mean a person who offers for sale, sells, or arranges for the sale of a franchise. In particular, the franchise seller is defined to include the franchisor's employee, representative, agent, and third-party broker involved in the activities of franchise sales. Thus, these third persons have to disclose pre-sale information in the case of earlier disclosure upon request.

(2) *State laws*

In fifteen franchise sale states, a franchisor is similarly responsible for making certain disclosures.²² Franchise sale law of all states defines the term 'franchisor' to mean a person who grants a franchise.²³ However, in some states, third persons may be held responsible for making pre-contractual disclosures. For example, in California, Glen said that a franchise broker must give each potential franchisee a copy of the entire disclosure document under the California Franchise Investment Law.²⁴ However, Glen does not elaborate on the expression 'must'. Thus, it might be questioned whether a franchise broker is legally required to provide a prospective franchisee with the franchisor's franchise disclosure document. In any case, the Californian court and other commentators interpreted that the franchise investment law only requires the franchisor to provide the prospect with a disclosure document.²⁵

22 California: CA CORP, § 31119(a); Hawaii: HI ST, § 482E-3(a); Illinois: IL ST CH 815, § 705/5(2); Indiana: IN ST, 23-2-2.5-9(2); Maryland: MD BUS REG, § 14-223 and 216; Michigan: MI ST, 445.1508(1); Minnesota: MN ST, § 80C.06(Subd.5); New York: NY GEN BUS, § 683(1); North Dakota: ND ST, 51-19-08(1); Oregon: OR ADC, 441-325-0020(2); Rhode Island: RI ST, § 19-28.1-8(a); South Dakota: SD ST, § 37-5B-17(1); Virginia: VA ST, § 13.1-563, in conjunction with § 13.1-565, and 21 VA ADC, 5-110-55; Washington: WA ST, 19.100.080(1); Wisconsin: WI ST, 553.27(4).

23 California: CA CORP, § 31007; Hawaii: HI ST, § 482E-2; Illinois: IL ST CH 815, § 705/3; Indiana: IN ST, 23-2-2.5-1; Maryland: MD BUS REG, § 14-201; Michigan: MI ST, 445.1502; Minnesota: MN ST, § 80C.01; New York: NY GEN BUS, § 681; North Dakota: ND ST, 51-19-02; Oregon: OR ST, § 650.005; Rhode Island: RI ST, § 19-28.1-3; South Dakota: SD ST, § 37-5B-1; Virginia: VA ST, § 13.1-559; Washington: WA ST, 19.100.010, and Wisconsin: WI ST, 553.03

24 Robin Day Glenn, 'Chapter 1: Franchises' in Alan S Gutterman, *California Transactions Forms Business Transactions*, at § 1:16, Westlaw, March 2020 Update.

25 *Migliore v Dental Fix Rx, LLC*, 2016 WL 7655768 (CD Cal, 2016) 1; Douglas L Carden and Phyllis Alden Truby, 'California' in W Michael Garner (ed), *Franchise Desk Book: Selected State Laws, Commentary and Annotations* (Vol 1, 3rd edn, American Bar Association 2019) at CA-117.

– Contents of pre-contractual information

(1) Federal law

The FTC Rule imposes on a franchisor an obligation to furnish a prospective franchisee with its current disclosure document (FDD).²⁶ According to section 436.5, the franchisor shall disclose twenty-three individual items of information in the FDD. These twenty-three disclosure items are information concerning the franchisor, the franchise system, the franchise business, and the terms of a franchise contract.²⁷ Each item is broken down into bite-sized pieces of pre-sale information. For example, the franchisor is required to include item three in the FDD, furnishing information about litigation relating to the franchisor and other specified persons.²⁸ In disclosing this item, the franchisor must elaborate on the litigation history, including pending actions, past actions involving the franchise relationship, convictions during the past ten years, as well as injunctions and restraining orders.²⁹

In principle, the franchisor must respond to all the required items affirmatively. The franchisor must state negatively if the information items are inapplicable.³⁰ It should be noted that the list of twenty-three informational items is inclusive. According to section 436.6(d) of the FTC Rule, the franchisor is prohibited from providing any information other than those required or permitted by the FTC Rule or state franchise law not preempted by the Rule. This prohibition is said to ensure that the franchisor will not furnish the potential franchisee with any non-material, confusing, or distracting information in the FDD, such as testimonials or general promotional information, by claiming that the provision of this information is not expressly prohibited by the laws.³¹

(2) State laws

Providing material information required by the FTC Rule is also obligatory in the sale states. For example, in Illinois and Oregon, a franchisor shall prepare the disclosure statement following the FTC Rule's requirements.³² It means that the franchisor must provide twenty-three items of information in the state disclosure document. In some states, the franchisor may be required

26 16 CFR, § 436.2(a).

27 David W Oppenheim and Rebekah Prince, 'Chapter 3: Franchise Disclosure Issues' in Ropert M Barkoff and others (eds), *Fundamentals of Franchising* (4th edn, American Bar Association 2016) 98.

28 16 CFR, § 436.5(c).

29 Brett Lowell, 'Chapter 9: Disclosure' in Alexander M Meiklejohn (ed), *Franchising: Cases, Materials, & Problems* (American Bar Association 2013) 406-07.

30 The analysis of section 436.6(c) provides an example that if the franchisor has no history of litigation, the franchisor could state that: "The franchisor has no litigation required to be disclosed by Item 3." See 72 FR 15515 (March 30, 2007).

31 72 FR 15515-15516 (March 30, 2007).

32 Illinois: IL ST CH 815, § 705/16 and Oregon: OR ADC, 441-325-0020(1).

to disclose additional, state-specific information in the disclosure document.³³ For instance, in California, the administrative regulation requires the disclosure statement to include additional paragraphs to item 17 required by the FTC Rule.³⁴ The extended paragraphs shall mention that the California Franchise Relations Act provides the franchisee's rights concerning termination and non-renewal. If a franchise contract contains terms that are inconsistent with the law, the law will override the contract's terms.³⁵

– *Format of pre-contractual information*

(1) *Federal law*

The FTC Rule sets a format of the pre-sale information disclosure. Under the FTC Rule, a franchisor must disclose pre-sale information in the form of the franchise disclosure document or FDD.³⁶ In formatting the FDD, the FTC Rule imposes a formal requirement that the franchisor must ensure the accessibility and the durability of the FDD.³⁷ First, the franchisor must organize the required information items clearly, legibly, and concisely in one document using plain English. According to section 436.1(o), the expression 'plain English' is defined to mean the organization of information and language usage, which is understandable by people unfamiliar with the franchise business. Second, the FDD format must permit a prospective franchisee to store, download, print, or otherwise maintain the document for future reference. In this case, the franchisor cannot provide the FDD in the form of video presentations or transmit the FDD through the internet in a format that is incapable of being downloaded or printed out.³⁸

33 It is claimed that eleven franchise sale states require some specific addenda in the disclosure document. Those states are California, Hawaii, Illinois, Maryland, Michigan, Minnesota, New York, North Dakota, Rhode Island, Virginia, and Washington. See John R F Baer, 'Chapter 10: State Franchise Sales Laws' in Alexander M Meiklejohn (ed), *Franchising: Cases, Materials, & Problems* (American Bar Association 2013) 480.

34 The FTC Rule sets item 17 to disclose information about contractual provisions addressing renewal, termination, transfer, and dispute resolution.

35 10 CA ADC, § 310.114.1(c)(5).

36 As of 1 July 2008, the franchisor is required to prepare the FDD, following the instructions set forth in Subpart C and D of the FTC Rule. According to section 436.6(a) of the FTC Rule, the franchisor's failure to follow those instructions would be regarded as an unfair or deceptive act in light of the FTC Act. Thus, to assist a franchisor in preparing the FDD, the Federal Trade Commission has issued the Franchise Rule Compliance Guide (Compliance Guide), which includes a part of the overview of the disclosure document. This part provides explanations and samples for each item of information required by the FTC Rule. The electronic version of the Compliance Guide can be accessed at <<https://bit.ly/3dARHoZ>>.

37 16 CFR, § 436.6(b).

38 16 CFR, § 436.6(d) and 72 FR 15515 (March 30, 2007).

(2) *State laws*

State franchise sale laws similarly require a franchisor to furnish pre-sale information documentarily. Under the state statutes, a disclosure document may be called differently, such as a disclosure statement, offering prospectus, and an offering circular. Nevertheless, the disclosure states can no longer depart from the FTC Rule format since the FTC Rule's requirements concerning the preparation of a disclosure document are mandatory.³⁹ Thus, the franchisor has to follow the FTC Rule's instructions when preparing the disclosure document unless the state legislation imposes additional, specific requirements for formatting the document.

– *Delivery of pre-contractual information*

(1) *Federal law*

The FTC Rule does not specify delivery methods. In this respect, the franchisor may choose several means of furnishing the FDD to a prospective franchisee. The franchisor can mail a hard copy of the FDD to the prospect.⁴⁰ Furthermore, the franchisor may transmit the FDD by electronic means. In the latter case, there are three different options for the franchisor. That is, the franchisor may (1) email a PDF file of the FDD to the prospective franchisee, (2) send a CD-ROM with a PDF file of the FDD to the prospective franchisee, and (3) give the prospective franchisee access to a website containing the FDD.⁴¹ In these three cases, the franchisor must ensure that the digitized document permits the prospective franchisee to store, download, print, or otherwise maintain the document for future reference.⁴²

(2) *State laws*

The state sale statutes do not differ from the FTC Rule. A franchisor is free to select a delivery method for furnishing a disclosure document. Some franchise sale states closely regulate some specific means of transmission. Taking California as an illustration, the franchise investment statute explicitly provides that a franchisor is not prevented from furnishing a copy of an offering circular to prospective franchisees through electronic means.⁴³ Nevertheless, the California administrative regulation contains the rule regulating pre-sale disclosure by electronic means.⁴⁴ According to the rule, the franchisor may deliver a disclosure document over the internet, or by other electronic means,

39 Baer (n 33) 469.

40 Oppenheim and Prince (n 27) 123.

41 Baer (n 33) 483.

42 16 CFR, §436.6(b).

43 CA CORP, § 31119(b).

44 10 CCR, § 310.114.4.

or in machine-readable media. However, the franchisor has to follow some requirements when disseminating the disclosure document electronically.⁴⁵

– *Timing for disclosing pre-contractual information*

(1) *Federal law*

The FTC Rule provides that the franchisor has to furnish a prospective franchisee with a copy of the current disclosure document at least 14 calendar days before the prospective franchisee signs a binding agreement with the franchisor or makes any payment to the franchisor or an affiliate in connection with the proposed franchise sale.⁴⁶ The count of a 14-day period will be triggered when the disclosure document is delivered to the prospective franchisee. In this case, the franchisor can sign a franchise contract, or the prospective franchisee can make the payment on the fifteenth day after the delivery date. In case a paper or tangible electronic copy of the disclosure, such as CD-ROM, was sent to the potential franchisee by first-class United States mail, the franchisor must add additional three calendar days to the waiting 14-day period.⁴⁷ This requirement is claimed to ensure that the prospective franchisee will have some time to review the disclosures.⁴⁸

Upon a reasonable request, a franchisor may be required to make an earlier disclosure than the 14-day standard. According to section 436.9(e), it is an unfair or deceptive act or practice for the franchisor to fail to furnish a copy of the franchisor's disclosure document to a potential franchisee earlier in the sales process than the period of 14-day if the potential franchisee makes a

⁴⁵ Those requirements are as follows.

First, before the delivery, the franchisor is required to advise the potential franchisee of the formats in which the document is available and any prerequisites or conditions necessary for receiving or reviewing it in a particular form.

Second, the franchisor must prepare the disclosure document that conforms with the requirements of law, and that has no extraneous content beyond what is required or permitted by the law except for the sole purpose of enhancing the prospective franchisee's ability to maneuver through the digitized document. In any case, all other features are prohibited, including audio, video, 'pop-up' screens, and links to external documents.

Third, the franchisor must deliver the disclosure document as a single, integrated document or file. In this case, the franchisor must furnish the document or file in the form that intrinsically enables the recipient to store, retrieve, and print the document.

Fourth, the franchisor must be able to prove that it electronically delivers the disclosure document in compliance with the rule. The franchisor must also keep records of the electronic delivery of the document and make those records available on demand by the Department of Business Oversight.

⁴⁶ 16 CFR, § 436.2(a).

⁴⁷ 16 CFR, §436.2(c)(3).

⁴⁸ 72 FR 15469 (March 30, 2007).

reasonable request.⁴⁹ In the section-by-section analysis of part 436, the Federal Trade Commission provides that the reasonableness of the request will be assessed on a case-by-case basis, taking into account the timing and manner in which the request is made. In this respect, the Commission has exemplified some instances of an unreasonable request. For example, it may be unreasonable for a potential franchisee to request a disclosure document by leaving a message with the doorman at the franchisor's headquarters.⁵⁰

(2) *State laws*

The timing for disclosure under state franchise sale laws is similar to that of the FTC Rule. In seven franchise sale states, the law requires the franchisor to provide the prospective franchisee with a disclosure document at least 14 days before the execution of a franchise agreement or the receipt of any consideration by the franchisor.⁵¹ The remaining jurisdictions adopt a shorter period than 14 calendar days.⁵² For example, in Indiana, Michigan, and New York, the franchisor is required to provide a prospective franchisee with a disclosure document at least ten days before the execution of a binding franchise contract by the prospective franchisee or before the receipt of any consideration by the franchisor.⁵³ However, this lesser time requirement is no longer valid since the FTC Rule has preempted the state laws.⁵⁴ Therefore, in those states, the franchisor must furnish the potential franchisee with a copy of the disclosure document at least 14 calendar days before the execution of a binding franchise contract by the prospective franchisee or before the receipt of any consideration by the franchisor.

As mentioned previously, a franchisor may have to disclose pre-sale information earlier than 14 days. Upon a reasonable request, the franchisor is required to furnish the potential franchisee with the disclosure document earlier in the sales process than 14 days. This conclusion results from the fact

49 This requirement aims to prevent the prospective franchisee's loss by enabling the prospect to review the franchisor's disclosure document before committing itself to pay money to advance the sale, such as travel costs to visit the headquarters of the franchisor. See 72 FR 15532 (March 30, 2007).

50 72 FR 15532 (March 30, 2007).

51 California: CA CORP, § 31119(a); Illinois: IL ST CH 815, § 705/5(2); Maryland: MD BUS REG, § 14-223 and 216; Oregon: OR ADC, 441-325-0020(2); Rhode Island: RI ST, § 19-28.1-8(a)(2); Washington: WA ST, 19.100.080(1); Wisconsin: WI ST, 553.27(4).

52 Hawaii: HI ST, § 482E-3(a); Indiana: IN ST, 23-2-2.5-9(2); Michigan: MI ST, 445.1508(1); Minnesota: MN ST, § 80C.06(Subd.5); New York: NY GEN BUS, § 683(8); North Dakota: ND ST, 51-19-08(6); South Dakota: SD ST, § 37-5B-17(2); Virginia: VA ST, § 13.1-565(3).

53 It should be noted that the franchise sale statute of Michigan and New York expressly adopt the standard of 'business' days.

54 Susan Grueneberg, 'Chapter 9: Inbound Transactions: Introducing a Non-U.S. Franchise Program to the United States' in Will K Woods (ed), *Fundamentals of International Franchising* (2nd edn, American Bar Association 2013) 343; Warren Lee Lewis, 'Chapter 1: Overview of the FTC Rule and Related Authorities' in Susan Grueneberg and Ann Hurwitz (eds), *The FTC Franchise Rule* (3rd edn, American Bar Association 2019) 11.

that the FTC Rule is also applicable in the disclosure states.⁵⁵ In New York, the franchisor may also be required to make an early disclosure in the case of the first face-to-face meeting.⁵⁶ Under the first face-to-face meeting rule, the franchisor must provide the prospective franchisee with a disclosure document at the earlier of the first face to face meeting between the franchisor and the prospective franchisee, which is held for the purpose of discussing the sale of a franchise.⁵⁷

– *Recipient of pre-contractual information*

(1) *Federal law*

The FTC Rule sets a prospective franchisee as a recipient of a disclosure document. The Rule defines a prospective franchisee to mean any person (including any agent, representative, or employee) who approaches or is approached by the franchise seller to discuss the possible establishment of a franchise relationship.⁵⁸ As can be seen, the FTC Rule permits the franchisor to make the agency disclosure. That is, the provision of the franchisor's disclosure document can be made to an agent, representative, or employee of the prospective franchisee. In this case, it is suggested that there must be the existence of a formal relationship between a representative and principal or the establishment of a fiduciary relationship by law, rules, or codes of conduct.⁵⁹ Besides, a franchisor has to disclose pre-contractual information to a prospective franchisee, who is already in the sales process. In other words, the franchisor has no duty towards any person who approaches the franchisor just for some general information.⁶⁰

(2) *State laws*

State franchise sale laws provide that a franchisor must provide a prospective franchisee with a disclosure document.⁶¹ No state laws define the term 'pros-

55 Some franchise sale states, such as Maryland, may explicitly duplicate the FTC Rule's requirement in their sale statute. See MD BUS REG, § 14-223(3).

56 The first meeting rule was adopted in Rhode Island. However, the state has abandoned this requirement since 2016. Therefore, New York is currently the only disclosure jurisdiction that has adopted the first meeting rule.

57 NY GEN BUS, § 683(8).

58 16 CFR, § 436.1(r).

59 Mary Beth Warman and Joel R Buckberg, 'Chapter 4: Delivery and Updating' in Susan Grueneberg and Ann Hurwitz (eds), *The FTC Franchise Rule* (3rd edn, American Bar Association 2019) 92.

60 72 FR 15532 (March 30, 2007).

61 In Virginia, section 13.1-559 of the Retailing Franchise Act requires that a disclosure document must be furnished to a 'franchisee'. This stipulation seems to be slightly confusing since the law defines the term 'franchisee' to mean a person to whom a franchise is granted and sold. However, this confusion might be marginal since commentators understand that the law requires the disclosure document to be given to the prospective franchisee. See Cory J Covert, 'Virginia' in W Michael Garner (ed), *Franchise Desk Book: Selected State Laws, Commentary and Annotations* (Vol 1, 3rd edn, American Bar Association 2019) at VA-27-28;

pective franchisee'. Only South Dakota and Washington franchise sale statutes expressly duplicate the FTC Rule's definition of a prospective franchisee.⁶² However, the FTC Rule's definition of a prospective franchisee would apply in the rest of state franchise sale laws by default. Thus, at the state level, a prospective franchisee can be any person (including any agent, representative, or employee) who approaches or is approached by the franchise seller to discuss the possible establishment of a franchise relationship.

3.2.3.3 Conclusions

The FTC Rule is a federal regulation that mainly regulates the franchisor's pre-sale disclosure duty throughout the USA. Although fifteen franchise sale states have their own franchise sale law, the statutes will apply insofar as they afford franchisees equal or greater protection. The franchisor's disclosure duty under the federal and state laws can be summarized as follows. First, the franchisor is primarily responsible for preparing a so-called 'franchise disclosure document', containing essential information about the franchisor, the franchise system, the franchise business, and the terms of a franchise contract. Second, the franchisor or the franchise seller shall provide the prospective franchisee with the disclosure document at least 14 calendar days before the execution of a franchise agreement or the franchisee's payment made to the franchisor. Federal and state sale laws do not require any specific means for delivering the disclosure document. Since the pre-sale disclosure duty is regulated and mandatory, the franchisor and prospective franchisee cannot agree to exclude the performance.

3.2.4 Australia

3.2.4.1 Introduction

The Franchising Code of Conduct (the Code) devotes its Part 2 to regulating the franchisor's pre-contractual information duties. In Part 2, the franchisor's pre-sale obligations include the duty to provide a disclosure document and

Philip F Zeidman, Legal Aspects of Selling and Buying: § 9:89. What do state registration/disclosure laws require?, Westlaw, September 2017 Update.

62 In Washington, the Bill (SB 6172) amended the Franchise Investment Protection Act in 2012 to conform to the FTC Rule's terminology. As a result of the amendment, the term prospective franchisee has replaced the previous term offeree throughout the Act. See Senate Bill Report SB 6172 (February, 2012) at <<https://bit.ly/3ps4HTh>>.

In South Dakota, Bill SB 52 was proposed to enact a new franchise statutory scheme in 2008. This Bill was eventually passed as Chapter 37-5B – Franchise Investment Act, replacing the old Chapter 37-5A. The term 'prospective franchisee' was put in place at the time the Bill was introduced. See Section 1 of Chapter 203 (SB 52) at <<https://bit.ly/2Kwefy4>>.

the duty to provide a key facts sheet.⁶³ Section 3.2.4 will collectively examine these two duties as a sole disclosure obligation. This section will break down the franchisor's obligation into six elements and then examine all the components in subsection 3.2.4.2. Subsection 3.2.4.3 will conclude on the contents and nature of the franchisor's pre-contractual information duty under the Australian legal system.

3.2.4.2 Elements of the pre-contractual information duty

– Provider of pre-contractual information

Under the Code, a franchisor is a provider of pre-contractual information. That is, the Code obligates a franchisor to perform a disclosure obligation by giving a prospective franchisee the documents mentioned in subclause (1A), including a disclosure document and a key facts sheet.⁶⁴ Under the Code, the term 'franchisor' is given specific meanings. Clause 4 defines the term 'franchisor' to mean five groups of persons.⁶⁵ In essence, a franchisor is understood as a person who grants a franchise or otherwise participates in a franchise as a franchisor.⁶⁶ Thus, a franchisor must be a person who can confer a prospective franchisee the right to operate a franchise business.⁶⁷

– Contents of pre-contractual information

The Code requires a franchisor to formulate, among other things, a disclosure document and a key facts sheet with specified contents.

First of all, a franchisor is required to create a disclosure document relating to a franchise that includes the informational items in Annexure 1 of the

63 The Code also requires a franchisor to provide a prospective franchisee with an information statement relating to franchising that is published on the ACCC's website before giving other disclosure-related documents. Nevertheless, the information statement is not intended to furnish a potential franchisee with any information about a specific franchisor or a franchise network. Instead, it helps encourage the prospective franchisee to conduct proper due diligence by getting legal, accounting, and business advice, reading all the documents carefully, and getting to know their rights under the Code. *See* Explanatory Statement, Select Legislative Instrument No.168, 2014, at 25. Thus, this section will not examine this obligation in detail.

64 The Code, cl. 9(1), in conjunction with cl. 9(1A).

65 Clause 4 states that franchisor includes the following:

- (a) a person who grants a franchise;
- (b) a person who otherwise participates in a franchise as a franchisor;
- (c) a subfranchisor in its relationship with a subfranchisee;
- (d) a subfranchisor in a master franchise system;
- (e) a subfranchisor in its relationship with a franchisee.

66 *Swevenings Pty Ltd v Ferguson Consolidated Holdings Pty Ltd (No 5)*, [2010] FMCA 63 [88].

67 *Dorrian v Rushlyn Pty Ltd*, [2013] FMCA 101 [236].

Code.⁶⁸ In Annexure 1, there are twenty-five items of essential information, which are broken down into fragments. For example, item 2 deals with the franchisor's details. In this second item, the franchisor should provide information about the name and address, or addresses, of registered office and principal place of business in Australia; the name under which the franchisor carries on business in Australia relevant to the franchise; a description of the kind of business operated under the franchise; the number of years that the franchise or franchise system has operated in Australia, to name a few. All informational items are intended to offer a comprehensive overview of the franchise, which helps a prospective franchisee make a reasonably informed decision and provides the prospective franchisee with current information that is material to the running of a franchised business.⁶⁹

Clause 8(3)(b)(ii) implies that a franchisor does not have to provide a prospective franchisee with all the disclosure items required by Annexure 1. The franchisor may delete some particular items from the disclosure document if applicable information does not exist for those items. The explanatory statement exemplifies that the franchisor may exclude the heading for item 12 from the disclosure document if the franchisor does not make goods or services available online and the franchisor does not intend to do so.⁷⁰ The franchisor may be allowed to provide more items of information in the disclosure document. According to clause 8(3)(a)(iii), the franchisor may add additional information under the heading 'Updates'.

Secondly, a franchisor is required to prepare a key facts sheet relating to a franchise that is in the form published on the Australian Competition and Consumer Commission (ACCC)'s website.⁷¹ More importantly, the franchisor must include in the key facts sheet the information required by the ACCC's form and the information about the matters relating to the franchise that is included in the disclosure document relating to the franchise.⁷² For example, in a key facts sheet, the franchisor must provide information about the name of the franchisor, the duration that the franchisor has operated the franchise system in Australia, the franchisor's financial viability, current legal proceedings, to name a few. The key facts sheet does not aim to replace the disclosure document. According to the Explanatory Statement to the Competition and Consumer (Industry Codes- Franchising) Amendment (Fairness in Franchising) Regulation 2021, this document is intended to get a prospective franchisee to pay attention to the most significant information in the disclosure documents.⁷³

68 The Code, cl. 8(1).

69 The Code, cl. 8(2).

70 Explanatory Statement, Select Legislative Instrument No.168, 2014, at 20.

71 The Code, cl. 9A(1)(a). The format of a key facts sheet can be accessed at <<https://bit.ly/3HORxKj>>.

72 The Code, cl. 9(A)(1)(b) and (c)(i).

73 Explanatory Statement to the Regulation 2021, at 10.

– *Format of pre-contractual information*

The Code requires the pre-contractual information to be disclosed in writing. This formal requirement can be inferred from clause 9(1) that the franchisor must provide a prospective franchisee with the documents, including a disclosure document and a key facts sheet, before entering into a franchise agreement. The disclosure document and the key facts sheet are standardized; that is to say, the franchisor must format the documents following the requirements imposed by the Code. Regarding the disclosure document, clause 8(1), in conjunction with clause 8(3)(a)(i)(ii), provide that the franchisor must create the document that conforms with the content, order, headings, and numbering set out in Annexure 1.⁷⁴ Concerning the key facts sheet, clause 9A(1)(a) requires the franchisor to make the sheet in the form published by the ACCC.

– *Delivery of pre-contractual information*

The Code does not specify methods for furnishing a disclosure document and a key facts sheet. Nor does the Explanatory Statement suggest how a franchisor should deliver the documents. Accordingly, it could be said that the franchisor can decide to provide a prospective franchisee with printed copies of the documents by mail. Alternatively, the franchisor may choose to transmit the documents electronically. In the latter case, Giles and Ward suggest that the franchisor has to comply with the following two threshold requirements imposed by the Electronic Transaction Act 1999 (Cth).⁷⁵ First, the information must be readily accessible in order to be useable for subsequent reference. Second, a person to whom the information is provided consents that the information is to be given by means of electronic communication.⁷⁶

The Code permits a prospective franchisee to specify the delivery of a disclosure document and a key facts sheet. According to clause 9(2C), the franchisee may request the franchisor send the documents in a printed form, electronic form, or both. In this case, the franchisor is obliged to comply with the franchisee's request. If the franchisor has already given the franchisee the documents in one of those forms, the franchisor does not have to comply with the franchisee's request for the other form. To illustrate, a prospective franchisee may ask a franchisor to send a copy of a disclosure document and a key facts sheet digitally. In this case, the franchisor must comply with the franchisee's request. Suppose the franchisor has already provided the prospect-

74 The ACCC has created a recommended format for the disclosure document that conforms to Annexure 1 of the Code. This model disclosure document can be accessed at <<https://bit.ly/37eLIDR>>.

75 Stephen Giles and Penny Ward, 'Australia' in Andrew P Loewinger and Michael K Lindsey (eds), *International Franchise Sale Laws* (2nd edn, American Bar Association 2016) 10.

76 The Electronic Transaction Act 1999 (Cth), sec. 9(1)(a) and (d).

ive franchisee with printed copies of the documents. In that case, the franchisor may refuse to provide the franchisee with the documents in an electronic format if the franchisee demands these.

– *Timing for disclosing pre-contractual information*

The Code adopts a 14-day time frame for disclosing pre-contractual information in a disclosure document and a key facts sheet. Clause 9(1) of the Code requires a franchisor to give a prospective franchisee a copy of the disclosure document and the key facts sheet at least 14 days before either of the following two triggering events. First, a prospective franchisee enters into a franchise agreement or an agreement to enter into a franchise agreement.⁷⁷ Second, a prospective franchisee makes a non-refundable payment of money or of other valuable consideration to the franchisor or an associate of the franchisor in connection with the proposed franchise agreement.⁷⁸ In this respect, the period of 14-day must be counted backward from the point at which the franchise agreement will be concluded or the point at which the prospective franchisee makes a non-refundable payment to the franchisor.⁷⁹

– *Recipient of pre-contractual information*

A prospective franchisee is a person to whom a franchisor must furnish a disclosure document and a key facts sheet.⁸⁰ Clause 4 defines a prospective franchisee to mean a person who deals with a franchisor for the right to be granted a franchise. According to Giles, the expression 'a person who deals with a franchisor' is susceptible to be construed to include other persons, such as a professional adviser and an agent of a franchisee.⁸¹ As far as case law is concerned, the definition offered by the Code is intended to be exhaustive.⁸² For example, the court in *Rafferty v Madgwick*s states that:

77 The Code, cl. 9(1)(a).

78 The Code, cl. 9(1)(b).

79 The nature of non-refundable payment was discussed by the court in the case *Palis Victoria v Gelare International*. According to the court, a question of whether the prepayment is required and whether it is refundable may partly be addressed by a disclosure document. Furthermore, a question of whether the advance is refundable should be considered in connection with clause 26 of the Code, dealing with termination in the cooling-off period. In sum, the prepayment is non-refundable if the franchisee does not cool off within the specified period or if the condition for a refund under the disclosure document is not satisfied. See *Palis Victoria Pty Ltd v Gelare International Pty Ltd*, [2015] FCCA 2785 [310] – [314].

80 The Code, cl. 9(1).

81 Stephen Giles, *Annotated Franchising Code of Conduct* (2nd edn, LexisNexis Butterworths 2021) 27.

82 *SPAR Licensing Pty Ltd v MIS QLD Pty Ltd* (No 2), [2012] FCA 1116 [102] – [103].

‘[T]his distinct definition makes sense in the light of the fact that it is meant to capture persons who are considering the purchase of or participation in a franchise, but who have not yet been granted or become involved in a franchise (that is, who are not yet actual franchisees).’⁸³

Thus, a prospective franchisee in light of the Code must be a person who will be an actual franchisee after the conclusion of a franchise agreement.

3.2.4.3 *Conclusions*

The Franchising Code of Conduct regulates the franchisor’s disclosure obligation by requiring a franchisor to provide a prospective franchisee with a disclosure document and a key facts sheet containing the information relating to a franchise specified by the Code. In this case, the franchisor must provide the prospective franchisee with copies of the documents at least 14 days before the prospective franchisee enters into a franchise agreement or before the prospective franchisee makes a non-refundable payment to the franchisor. However, the Code does not regulate all aspects of the performance of the disclosure duty. Thus, the franchisor may decide some aspects of the performance, such as a delivery method. In this case, the franchisor may have to comply with the electronic transaction law rules if the franchisor opts for the electronic transmission of the documents. Since the franchisor’s disclosure duty is mandatory, the parties cannot agree to exclude or deviate from the rules regulating the performance of the pre-contractual obligation.

3.2.5 Comparative analysis

3.2.5.1 *Introduction*

The franchise legal framework of the DCFR, the USA, and Australia establishes the franchisor’s pre-contractual duty of disclosure toward a prospective franchisee because of a concern over the problem of asymmetric information inherent in a franchise relationship. From the descriptive examinations, the disclosure obligation imposed by the legal framework of the selected legal systems can generally be broken down into the following five components: (1) the provider of pre-contractual information, (2) the contents of pre-contractual information, (3) the format of pre-contractual information, (4) the delivery of pre-contractual information, (5) the timing for disclosing pre-contractual information, and (6) the recipient of pre-contractual information. This section will juxtapose and discuss those six elements of the franchisor’s disclosure duty in subsection 3.2.5.2. Subsection 3.2.5.3 will conclude and put

83 *Rafferty v Madgwicks* [2012] FCAFC 37 [146].

forward key recommendations for comprehensive franchise law to regulate the franchisor's pre-contractual disclosure obligation.

3.2.5.2 Comparison and discussion

– Provider of pre-contractual information

(1) Similarity

The DCFR, the USA, and Australia similarly obligate a franchisor to prepare and provide a prospective franchisee with pre-contractual information.⁸⁴ Under the chosen legal systems, a franchisor denotes a person who grants the right to conduct a franchised business and participates in a franchise relationship as a franchisor. In this respect, other third persons, such as the franchisor's agents or representatives, are generally not required by the laws to prepare and, in particular, disclose pre-contractual information. The rationale behind this construction is straightforward; the franchisor is an owner of a franchise business who ordinarily possesses material information about the business. Thus, the franchisor is in a perfect position to prepare for disclosing such substantial information.

(2) Difference

Unlike the DCFR and Australia, the US legal system imposes the disclosure duty on third persons other than a franchisor in specific circumstances. In the case of responsive disclosure upon request, the US federal regulation – the FTC Rule – requires a franchise seller to give a prospective franchisee a copy of the franchisor's disclosure document. In terms of a definition, the federal legislation defines a franchise seller to include the franchisor's representatives, agents, employees, and brokers. In this case, those third persons can be required to perform the disclosure duty.⁸⁵ This requirement results from the Federal Trade Commission's concern that franchise agents may deceive some prospective buyers of a franchise. In America, franchise brokerage services are ubiquitous businesses. Under some circumstances, some franchise brokers may influence potential franchisees to make an investment decision before examining the franchisor's disclosure document. Therefore, the FTC Rule formulates this third-party disclosure to protect prospective franchisees in the sales process.

(3) Discussion

The three selected legal systems commonly accept that an owner of a franchise business or a franchisor shall primarily be responsible for preparing and disclosing qualified information to prospective purchasers during the pre-contractual phase. According to Buchan, a franchisor is a key source of pre-

⁸⁴ See subsections 3.2.2.2, 3.2.3.2, and 3.2.4.2.

⁸⁵ See subsection 3.2.3.2.

contractual information.⁸⁶ Thus, the requirement that the franchisor must provide a prospective franchisee with the information should incontestably be adopted under comprehensive franchise law. A franchisor may not be the only actor in this regard. The US legal system shows that the disclosure duty can be imposed on other third persons connected with the franchisor, such as the franchisor's brokers and consultants. In the USA, the involvement of those persons in a franchise sales process seems commonplace because franchisors often benefit from brokerage services in franchise sales activities. For instance, franchise recruitment consultants may help find and pre-screen potential franchisees for franchisors to select.⁸⁷

In my opinion, comprehensive franchise law should require pre-sale disclosure by franchise agents and brokers only for exceptional purposes. A seemingly acceptable goal is to protect prospective franchisees against misbehaviors in franchise sales. In this case, legal systems should ensure that they have supportive evidence indicating that the use of franchise agents and brokers in franchise sales is pervasive, and the third parties' misconduct is probable. For example, there should be a considerable number of cases showing that franchise brokers fraudulently induce prospective buyers to purchase franchises by not having an opportunity to study pre-sale information before the conclusion of franchise agreements. Without firm evidence of this incident, the imposition of a third parties' disclosure obligation would be unnecessary and redundant. Moreover, it would cause uncertainty about who is responsible for disclosing pre-contractual information to prospective franchisees.

In case of third-party disclosure, I suggest that comprehensive franchise law makes the following three points explicit. First, the law should impose the disclosure duty on third persons who are authorized to engage in franchise sales activities on the franchisor's behalf. In practice, there are various types of intermediaries, such as agents, brokers, and consultants. This requirement aims to designate the persons to whom prospective franchisees may approach for the disclosure of pre-sale information. Second, the law should strive to eliminate any potential confusion about the information given. Typically, the franchisor's agents, brokers, and employees do not hold or possess essential information about a franchise themselves. In this case, the law should provide that the designated third persons are required to provide prospective franchisees with the information that is prepared by the franchisor. Otherwise, the information provided by those persons might be susceptible to inaccuracy and outdatedness. Third, the law should provide that the third-party disclosure of pre-sale information amounts to the franchisor's disclosure so that any claim

86 Jenny Buchan, 'Ex ante information and ex post reality for franchisees: The case of franchisor failure' (2008) 36 *Australian Business Law Review* 407, 419.

87 Don Daszkowski, 'The Rise of Franchise Brokers and Consultants' IFA (31 March 2017) <<https://bit.ly/2MC8lsz>> accessed 17 February 2023.

arising out of the failure to perform the duty can be raised against the franchisor.

– *Contents of pre-contractual information*

(1) *Similarity*

The DCFR, the USA, and Australia are similar in that their franchise legal framework draws up a list of pre-contractual information items that a franchisor needs to provide. The DCFR makes a list of eight informational items, and the American and Australian laws list twenty-three disclosure items.⁸⁸ In any event, these listed disclosure items are material information that enables prospective franchisees to enter into a franchise contract with full knowledge of relevant facts about a franchise under consideration. In this respect, the contents of pre-sale information required by the selected legal systems are relatively comparable. That is, the franchise legal framework of the chosen legal systems requires a franchisor to provide a prospective franchisee with information about the franchisor, the franchise system, the franchise business, and the terms of a franchise agreement.

(2) *Difference*

The USA differs from the DCFR and Australia in that the list of informational items to be disclosed in the FDD is inclusive. This conclusion is drawn from the fact that the FTC Rule prohibits the franchisor from including any materials or information other than those required or permitted by the Rule or state law not preempted by the Rule.⁸⁹ This prohibition aims to ensure that a franchisor will not provide immaterial and irrelevant information to prospective franchisees. Conversely, providing additional information is permissible under the DCFR and Australian legal system. Under the DCFR, a franchisor may, by its initiative, provide a prospective franchisee with additional informational items that would enable the franchisee to decide on a reasonably informed basis whether or not to enter into a franchise contract. The franchisor may be required to provide additional information other than the eight disclosure items, provided that good commercial practice is required.⁹⁰ Likewise, the Australian Franchising Code of Conduct allows a franchisor to provide additional information in a disclosure document. In general, the franchisor has to respond to twenty-five disclosure items set out by Annexure 1 in the disclosure document. The franchisor may add further information under the heading 'Update' in the document.⁹¹

⁸⁸ See subsections 3.2.2.2, 3.2.3.2, and 3.2.4.2.

⁸⁹ See subsection 3.2.3.2.

⁹⁰ See subsection 3.2.2.2.

⁹¹ See subsection 3.2.4.2.

(3) *Discussion*

The rationale for disclosing pre-contractual information to a prospective franchisee is to enable the latter to make an informed decision whether to enter into a franchise contract with a franchisor. In this respect, the information to be given should be material; it should sufficiently enhance the prospective franchisee's understanding of a franchise and the franchisor before the conclusion of a franchise agreement. From the comparison, the disclosure items required by the DCFR, the USA, and Australia's franchise legal framework are relatively similar. In short, the franchisor is required to disclose material information about the franchisor, the franchise system, the franchise business, and the fundamental rights and obligations under a franchise contract.

The franchisor's disclosure may not be user-friendly as the disclosure items required by franchise legal frameworks can be highly intricate. Taking the US legal system as an illustration, a franchisor must prepare the disclosure document containing twenty-three items of the information prescribed by the FTC Rule. Under the Rule, each informational item is then broken down into a substantial number of sub-items to which the franchisor is instructed to respond fully.⁹² Following those instructions dutifully would end up creating an intimidating disclosure document containing an enormous amount of pre-contractual information. This assumption is not exaggerated. Karp and Stern claim that the entire franchise disclosure document in practice could exceed 300 pages, which would be terrifying to prospective franchisees.⁹³

The example given above shows that a single disclosure document would contain detailed and elaborate pre-sale information. This lengthy document would prevent a prospective franchisee from assimilating and finding helpful information. According to Emerson and Benoliel, most prospective franchisees are inexperienced business owners. When studying complex disclosure items, those inexperienced prospects could face the following three problems: awareness, screening, and comprehension problems. First, prospective franchisees may not be able to look for legal and commercial risks involving a franchised business. Second, prospective franchisees may find it difficult to differentiate between relevant and irrelevant information about the franchise. Third, prospective franchisees may not be able to comprehend and evaluate the complex pre-contractual information.⁹⁴ A cumbersome amount of pre-sale information provided to the potential franchisees could intensify those three problems.

The difficulties identified in the preceding paragraph would cause a state of ignorance, meaning a prospective franchisee lacks relevant information before the conclusion of a franchise agreement. To avoid informational ignor-

⁹² 16 CFR, § 436.6(c).

⁹³ Eric H Karp and Ari N Stern, 'A Proposal for a Mandatory Summary Franchise Disclosure Document' (2016) 35 Franchise Law Journal 541, 543.

⁹⁴ Robert W Emerson and Uri Benoliel, 'Are Franchisees Well-Informed: Revisiting the Debate over Franchise Relationship Laws' (2012) 76 Albany Law Review 193, 209-12.

ance, a prospective franchisee may have to hire some specialists, such as legal advisors and accountants, to do due diligence by evaluating potential risks and extracting significant information contained in a disclosure document. Hiring specialists could be detrimental to the franchisee's finances because their services can be notoriously expensive. For example, in Australia, the cost of legal advice is claimed to be 500 AUD per hour.⁹⁵ This cost seems to be prohibitive as it is said that a franchisee may not undertake proper due diligence because of reluctance to incur a professional service's cost.⁹⁶ Thus, the franchisee would jump to make an investment decision without reviewing the disclosed pre-contractual information.⁹⁷

As can be seen, the franchise legal frameworks may inadvertently restrain a prospective franchisee's decision-making by requiring the franchisor's detailed and complex disclosure. In remedying that deficiency, comprehensive franchise law should streamline the franchisor's disclosure of pre-contractual information to facilitate the franchisee's utilizing the information. In doing so, the law may require a franchisor to provide a reasonable number of informational items. This reasonableness requirement could help a prospective franchisee comprehend the disclosure items at marginal cost. In any event, I suggest that the law does not compromise the materiality of the pre-contractual information. That is, the comprehensive franchise law should ensure that it equips the prospective franchisee with full knowledge about the franchisor, the franchise system, the franchise business, and the fundamental rights and obligations under a franchise contract.

Based on the suggestion mentioned above, I believe that the DCFR's approach offers an excellent example for demarcating the amount of the pre-contractual information to be provided. The descriptive section shows that the DCFR requires a franchisor to provide a prospective franchisee with a non-exhaustive list of eight informational items.⁹⁸ In my view, these items of information sufficiently offer insights into the franchisor, the franchise system, the franchise business, and the franchise contract terms to be concluded. Since the DCFR does not require the provisions of detailed disclosures, as the American and Australian legal systems do, the franchisor's disclosure of the information could be made with a high degree of conciseness that facilitates a prospect-

⁹⁵ Explanatory Statement, Select Legislative Instrument No.168, 2014, at 93.

⁹⁶ Lorelle Frazer and others, 'Pre-contractual Due Diligence by Franchisees and Independent Small Business Buyers' (2018) 46 Australian Business Law Review 157, 158.

⁹⁷ The franchisee's unrealistic optimism would escalate this assumption. Empirical studies show that a franchisee tends to be overly optimistic about the future, which makes the franchisee disinterested in reading a disclosure document. See Uri Benoliel and Jenny Buchan, 'Franchisee's Optimism Bias and the Inefficiency of the FTC Franchise Rule' (2015) 13 DePaul Business & Commercial Law Journal 411, 411-31; Uri Benoliel, Jenny Buchan, and Tony Gutentag, 'Revisiting the Rationality Assumption of Disclosure Laws: An Empirical Analysis' (2017) 46 Hofstra Law Review 469, 469-88.

⁹⁸ See subsection 3.2.2.2.

ive franchisee's effective use of the information given. Thus, comprehensive franchise law may follow the DCFR in listing the informational items to be provided in a disclosure document.

The Australian model in introducing a mandatory key facts sheet could also help prevent prospective franchisees from relinquishing studying disclosed information.⁹⁹ Under the Australian Franchising Code of Conduct, this document is intended to guide the franchisee to essential information contained in a disclosure document. In this case, the franchisee would be equipped with some knowledge about a franchise before studying the disclosure document. Nevertheless, the descriptive section shows that the Code requires a specific format of a key facts sheet. That is, the franchisor has to prepare the document following the form published by the ACCC, an Australian franchise regulator. Thus, this model would work well in legal systems that have established similar regulatory authorities that will be assigned to prepare and publish a format of a key facts sheet.

– *Format of pre-contractual information*

(1) *Similarity*

In terms of the disclosure format, the USA and Australia are similar in that their franchise legislation requires the disclosure of pre-sale information to be made in writing. Under these jurisdictions, a franchisor is required to prepare a written document, commonly known as a 'disclosure document'. This disclosure document is created to contain the informational items required by the laws. In preparing the document, the American and Australian legal systems similarly require a franchisor to follow instructions prescribed by franchise-specific laws. In light of the instructions, a disclosure document usually begins with a cover page stating, among other things, the title of the document and the name and contact information of the franchisor. The document also has a table of contents regarding disclosure items. The main body of the document contains details about each pre-sale information item required by the laws. If applicable, there can be an attachment to the disclosure document.

(2) *Difference*

Unlike the US and Australian legal systems, the DCFR does not require formatting informational items to be disclosed. Strictly speaking, the DCFR does not obligate a franchisor to create a written document, as do the counterpart jurisdictions. Because there is no formal requirement, it could be concluded that, under the DCFR, a franchisor may provide a prospective franchisee with pre-contractual information enumerated by IV.E. – 4:102(1) in any form. For example, a franchisor may organize the pre-contractual information in the form

⁹⁹ See subsection 3.2.4.2.

of an audio or video presentation uploaded onto YouTube's website. Despite the lack of formality, it could be argued that a franchisee may request the franchisor's disclosure to be made in writing. According to IV.E. – 2:402, a party to a franchise contract may request a signed document containing the terms of the contract. This provision aims to entitle parties to a franchise contract to obtain evidence of the contract.¹⁰⁰ Thus, this article may be utilized by analogy to permit a prospective franchisee to ask for the disclosure of pre-contractual information in a written format.

(3) *Discussion*

From the comparison, the approach to formatting the disclosure of pre-contractual information is twofold.

First, there is no formality regarding the disclosure of pre-contractual information. Among the selected legal systems, the DCFR seems to adopt this approach. Because of the lack of formal requirements, a franchisor may give a potential franchisee pre-contractual information orally unless the franchisee requests the disclosure to be made in writing. In terms of advantages, a verbal format of the disclosure would help some prospective franchisees get access to pre-sale information on an equal footing. Strictly speaking, prospective franchisees with visual impairments or dyslexia will be able to use and understand the information given more efficiently if the audio format of disclosure is permissible under a franchise legal framework.

The second approach to which the USA and Australia adopt is that the franchisor's disclosure of pre-sale information must be made in writing. In this respect, a franchisor usually has to create a so-called 'disclosure document' containing the required informational items. Because of its durability, a written format of the disclosure can be advantageous to prospective franchisees in that the franchisees may keep the disclosure document for future reference before concluding a franchise contract. After the conclusion of the contract, the franchisees may present the document as documentary evidence when legal actions against the franchisor are brought to court. In short, a written form of pre-sale disclosure can serve an evidentiary function *ex ante* and *ex post*.

Regarding a formality issue, I propose that comprehensive franchise law adopts the American and Australian approach; the law should require the franchisor's disclosure of pre-contractual information to be made in writing. Specifically speaking, a franchisor should be required to provide a prospective franchisee with the information included in a so-called 'disclosure document'. Providing pre-sale information in a disclosure document would benefit a prospective franchisee in the following two aspects.

100 Bar and Clive (n 4) 2334-335.

First, a disclosure document could serve an evidentiary role. In negotiating a franchise contract, a prospective franchisee may need to refer back and forth to some essential information to decide whether to enter into the contract. In this regard, a disclosure document would permit the franchisee to utilize the information given several times until or even after signing a franchise contract. In contrast, it would not be feasible for a potential franchisee to do so if pre-sale information is presented verbally.

Second, a disclosure document would be a proper medium in terms of informational transmissibility. Assuming that the franchise legal framework requires the disclosure of a considerable amount of pre-sale information, the franchisor could put all items of information more efficiently. In this respect, an oral disclosure might not be proper because it would be impractical for the franchisor to provide the franchisee with detailed informational items verbally. Conversely, a disclosure document would visibly record all pieces of material pre-contractual information. Thus, the information would be provided to the prospective franchisee effectively when the disclosure takes a written form.

Legal requirements for creating a disclosure document can be too intricate. As can be seen in the US and Australian franchise laws, a franchisor must comply with a myriad of instructions when preparing a disclosure document. Some instructions might aim at something other than providing material information for a prospective franchisee to decide whether to engage in a franchise relationship with a franchisor. For example, in Australia, Annexure 1 of the Franchising Code of Conduct requires the first page of the disclosure document to include the document title in a bold upper case; the franchisor's name, business address and phone number; etc. It also requires the inclusion of a relatively long statement that aims to urge some caution to a prospective franchisee. These requirements would protect a prospective franchisee in that they hinder the franchisor from presenting a disclosure document in the guise of a marketing brochure that would distract the prospective franchisee.

Despite the benefit mentioned previously, I suggest that the format of a disclosure document should be simplified and streamlined so that the document is made user-friendly. In other words, a disclosure document should not be complicated and intimidate the franchisee's attempt to utilize the pre-contractual information given. As can be seen, the chosen legal systems agree that the primary goal of providing a prospective franchisee with the disclosure document is to equip the franchisee with essential information about a franchise and a specific franchisor. In this regard, I propose that disclosure rules of comprehensive franchise law diminish some excessive formality that does not aim at disseminating substantial information to the prospective franchisee. For example, the rules may not restrict the fonts or sizes of the letters in a disclosure document. Suppose some statements, such as cautions, need to be added on the first page to encourage the prospective franchisee's usage of the document. In that case, I recommend that warning messages quickly capture

the franchisee's attention and allow the franchisee to comprehend within a short time. In this respect, warning messages should be effective; they should be simple, accurate, and specific, resulting in achievable actions.¹⁰¹

In the meantime, the disclosure rules should ensure that the structure of a disclosure document is readable and well-organized to facilitate the prospective franchisee's usage. In doing so, the rules may obligate the franchisor to put the disclosure items addressing essential information about the franchisor, the franchise system, the franchise business, and the terms of a franchise contract in a logical order. The rules of comprehensive franchise law should also ensure that every prospective franchisee can have an equal chance to access pre-contractual information. Strictly speaking, the disclosure rules should require that a disclosure document is created in a manner that is reasonably accessible for individual franchisees. In other words, the rules should instruct the franchisor to present the required pre-sale information in an accessible manner, taking into account the individual franchisee's capacity to access such pre-sale information. For those people with visually impaired abilities, the franchisor may have to digitize a disclosure document that would be compatible with some assistant devices, such as a document reader. For foreign franchisees, the franchisor may have to present the disclosure document in a language that the franchisee may understand well. These examples illustrate that the comprehensive franchise law may help ensure the franchisee's unobstructed access to pre-contractual information in reality.

– *Delivery of pre-contractual information*

(1) *Similarity*

The DCFR, the USA, and Australia do not specify a means for delivering pre-contractual information required by the laws. The absence of such a specification could be explained by the fact that the delivery methods will generally relate to the required format of the disclosure of pre-sale information. Under the DCFR, there is no formal requirement for the disclosure of pre-contractual information. In particular, no written form of disclosure is required. In theory, a franchisor may give a prospective franchisee the disclosures verbally. In the USA and Australia, a franchisor is obliged to provide a prospective franchisee with a copy of a disclosure document. Since no specific delivery method is required, the franchisor may send a copy of the document in several ways, including hand-delivering at a face-to-face meeting, post, or through electronic means. This conclusion holds true for the DCFR if a franchisor chooses to provide a prospective franchisee with a disclosure document.

101 Sally Potter, 'Why some people don't respond to warnings: writing effective short warning messages' (2021) 36 Australian Journal of Emergency Management 29, 30.

(2) *Difference*

When it comes to providing pre-sale information electronically, the US and Australian legal systems differ from the DCFR in that the former two jurisdictions have legal rules regulating the electronic transmission of the disclosure to some extent. In America, franchise sale law of some states, such as California, impose specific requirements for delivering a disclosure document through electronic means.¹⁰² Australia has the Electronic Transaction Act 1999 (Cth), which is currently in force.¹⁰³ Some commentators argue that a franchisor must comply with the electronic transaction law's requirements when sending the disclosure document electronically.¹⁰⁴ In contrast, the DCFR does not contain any model rule regulating the electronic transmission of pre-contractual information in the franchising context.

(3) *Discussion*

From the comparison, the DCFR, the USA, and Australia do not regulate how a franchisor delivers pre-contractual information. It might be because the delivery methods ordinarily relate to a form of pre-sale disclosure required by franchise-specific law's disclosure rules. Suppose a franchisor is obliged to give a prospective franchisee a copy of a disclosure document containing the required informational items. In that case, the franchisor may choose various means for providing such a copy, including paper-based and electronic dissemination. Thus, I suggest that comprehensive franchise law adopts the same approach; it should allow a franchisor to choose methods that it sees fit for delivering pre-contractual information.

As illustrated in the preceding paragraph, a franchisor may prepare a digital copy of a disclosure document for its franchisees. This practice is not unusual in this Digital Era, where advanced technology is dominant in our daily lives. From my experience, many businesses choose to make use of electronic papers or documents in current commercial practices. This holds true in the context of franchise businesses. Some franchisors may disseminate their documents, including disclosure documents, to franchisees electronically. Nevertheless, there is a problem; those digitized materials may be transient because a digital disclosure document may last for a short time.

In the context of electronic transmission, I suggest that disclosure rules of comprehensive franchise law regulate the franchisor's provision of an electronic disclosure document to some degree.¹⁰⁵ This suggestion rests on

¹⁰² See subsection 3.2.3.2.

¹⁰³ See subsection 3.2.4.2.

¹⁰⁴ Giles and Ward (n 75) 10.

¹⁰⁵ It should be noted that the creation of a digital franchise disclosure document can be subject to national electronic transaction law that governs information generated, sent, received, or stored by electronic means. In this case, the disclosure rules of comprehensive franchise law may leave this technical issue to that electronic regulation. The sample of the electronic

the fact that a digital copy of the document provided to a prospective franchisee usually is non-physical and needs supportive devices to read it. In this case, the electronic format of the document would obstruct a prospective franchisee from utilizing the information given effectively. For example, a prospective franchisee may not be able to access an electronic disclosure document because the franchisee's computer device is not compatible with that digital document.

In regulating the provision of a digital disclosure document, I propose that the disclosure rules impose the following three requirements to ensure a prospective franchisee's effective use of pre-contractual information sent electronically.

First, the rules should require a franchisor to create an electronic disclosure document in a durable format. This durability of the electronic information will ensure that a potential franchisee can utilize the information in the future until the conclusion of a franchise contract. Inspired by the US FTC Rule, a disclosure document should be required to be delivered in the format that enables the prospective franchisee to store, download, print, or otherwise maintain the document for future use. For instance, a disclosure document may be prepared in a PDF or MS Word format. This requirement is said to enable a potential franchisee to study the document independently or pass this document to its consultants.¹⁰⁶

Second, the rules should require a franchisor to ask for a prospective franchisee's prior consent to the electronic transmission of the document. This requirement aims to prompt a prospective franchisee that a disclosure document will be delivered electronically so that the franchisee prepares for the delivery. This condition is vital as a potential franchisee may not be ready for the electronic transmission for some technical reasons. Thus, the franchisor should be permitted to furnish the potential franchisee with a digitized disclosure document only upon the potential franchisee's consent to the electronic delivery.

Third, in asking for the franchisee's consent, the rules should require the franchisor to consult and inform the franchisee of any precondition for reviewing the document in a digital format. For instance, the franchisor may have to advise the prospective franchisee that the franchisor will deliver a PDF version of a disclosure document through a website portal. In getting that PDF file, the prospective franchisee may be required to create an account on the site. These requirements would ensure that the prospective franchisee will be well prepared to receive pre-contractual information sent electronically.

transaction rules can be found in the UNCITRAL Model Law on Electronic Commerce, which is accessible at <<https://bit.ly/37D6wFk>>.

106 72 FR 15515 (March 30, 2007).

– *Timing for disclosing pre-contractual information*

(1) *Similarity*

The DCFR, the USA, and Australia agree that a prospective franchisee should have sufficient time to study pre-contractual information provided by a franchisor. Thus, the chosen legal systems similarly impose a waiting period in the sense that the franchisor is required to provide the prospective franchisee with the required items of information for a certain period before the triggering event specified by franchise-specific law. Besides, the three legal systems generally accept that the point at which a franchisor and a prospective franchisee conclude a franchise contract is regarded as the triggering event by which the franchisor has to give the franchisee the required pre-sale disclosures.

(2) *Difference*

The DCFR markedly differs from the US and Australian legal systems in terms of a waiting period. Unlike the two jurisdictions, the DCFR does not prescribe a fixed period for a franchisor to disclose pre-contractual information. Under the DCFR, a franchisor is required to provide pre-contractual information within a reasonable time before the conclusion of a franchise contract. Conversely, America and Australia fix the timing for disclosure by adopting a waiting period of 14 days. In these countries, the franchisor must provide a copy of a disclosure document at least 14 days before the prospective franchisee enters into a franchise contract.¹⁰⁷ The USA differs from Australia in that the franchisor may be required to furnish the prospective franchisee with the disclosure document earlier than 14 days in the case of a reasonable request by the franchisee.

(3) *Discussion*

From the comparison, the selected legal systems accept that a prospective franchisee should have sufficient time to review pre-sale information given by a franchisor. Thus, the selected legal systems set a waiting period within which a franchisor has to provide a prospective franchisee with pre-sale information and allow the franchisee to study the information before the conclusion of a franchise contract. However, the timing for disclosure varies among the legal systems. Despite the variation, the prescription of the waiting period can be divided into two cases as follows.

Firstly, a waiting period is not fixed by the law. In other words, the timing for disclosure may be subject to the determination of some open standards. As can be seen, the DCFR requires the period for disclosure to be reasonable. This reasonableness standard is elusive, which will be determined on a case-by-

¹⁰⁷ It should be noted that the Australian Franchising Code of Conduct allows a franchisee to terminate a franchise agreement in a 14-day cooling-off period. *See* The Code, cl. 26(1).

case basis. From my viewpoint, this approach creates no realistic expectation for a prospective franchisee. That is, the franchisee may not be able to expect when it is reasonable for the franchisor to furnish the franchisee with pre-contractual information before the conclusion of a franchise contract. In this case, the franchisee may have to rely upon case law in which courts offer a clear-cut answer by specifying the timing for disclosure by a franchisor.

Relying on case law may not be useful for two reasons. First, there may be no relevant case law on this point. In many legal systems, courts usually decide cases upon lawsuits filed by parties to a franchise contract. Thus, the judges cannot lay down any concrete guidelines if no party raises an issue regarding the time frame for franchise disclosure to courts for adjudicating. Second, court decisions may be contradictory in the sense that the judges in different cases may concretize the reasonableness standard inconsistently. For instance, while courts in some cases may deem 14 days reasonable, courts in other like-cases may consider 30 days reasonable. This inconsistency would result in uncertainty that might discourage investors from entering into franchise businesses.

Secondly, a waiting period is fixed or predetermined by the law. The USA and Australia embrace this model. I believe that this model would protect a prospective franchisee because of certainty. Thus, I suggest that disclosure rules of comprehensive franchise law adopt a fixed-period approach. A clear and predictable disclosure time frame would allow a prospective franchisee to anticipate the duration within which the franchisee may study pre-contractual information before concluding a franchise agreement. Nonetheless, a period fixed by franchise-specific law may vary from legal system to legal system. This divergence raises a question as to the appropriate extent of timing for disclosure. As can be seen, the USA and Australia adopt a 14-day standard. In this regard, one may assume that the 14-day standard is appropriate.¹⁰⁸

However, I remain skeptical of whether a 14-day period is an appropriate disclosing period for legal systems to adopt, considering that no uniformity concerning the disclosure timing among the countries regulating franchise sales exists. In Europe, France and Spain obligate a franchisor to provide required information to potential buyers at least 20 days before the conclusion of a franchise contract.¹⁰⁹ Unlike those European countries, Italy and Belgium adopt a period of 30 days and one month, respectively.¹¹⁰ Similarly, the

108 Mark Abell, *The law and regulation of franchising in the EU* (Edward Elgar 2013), at [5.30]. A further piece of literature on waiting and cooling-off periods for franchise agreement is Courtenay Atwell's PhD thesis. See Courtenay Atwell, 'Early withdrawal rights in franchise contracts: A comparative study of their role and effectiveness in Australia, England and France' (DPhil thesis, UNSW Business School 2018).

109 Article L.330-3 of the French Commercial Code and Article 3 of the Spain Royal Decree 201/2010 of 26 February.

110 Article 4(1) of the Italian Law No 129/2004 and Article X.27 of the Belgian Code of Business Law.

Netherlands imposes a 4-week disclosure period.¹¹¹ In other regions, Malaysia and Brazil require a franchisor to provide a prospective franchisee with a copy of a disclosure document at least ten days before signing a franchise contract.¹¹² Conversely, China and Mexico opt for a minimum of 30 days.¹¹³ In sum, the timing for disclosure under franchise regulations can range from 10 days to one month.

Despite the discrepancy in a timing requirement, I suggest that comprehensive franchise law adopts a one-month disclosure period. In the course of one month, I believe that time constraints are eliminated; hence, a prospective franchisee will have sufficient time to study, consult, and decide.¹¹⁴ First, the franchisee will be able to digest all pre-contractual informational items given in a disclosure document. The more items the law requires to provide to the franchisee, the more time is needed. Second, the franchisee can seek specialists' advice on some informational items. Taking the DCFR as an example, a franchisor must provide a prospective franchisee with information about the terms of a franchise contract. In this case, a prospective franchisee may need a lawyer to offer opinions on those contractual clauses. Third, the franchisee must have enough time after studying and consulting to decide whether to conclude a franchise contract. Thus, a one-month disclosure period would allow a prospective franchisee to execute a series of these three steps.

Furthermore, a question may be raised about the event or point in time that will trigger a one-month disclosure period. From the comparison, the DCFR, the US, and Australian legal systems agree that the point at which a franchisor and a prospective franchisee conclude a franchise contract is considered the triggering event. This condition seems to be a standard requirement as other jurisdictions with franchise disclosure law, such as Belgium and the Netherlands, adopt the same condition.¹¹⁵ Thus, I suggest comprehensive franchise law follows this commonality. A franchisor should be required to provide a prospective franchisee with a disclosure document at least one month before the conclusion of a franchise contract. For instance, if a franchise contract is to be signed on 15th June 2023, the franchisor must provide pre-sale information required by the law to the franchisee by 15th May 2023.

The USA and Australia also require a franchisor to disclose pre-contractual information before the prospective franchisee's payments. This requirement seems to suit the franchising practice that a potential franchisee may be

111 Article 7:914(1) of the Dutch Civil Code.

112 Section 15(1) of the Malaysia Franchise Act of 1998 and Article 4 of the Brazilian Law no.8.955 of December 15, 1994.

113 Article 21 of the Chinese Regulations on Administration of Commercial Franchise of 2007 and Article 142 of the Mexican Industrial Property Law.

114 In general, it is claimed that time constraints would restrict the purchaser's ability to effectively evaluate the business proposal. *See Frazer and others* (n 96) 159.

115 Article X.27 of the Belgian Code of Business Law and Article 7:913(1) of the Dutch Civil Code.

required to pay some money or other considerations before making a franchise contract. In my view, the decision to pay money or other considerations is undoubtedly an investment decision. Accordingly, the franchisee should also be informed of all relevant material information before making such a decision. Thus, I suggest that comprehensive franchise law adopt this approach by requiring a franchisor to provide a prospective franchisee with a disclosure document at least one month before the prospective franchisee's prepayment to the franchisor too. For example, a franchise contract is to be signed on 15th June 2023. However, if a prospective franchisee is required to pay an initial fee on 7th June 2023, the franchisor must furnish the franchisee with pre-sale information required by the law by 7th May 2023, not 15th May 2023.

– *Recipient of pre-contractual information*

(1) *Similarity*

The DCFR, the USA, and Australia similarly accept that pre-contractual information required by the law must be provided to a prospective franchisee. In other words, a prospective franchisee must be a recipient of the information because it will end up in concluding a franchise agreement as an actual franchisee with a franchisor. The selected legal systems commonly accept that the prospective franchisee is vulnerable to risk losing its money in investing in a franchise business because of the lack of material information for making an investment decision. With these concerns in mind, the chosen legal systems obligate a franchisor to furnish a prospective franchisee with the disclosure items before the franchisee concludes a franchise contract or makes any payment to the franchisor.

(2) *Difference*

The US legal system differs from the DCFR and Australia in that the former broadly defines the term 'prospective franchisee'. In America, the FTC Rule defines the term 'prospective franchisee' to mean any person who approaches or is approached by a franchise seller to discuss the possible establishment of a franchise relationship. That person can be any agent, representative, and employee of an actual franchisee. In contrast, the DCFR and the Australian legal system seem to understand that a 'prospective franchisee' is a person who will be an actual franchisee. Literally speaking, a franchisor cannot deliver the disclosure items to the franchisee's agent and employee since they are not regarded as prospective franchisees.

The difference among the selected legal systems in defining the term 'prospective franchisee' would not affect the eventual outcome. Under the DCFR and the Australian legal system, the franchisee's agent or employee can be the recipient of pre-contractual information. These representatives may receive the disclosures on behalf of the franchisee by virtue of the law of agency or mandate. Taking the DCFR as an illustration, Part D of Book IV contains model

rules concerning mandate contracts. Under the rules, the franchisee may authorize its agent by a mandate contract to negotiate and conclude a franchise contract between the franchisee and the franchisor, or lead to or facilitate the conclusion between those people.¹¹⁶ Thus, under the DCFR, the franchisor may disseminate the disclosure items to the franchisee's agent or employee if the franchisee's agent or employee is authorized to receive those disclosures.

(3) *Discussion*

Franchise law's disclosure rules always designate a person who is entitled to receive pre-contractual information. From the comparison, the chosen legal systems commonly accept that a recipient of pre-contractual information is a person commonly known as a 'prospective franchisee'. In my view, comprehensive franchise law should adopt this element and define the term 'prospective franchisee'. From the comparison, the DCFR, the USA, and Australia agree that a person who approaches a franchisor for a right to conduct a franchise business is regarded as a prospective franchisee. To put it another way, a prospective franchisee is a person who intends to engage in a franchise relationship as an actual franchisee after the conclusion of a franchise contract with a franchisor. Thus, I propose that comprehensive franchise law follows this common approach and defines the word "prospective franchisee" to mean a person who approaches, or is approached by, a franchisor for the right to conduct a franchise business.

One might raise a question as to when a person is considered approaching a franchisor or being approached by a franchisor. In response to this question, I propose that comprehensive franchise law provides a useful yardstick for determining the existence of the status of a prospective franchisee. Setting that criterion aims to ascertain the point at which a franchisor owes the disclosure duty towards a prospect. Unfortunately, the disclosure rules of the DCFR, the US, and Australian franchise laws offer no guide in this regard. Despite the absence of guidance, I suggest that comprehensive franchise law deems a person who expresses its intention to negotiate for the right to conduct a franchise business to be a prospective franchisee in light of the law. In this case, a person showing general interest in a franchise business might not be considered a prospective franchisee until it states an intention to negotiate for a franchise contract. However, whether that intention exists must be decided on a case-by-case basis.

The comparison of the selected legal systems also shows that the agency disclosure is allowable, meaning a franchisor may disclose pre-contractual information to a third person other than an actual franchisee. Thus, it is questioned whether the term 'prospective franchisee' should be defined to include some types of third persons, in particular, the franchisee's agent and employee. From my perspective, this issue is a matter of legal policy; hence,

116 The DCFR, IV.D. – 1:101(1).

no clear-cut answer could be given in response to this question. In some legal systems, a prospective franchisee may be confined to an actual franchisee. In this regard, a franchisor is obliged to furnish that person with pre-contractual information. In other words, it is not obligatory for the franchisor to provide other third persons with pre-sale information.

Nevertheless, it does not mean that a franchisor is prevented from furnishing a third person with pre-sale information. Under certain circumstances, the franchisor may have to do so if that third person is authorized to negotiate for a grant of a franchise on the franchisee's behalf. In this case, legal systems should have mechanisms to ensure that an actual franchisee is kept informed of any material information acquired by its representative. This issue would be marginal in practice since legal systems ordinarily have the law of agency or mandate normally dealing with these mechanisms. Taking the DCFR as an example, the rule regulating a mandate contract requires an agent to reasonably inform the principal of the existence of, and the progress in, the negotiations or other steps leading to the possible conclusion or facilitation of the prospective contract.¹¹⁷ The drafters of the DCFR provide that this rule aims at requiring the agent to keep its principal informed of all relevant information received during the performance.¹¹⁸

3.2.5.3 Conclusions

– Concluding remarks

The DCFR, the USA, and Australia have a common perception that a franchise purchase is an investment. Accordingly, the selected legal systems agree that a prospective franchisee should have some material information to make a reasonably informed decision. A wise decision would prevent the franchisee from facing financial disasters because of investing in the wrong business. With this viewpoint, the DCFR, the USA, and Australia formulate franchise law's disclosure rules establishing the franchisor's pre-contractual duty to provide information to a prospective franchisee. In essence, the disclosure obligations under the DCFR and the US and Australian legal systems are fundamentally similar. Under the chosen legal systems, the franchisor is required to provide a prospective franchisee with pre-sale informational items within a certain period before the conclusion of a franchise contract. Nonetheless, the DCFR, the USA, and Australia slightly differ in terms of the format and delivery of pre-contractual information and the requirement as regards the waiting period.

¹¹⁷ The DCFR, IV.D. – 3:401.

¹¹⁸ Bar and Clive (n 4) 2156.

– *Key recommendations*

(1) *Establishment of the pre-contractual information duty*

Because of informational asymmetry, a prospective franchisee should be furnished with materially relevant information about a franchise. The goal is to enable a prospective franchisee to make a sensible investment decision. In reaching that objective, legal systems should formulate disclosure rules under comprehensive franchise law. The rules should establish the franchisor's disclosure duty that obligates the franchisor to provide material information to a prospective franchisee before the sale of a franchise.

(2) *Definition of a prospective franchisee*

It is suggested that comprehensive franchise law defines the term 'prospective franchisee'. Defining that word would facilitate a search of a person entitled to receive the disclosures provided by a franchisor. The law should define 'prospective franchisee' to mean a person who approaches or is approached by a franchisor for the right to conduct a franchise business. It is also advised that comprehensive franchise law provides a criterion for determining the existence of a prospective franchisee. In this case, the law should deem a person who expresses its intention to negotiate for the right to conduct a franchise business to be a prospective franchisee.

(3) *Contents of pre-contractual information*

Comprehensive franchise law's disclosure rules should specify items of pre-contractual information required to be provided. In principle, the disclosure items should sufficiently provide insights into the franchisor's identity, the franchise system, the franchise business, and the fundamental rights and obligations under a franchise contract. Most importantly, the rules should require a franchisor to provide a reasonable amount of informational items. The DCFR's approach would be considered a good model in this regard.

(4) *Format of pre-contractual information*

Comprehensive franchise law's disclosure rules should require the franchisor's disclosure of pre-contractual information to be made in writing in the form of a disclosure document. The rules should simplify and streamline the disclosure document's format so that the document is made user-friendly. The rules should also instruct the franchisor to disclose pre-sale informational items in the format and language that can be accessed by a prospective franchisee, considering the individual franchisee's capacity to access the information.

(5) *Delivery of pre-contractual information*

Comprehensive franchise law's disclosure rules should permit a franchisor to choose methods for delivering a disclosure document as it sees appropriate. The franchisor may opt for paper-based or electronic communication. In the

latter case, the rules should regulate the electronic transmission of a disclosure document by imposing three requirements as follows. First, the rules should require a franchisor to create an electronic disclosure document in a durable format. Second, the rules should require a franchisor to ask for a prospective franchisee's prior consent to the electronic transmission of the document. Third, the rules should require a franchisor to consult and inform a prospective franchisee of any precondition for reviewing a digitized document.

(6) *Timing for furnishing pre-contractual information*

Comprehensive franchise law's disclosure rules should fix a time frame within which a franchisor must provide pre-sale information and allow a prospective franchisee to study the information. The waiting period should sufficiently allow a prospective franchisee to study, consult, and decide. Thus, adopting a one-month period is suggested. The rules should require a franchisor to provide a prospective franchisee with a disclosure document at least one month before the conclusion of a franchise contract or the prospective franchisee's prepayment to the franchisor, depending upon which event happens first.

3.3 DUTY TO PROVIDE COMPLETE, CURRENT AND ACCURATE INFORMATION

3.3.1 Introduction

Section 3.3 will examine how the franchise legal framework of the DCFR, the USA, and Australia regulates the establishment of the franchisor's duty to provide complete, current and accurate pre-sale information. The descriptive examination of the franchise legal frameworks will be conducted in sections 3.3.2, 3.3.3, and 3.3.4, respectively. Section 3.3.5 will compare, contrast, and discuss the approaches to establishing the franchisor's duty to provide complete, current and accurate information taken by the chosen legal systems to offer guidelines for developing franchise rules regulating the franchisor's duty under comprehensive franchise law.

3.3.2 The Draft Common Frame of Reference (DCFR)

3.3.2.1 Introduction

The duty to provide complete, current and accurate information is not recognized under the DCFR as a distinct obligation compared to the disclosure obligation. No model rules establish the duty to provide complete, current and accurate information as IV.E. – 2:101, in conjunction with IV.E. – 4:102(1), constitutes the duty of disclosure. Nevertheless, the construction of this duty could be implied; a franchisor may be required to ensure the correctness,

completeness, and transparency of pre-contractual information required to be provided. This implication can be taken from applying the disclosure rule in Part E of Book IV and the rule governing the requirement of good faith and fair dealing in Book III. This section will elaborate on the application of the rules in subsections 3.3.2.2 and 3.3.2.3, respectively. Conclusions about the nature and contents of the franchisor's duty to provide complete, current and accurate information will be made in subsection 3.3.2.4.

3.3.2.2 *Disclosure rule*

Neither IV.E. – 2:101 nor IV.E. – 4:102(1) explicitly requires that the franchisor ensures the correctness, completeness, and transparency of pre-contractual information required to provide to a prospective franchisee. It would seem that the drafters of the DCFR intend the franchisor to owe the duty to provide complete, current and accurate information towards the franchisee. This intention can be observed in the Comments to IV.E. – 2:101. The commentaries provide that the provision of pre-contractual information aims to enable the recipient of the information to decide on a reasonably informed basis whether to conclude a contract on the terms under consideration. Accordingly, the DCFR would require the franchisor to ensure that the information to be provided is correct, complete, and transparent.¹¹⁹

It should be mentioned that the duty to provide complete, current and accurate information would not be peculiar in the context of national franchise law in Europe. A franchisor may be required to ensure the truthfulness of pre-contractual information to be given under franchise legislation. For instance, in Spain, article 62.3 of the Retail Trade Act and article 3 of the Royal Decree 201/2010 require the franchisor to disclose pre-contractual information to a prospective franchisee. In complying with that obligation, it is said that the franchisor must provide the required information which is truthful and not misleading.¹²⁰ Thus, it could be argued that the franchisor's disclosure of pre-contractual information under the DCFR should follow this direction too.

3.3.2.3 *Rule relating to good faith and fair dealing*

The principle of good faith and fair dealing recognized by the DCFR may require the franchisor to ensure the correctness, completeness, and transparency of pre-contractual information. Under the DCFR, III. – 1:103(1) formulates a fundamental principle that a person has to act in accordance with good faith

¹¹⁹ Bar and Clive (n 4) 2287.

¹²⁰ Jaume Martí Miravalls, 'Spanish Legal System on Disclosure in Franchise Networks: Problem and Proposals for an Improved Regulation' (2014) 25 *European Business Law Review* 943, 948; Mónica Esteve Sanz and others, 'Chapter 42: Spain' in Mark Abell (ed), *The Franchise Law Review* (2nd edn, Law Business Research Ltd 2015) 542.

and fair dealing in performing an obligation.¹²¹ In the franchising context, it could be said with certainty that the franchisor's performance of the disclosure obligation must correspond to the standard of conduct in good faith and fair dealing. However, there is a question: how does a franchisor perform the disclosure duty in accordance with good faith and fair dealing?

In Book I of the DCFR, I. – 1:103(1) defines the expression 'good faith and fair dealing' to mean a standard of conduct characterized by honesty, openness, and consideration for the interests of the other party to the relationship in question. In this respect, the drafters of the DCFR clarify these three determinants as follows.¹²² First, 'honesty' is understood by its normal meaning. According to the dictionary, telling the truth is characterized as an example of being honest.¹²³ Second, the term 'openness' points out transparent behaviors. Third, consideration for the other party's interests depends on the circumstances of the case. In the context of negotiating for a franchise contract, it seems to me that a franchisor should help a prospective franchisee to conclude the contract with no false assumptions. Therefore, after taking into account all the determinants, it could be concluded that a franchisor has an obligation in good faith and fair dealing to ensure that the pre-sale information to be disclosed is correct, complete, and transparent.¹²⁴

3.3.2.4 Conclusions

The DCFR does not contain specific provisions that establish the duty to provide complete, current and accurate information as a duty distinct from the franchisor's disclosure obligation. However, the rules regulating the pre-contractual disclosure duty and the duty of good faith and fair dealing can be utilized to constitute the franchisor's duty. In this case, the duty to provide complete, current and accurate information would be regarded as an auxiliary duty requiring the franchisor to perform the pre-contractual disclosure obligation with a certain degree of care. In other words, a franchisor would be required

121 Despite the auxiliary nature, the franchisor's duty to provide complete, current and accurate information is obligatory in light of III. – 1:102(1).

122 Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.1, Oxford University Press 2010) 89.

123 Diana Lea and Jennifer Bradbery, *Oxford Advanced Learner's Dictionary* (10th edn, Oxford University Press 2020) 747.

124 Some European countries utilize the principle of good faith to ensure the currency and truthfulness of pre-contractual information in the franchising context. For example, in Germany, some regional courts have concertized the general principle of good faith to create the duty to provide complete, current and accurate information. As far as court decisions are concerned, three Higher Regional Courts held that the franchisor has to give the franchisee the correct and full information concerning the profitability of the franchise system. See OLG München, 16.09.1993, 6 U 5495/92, OLG Düsseldorf, 25.10.2013, I-22 U 62/13 and OLG Frankfurt, 03.06.2016, 13 U 107/14.

to provide a prospective franchisee with pre-contractual information, which is correct, complete, and transparent. Thus, the franchisor's non-performance of the duty would amount to the non-performance of the pre-contractual duty of disclosure that allows an aggrieved franchisee to seek private law remedies under the DCFR.

3.3.3 The United States of America (USA)

3.3.3.1 Introduction

Federal and state franchise sale laws do not distinctively establish the franchisor's duty to provide complete, current and accurate information. Nonetheless, the establishment of this duty could be implied from federal and state franchise sale law rules regulating disclosure requirements, updating requirements, and prohibitions against unlawful conduct. As will be seen, these franchise rules may, directly and indirectly, ensure the accuracy, currentness, and completeness of pre-contractual information to be disclosed. This section will examine how the rules regulating disclosure requirements, updating requirements, and prohibitions against unlawful conduct constitute the franchisor's duty to provide complete, current and accurate information in subsections 3.3.3.2, 3.3.3.3, and 3.3.3.4, respectively. Subsection 3.3.3.5 will conclude on the nature and contents of the franchisor's duty in the USA.

3.3.3.2 Disclosure requirements

– Federal law

The FTC Rule does not contain any provision that imposes the duty to provide complete, current and accurate information as a distinct duty on a franchisor. Nevertheless, providing complete and accurate information to a prospective franchisee is indeed one of the FTC Rule's objectives. This assumption can be inferred from the court decision in *FTC v USA Beverages*. In this case, the court acknowledged that the FTC Rule intended to ensure that prospective franchisees receive complete and accurate information necessary for making an investment decision.¹²⁵ As described in section 3.2.3, the FTC Rule requires a franchisor to disclose the required information in a disclosure document.¹²⁶ According to section 436.1(d), the term 'disclose' is defined to include presenting all material facts accurately. For example, the franchisor is obliged to include accurate information about the principals of the company, litigation history,

¹²⁵ *Federal Trade Commission v USA Beverages, Inc*, 2006 WL 8432509 (SD Fla, 2006) 12.

¹²⁶ 16 CFR, §436.6(b).

and lists of previous buyers in the disclosure document.¹²⁷ Thus, it could be concluded that a franchisor has the duty to disclose accurate information to a prospective franchisee under the federal legislation.

– *State laws*

In some franchise sale states, franchise-specific law rules carefully regulate the truthfulness of statements in a disclosure document. For example, in Illinois, the franchise disclosure law rule mandates that all statements in the disclosure document must be of the following three qualities. First, they must be free from any false or misleading statement of a material fact. Second, they must not omit to state any material fact required to be stated or necessary to make the statements not misleading. Third, they must be accurate and complete as of the effective date thereof.¹²⁸ Accordingly, a franchisor could be said to have the duty to ensure that statements or representations, such as sales projections, are not false or omitting to state any material fact or are accurate and complete.¹²⁹ Otherwise, the franchisor's failure to comply with these three requirements would be actionable under the disclosure statute.

3.3.3.3 *Updating requirements*

– *Federal law*

Not only does the FTC Rule regulate the accuracy of the disclosure items, but the Rule also oversees their currentness. In regulating the disclosure items' currentness, the Rule requires a franchisor to furnish a prospective franchisee with an up-to-date disclosure document.¹³⁰ This inference is drawn from sections 436.2(a) and 436.7(a), requiring that the franchisor's disclosure document must be current as of the close of the franchisor's most recent fiscal year. In keeping all information in the disclosure document up-to-date, the FTC Rule sets out the instructions for updating the disclosures as follows.¹³¹

First, a franchisor shall make an annual update. That is, the franchisor must prepare a revised disclosure document within 120 days after the close of the fiscal year.¹³² For example, if the franchisor's fiscal year of 2022 adheres to a calendar year, the franchisor must update the disclosure document version 2022 by the 1st May 2023. After the annual revision is made, the franchisor and other franchise sellers are required to distribute a disclosure document

¹²⁷ *FTC v Holiday Enterprises, Inc.*, 2008 WL 953358, (ND Ga, 2008) 8.

¹²⁸ IL ST, CH 815 § 705/16.

¹²⁹ *Team Tires Plus, Ltd v Heartlein*, 2004 WL 3406090, (D Minn, 2004) 9.

¹³⁰ *Family Wireless #1, LLC v Automotive Technologies, Inc.*, 2016 WL 183475 (D Conn, 2016) 2.

¹³¹ 72 FR 15518 (March 30, 2007).

¹³² 16 CFR, §436.7(a).

version 2023 in the sales of a franchise during the rest of 2023. For instance, the franchisor must furnish the prospective franchisee with a 2023 franchise disclosure document if a franchise contract is to be concluded on the 1st October 2023.

Second, a franchisor shall also make a quarterly update. Nonetheless, this quarterly update is exceptional and required only in certain circumstances. That is, the franchisor must prepare revisions to reflect any material change to information included in the disclosure document within a reasonable time after the close of each quarter of the fiscal year.¹³³ The Compliance Guide to the Franchise Rule exemplifies that material changes include the fact that the franchisor recently files a bankruptcy petition or the franchisor is filed a legal action that may harm the franchisor's financial condition.¹³⁴ In this case, at the time of disclosure, a prospective franchisee must be furnished with the franchisor's current disclosure document and the quarterly revisions made to the information contained in the document.

– *State laws*

Likewise, state franchise sale statutes may ensure the currentness of pre-sale disclosure items. In other words, the state statutes may require a franchise disclosure document to be current as of the franchisor's most recent fiscal year. The laws may impose updating requirements equivalent to those required by the FTC Rule. For example, in South Dakota, the franchise sale law requires a franchisor to revise its disclosure document within 120 days after the close of the fiscal year. The franchisor is also required to prepare revisions to the disclosure document to reflect any material change to the disclosures within a reasonable time after the close of each quarter of the fiscal year.¹³⁵

Some franchise sale states may lay down updating requirements stricter than those of the FTC Rule.¹³⁶ For example, in Hawaii, the franchise investment law provides that an offering circular containing disclosure items shall expire three months after the end of the franchisor's fiscal year. In this case, a franchisor must apply for renewal by submitting the most recent amended offering circular within sixty days before the expiration date.¹³⁷ In contrast, the FTC Rule does not establish a like-renewal procedure. In Illinois, the franchise disclosure law articulates that a franchisor shall make quarterly revisions to reflect any material change to the disclosures within 30 days after the close

¹³³ 16 CFR, §436.7(b).

¹³⁴ The Compliance Guide to the Franchise Rule (2008), at 126 <<https://bit.ly/3hUBg9N>> accessed 21 January 2022.

¹³⁵ SD ST, § 37-5B-7(2) – (4).

¹³⁶ Baer (n 33) 528.

¹³⁷ HI ST, § 482E-3(d).

of each quarter of the franchisor's fiscal year.¹³⁸ Conversely, the FTC Rule merely requires the revisions to be made within a reasonable time.

3.3.3.4 Prohibition against misrepresentations

– Federal law

The FTC rule contains provisions that aim to prevent the communication of misleading statements and preserve the integrity of information in a disclosure document.¹³⁹ For example, section 436.9(a) makes it unlawful for a franchisor to make any verbal, visual, and written claim or representation that contradicts the information required to be disclosed. Furthermore, according to section 436.9(b), it is unlawful for the franchisor to make some misrepresentations specified by the Rule. Besides the FTC Rule, some provisions of the Federal Trade Commission Act (FTCA) apply to the franchisor's disclosure of pre-sale information in the sales of a franchise. For instance, under the FTCA, any unfair or deceptive practices in commerce or affecting commerce is unlawful and actionable.¹⁴⁰ As far as case law is concerned, the rules of the FTCA can be applied to cases where a franchisor made untrue statements, such as false income claims.¹⁴¹

– State laws

Franchise sale law of all sixteen franchise sale states similarly prohibits making misrepresentations or untrue statements by a franchisor through a so-called 'antifraud provision'.¹⁴² For example, California franchise investment law provides that it is unlawful for a franchisor willfully to make any untrue statement of a material fact in any statement disclosed in the disclosure document. It is also unlawful for a franchisor willfully to omit to state in any such statement any material fact which is required to be stated in the disclosure document.¹⁴³ In light of the antifraud regulation, some courts assume that

¹³⁸ IL ST, CH 815 § 705/11.

¹³⁹ 72 FR 15531 (March 30, 2007).

¹⁴⁰ 15 USCA, § 45(a)(1), in conjunction with § 57b(a)(1).

¹⁴¹ *USA Beverages* (n 125) [11]; *Federal Trade Commission v American Entertainment Distributors, Inc.*, 2012 WL 12964783, (SD Fla, 2012), [6].

¹⁴² California – CA CORP, § 31202; Florida: FL ST § 817.416(2)(a); Hawaii – HI ST, § 482E-5(b)(1); Illinois – IL ST, CH 815 § 705/6(c); Indiana – IN ST, 23-2-2.5-27(2); Maryland – MD BUS REG, § 14-229(a)(2); Michigan – MI ST, 445.1505(b); Minnesota – MN ST, § 80C.13; New York – NY GEN BUS, § 687; North Dakota – ND ST, 51-19-11(2)(b); Oregon – OR ST, § 650.020(1)(b); Rhode Island – RI ST, § 19-28.1-17; South Dakota – SD ST, § 37-5B-25(1); Virginia – VA ST, § 13.1-563(2); Washington – WA ST, 19.100.170(2); Wisconsin – WI ST, 553.41(4).

¹⁴³ CA CORP, § 31202.

the franchisor owes the franchisee a duty to disclose truthful and non-misleading information in a disclosure document.¹⁴⁴

3.3.3.5 Conclusions

At the federal and state levels, the US franchise sale law does not explicitly require a franchisor to ensure that the disclosures are accurate, complete, and current. Nevertheless, the FTC Rule and state franchise sale laws have several provisions that would ensure the disclosure's accuracy, completeness, and currentness. First of all, federal and state franchise legislation typically require a franchisor to disclose accurate information in a disclosure document. Secondly, the federal and state franchise sale laws impose on a franchisor the duty to update its disclosure document, either annually or quarterly, to ensure that a prospective franchisee receives current information. Lastly, the federal and state franchise sale laws' antifraud provision prevents a franchisor from engaging in unlawful conduct, including making misrepresentations or untrue statements. These rules would ensure that the disclosure items are accurate, complete, and current.

3.3.4 Australia

3.3.4.1 Introduction

The Franchising Code of Conduct (the Code) does not explicitly constitute the franchisor's the duty to provide complete, current and accurate information as a distinct obligation. However, the Code contains several provisions that could be utilized to ensure that the disclosure items are current and candid. These provisions are associated with the franchisor's duty to maintain a disclosure document and the duty to act in good faith. Apart from the Code, the Australian Consumer Law (ACL) can also prohibit a franchisor from engaging in misleading conduct. This competition and consumer law would also ensure the currentness and accuracy of pre-contractual information. This section will examine the rules regulating the duty to maintain a disclosure document, the duty to act in good faith, and the prohibition against misleading conduct in subsections 3.3.4.2, 3.3.4.3, 3.3.4.4, respectively. Conclusions about the nature and contents of the duty will be made in subsection 3.3.4.5.

3.3.4.2 Duty to maintain a disclosure document

As described in section 3.2.4, a franchisor owes a pre-contractual information obligation towards a prospective franchisee. That is, the Code requires the

144 *Abbo v Wireless Toyz Franchise, LLC*, 2014 WL 1978185 (Mich App, 2014) 8.

franchisor to give the prospective franchisee a disclosure document containing the information set out in Annexure 1. The franchisor must also provide the franchisee with a key facts sheet containing the information disclosed in the disclosure document. In furnishing the franchisee with pre-sale information, the underlying principle is that the information must be up-to-date. This concept is derived from paragraph (b) of clause 8(2), providing that the franchisor's disclosure is intended to give a prospective franchisee current information. The currentness concept is also re-formulated in clauses 9(1A)(b)(i) and 9(1A)(c)(i), requiring a franchisor to give a prospective franchisee an updated disclosure document and an updated key facts sheet.¹⁴⁵

Additionally, the Code imposes updating requirements to ensure that a disclosure document and a key facts sheet contain current pre-contractual information. These requirements are mainly outlined by clauses 8 and 9A. According to clauses 8(6) and 9A(2), a franchisor must update a disclosure document and a key facts sheet within four months after the end of each financial year. Suppose the franchisor's financial year ends on 30 June 2023. In this case, the franchisor must revise the disclosure document and the key facts sheet by 31 October 2023.¹⁴⁶ Under certain circumstances, the franchisor needs not to update these two documents after the end of the financial year. These situations are prescribed by clauses 8(7) and 9A(3). In the previous example, the franchisor does not have to update the disclosure document and the key facts sheet by 31 October if the franchisor does not intend to enter into a franchise contract or conclude one franchise agreement during 2023.¹⁴⁷

3.3.4.3 Duty to act in good faith

The Code expressly requires the parties to a franchise agreement to act towards the other party with good faith.¹⁴⁸ Clause 6(1) regards this requirement as an obligation to act in good faith. According to clause 6(2)(b), the obligation

¹⁴⁵ Some court decisions seem to affirm this concept. For example, the Federal Court in *SPAR Licensing v MIS QLD* held that the franchisor must ensure that the disclosure document is current at the time the franchise agreement is made or at least 14 days before the conclusion of the contract. See *SPAR Licensing Pty Ltd v MIS QLD Pty Ltd*, [2014] FCAFC 50 [40].

¹⁴⁶ In updating a disclosure document, it is said that some items of information need to be incorporated into the document. Those items include the additional financial statements for the last completed financial year, the independent audit report, the table of transfers and terminations of a franchise in the previous fiscal year, the list of newly-granted franchisees, and any changes in the structure of the board of directors of the firm. See Corrinne Attard and Denial Jepson, 'Australia: Franchise disclosure update time is here again' (*Mondaq*, 16 August 2018) <<https://bit.ly/314t7cM>> accessed 22 January 2022.

¹⁴⁷ The Code, cl. 8(7)(a) and cl. 9A(3)(a).

¹⁴⁸ Clause 6(3) offers two standards for determining whether the party acted in accordance with good faith. Firstly, the party may be deemed to act in good faith if it acted honestly and not arbitrarily. Secondly, the party may be deemed to act in good faith if it cooperated to achieve the purposes of a franchise agreement.

to act in good faith also applies to a person who negotiates for the proposed franchise agreement. Although clause 6(2)(b) imposes an obligation to act in good faith on both parties: the franchisor and prospective franchisee, this provision is said to have an objective of controlling the franchisor's opportunistic conduct and redressing the imbalance of bargaining power.¹⁴⁹ Therefore, in negotiating for a franchise contract, the franchisor will be required to act honestly and not arbitrarily or capriciously.¹⁵⁰ Furthermore, the franchisor will be required to act cooperatively, such as disclosing information to the other party, listening to the other, and negotiating in good faith.¹⁵¹

The obligation to act in good faith under clause 6(2)(b) is characteristically elusive. Accordingly, the good faith obligation under the Code could be construed to cover several sub-duties. Among other things, it could be argued that the franchisor's duty to provide complete, current and accurate information is an instance of the obligation to act in good faith. This good faith duty would require a franchisor to ensure that the information included in a disclosure document is accurate and not misleading. According to Buberis, the ACCC in the case *Ultra Tune* used to allege that the franchisor's false and misleading misrepresentation made in a pre-contractual stage was a contravention of the obligation to act in good faith under clause 6, and the court accepted that allegation.¹⁵² This result seems to suggest that the obligation to act in good faith can be a genesis of the obligation in which the franchisor needs to ensure that the disclosures are correct and candid.¹⁵³

On the other hand, the franchisor is allowed to act in its legitimate commercial interests.¹⁵⁴ In theory, the franchisor may argue that it has no duty to be truthful because of intending to protect its legitimate interests. However, Giles points out that the scope of legitimate commercial interests in franchising remains uncertain and arguable.¹⁵⁵ Despite this uncertainty, I believe that the Code would not allow any party to argue for its own legitimate interests to act opportunistically or unfairly due to two reasons. First, the notion of legitimate interests is understood by Australian courts that a party needs not to act in the interest of the other party or subordinate its legitimate interests

149 Explanatory Statement, Select Legislative Instrument No.168, 2014, at 18; Alan Wein, Review of the Franchising Code of Conduct (2013), at 63.

150 *Kiraig Pty Ltd v Rent the Roo Pty Ltd*, [2017] FCCA 1493 [156].

151 *Macquarie International Health Clinic Pty Ltd v Sydney South West Area Health Service*, [2010] NSWCA 268 [16].

152 Peter Buberis, *Australian Franchising Code of Conduct: A Critical Analysis with Current Case law* (Emerald Publishing 2020) 163.

153 This conclusion conforms with other Australian commentators who contend that a seller of any business has the duty not to mislead or deceive. See Frazer and others (n 96) 175.

154 The Code, cl. 6(6).

155 Giles (n 81) 43.

to the other's.¹⁵⁶ Second, it is said that the obligation to act in good faith is established under the Code to address serious misconduct, such as opportunistic and unfair conduct.¹⁵⁷ This idea should be considered strict in that the parties' performance of an obligation in good faith cannot be excused by personal interests, albeit legitimate in a commercial sense. Thus, the Code would not permit the franchisor to provide the prospective franchisee with outdated and inaccurate pre-sale information by arguing for its own legitimate interests since this conduct would be considered unfair.

In addition, the franchisor would have the duty to ensure that the disclosures are up-to-date by virtue of clause 6(2)(b). In this case, one commentator offers some practical illustrations. Required by good faith, Schaper suggests that a franchisor may be required to inform a prospective franchisee of any significant change to the existing disclosure document before updating the document is completed. Schaper explains that the Code requires the franchisor to update the disclosure document within four months after the end of the financial year. However, there is a possibility that, during the period, the disclosure document provided is not the latest or updated version.¹⁵⁸ Consequently, the franchisor has the duty of good faith to inform the prospective franchisee of a change of material information that is necessary for a prospective franchisee to make a reasonably informed decision.¹⁵⁹

3.3.4.4 Prohibition against misleading conduct

The franchisor's conduct in the pre-contractual phase can also fall within the ambit of the Australian Consumer Law (ACL).¹⁶⁰ For example, it is accepted that section 18 of the ACL applies to regulate the franchisor's behaviors.¹⁶¹ Section 18(1) of the ACL would prohibit a franchisor from engaging in conduct in trade or commerce that is misleading or deceptive or is likely to mislead or deceive. This provision does not define the expression 'misleading or

156 Alicia Hill, 'Good Faith: Enforcement in Australia' (2013) 11 *International Journal of Franchising Law* 29, 38. See also Digby J's opinion in *Delahunt v Swim Loops Pty Ltd*, [2018] VSC 269 [55].

157 Giles (n 81) 42.

158 Michael Schaper was the Deputy Chair of the ACCC. He aired his view on the webinar hosted by the ACCC. This webinar, titled 'The new Franchising Code – what you need to know and do now', has been uploaded on the ACCC's YouTube channel <<https://youtu.be/mK7TnjDVutA>>.

159 For example, a franchisor may have to inform a prospective franchisee of a change in majority ownership of the franchisor or the franchise system. See ACCC, 'Franchisor obligations when giving information' <<https://bit.ly/3GsGhSF>> accessed 21 January 2022.

160 The purpose of the legislation is to promote informed commercial activity based on accurate information. See *Bullabidgee Pty Ltd v McCleary* [2011] NSWCA 259 [69].

161 Wein (n 149) at 12; Brendan Sweeney, Mark Bender, and Nadine Courmadias, *Marketing and the Law* (5th edn, LexisNexis, 2015) 670- 72. The ACL is set out in Schedule 2 of the Competition and Consumer Act 2010. The electronic version of the ACL can be accessed at <<https://bit.ly/2B0bO1H>>.

deceptive'. Despite the absence of the definition, some court interpretations can be followed.¹⁶² In *Parkdale Custom Built Furniture*, Gibbs CJ provided that the words 'mislead' and 'deceive' mean 'to lead into error'.¹⁶³ Therefore, in light of the ACL, the franchisor would have to ensure that pre-contractual information to be provided is not misleading and does not induce the prospective franchisee to make an error.

The ACL would specifically regulate the franchisor's misleading representations about future matters. A future matter is said to be a prediction or projection of anything that will occur in the future.¹⁶⁴ In this case, section 4(1) of the ACL requires the franchisor to have reasonable grounds for making a representation with respect to any future matter.¹⁶⁵ For example, suppose the franchisor states that it will pay a franchisee \$4,000 every month. In that case, the court in the case *South East Melbourne Cleaning* provides that the franchisor must:

'[h]ave a source of funds sufficient to pay the promised amount, a business system capable of collecting payments from its customers and actually paying its franchisees on time, and a willingness to implement such a system and to pay franchisees in accordance with their entitlements under their franchise agreements.'¹⁶⁶

Therefore, under section 4(1) of the ACL, a franchisor will be taken to make a misleading representation about future incomes if it does not have the reasonable grounds illustrated above in support of making the representation.

3.3.4.5 Conclusions

The Franchising Code of Conduct and the Australian Consumer Law may establish the franchisor's duty to provide complete, current and accurate information. First, this franchisor's duty exists under the Code in the form of the duty to maintain a disclosure document and the duty to act in good faith. In the former case, a franchisor is required to create a disclosure document including current information about franchising. In ensuring that the information in the disclosure document is up-to-date, the Code requires the franchisor to update the document annually. In the latter case, a franchisor has an obligation to act in good faith. This duty would require the franchisor

¹⁶² Explanatory Memorandum to Trade Practices Amendment (Australian Consumer Law) Bill (No.2) 2010, at [3.14], <<https://bit.ly/3dIKk3W>> accessed 21 January 2022.

¹⁶³ *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* [1982] HCA 44; 149 CLR 191 [8].

¹⁶⁴ *P C Yarak Pty Ltd & Anor v Quick Cash Advance Pty Ltd & Anor* [2018] SADC 26 [144].

¹⁶⁵ Failure to have reasonable grounds for making a representation as to a future matter will be considered misleading by virtue of section 4(1) of the ACL. See *Carazi Pty Ltd v Blow Dry Bar Franchising Pty Ltd (in liq) (No 2)*, [2015] NSWSC 108 [36] – [37].

¹⁶⁶ *Australian Competition and Consumer Commission v South East Melbourne Cleaning Pty Ltd*, [2015] FCA 25 [97].

to provide accurate and current pre-sale information to a prospective franchisee. In this case, the franchisor could not refuse to perform the duty by arguing for its legitimate commercial interests. The Australian Consumer Law would also help ensure the truthfulness of any statement made by a franchisor. Under the ACL, the franchisor must refrain from engaging in misleading or deceptive conduct, leading a prospective franchisee to make errors. This requirement implies that the franchisor must provide the prospective franchisee with truthful information. Otherwise, the franchisee may allege the franchisor of breaching the ACL's rule.

3.3.5 Comparative analysis

3.3.5.1 Introduction

From the descriptive examinations, a general impression is that the DCFR, the USA, and Australia do not have rules explicitly establishing the franchisor's duty to provide complete, current and accurate information as a distinct pre-contractual duty. The selected legal systems are similar in that the duty to provide complete, current and accurate information could implicitly be constituted under their franchise legal framework. In other words, the franchise legal framework of the DCFR, the USA, and Australia provide several rules to ensure the integrity and truthfulness of the pre-sale information to be provided. In this case, the franchisor would be required to ensure that the disclosure items are accurate, complete, and current. However, the rules or mechanisms to be utilized may vary. This section will compare, contrast, and discuss the applicable rules of the franchise legal framework of the DCFR, the USA, and Australia in subsection 3.3.5.2. Subsection 3.3.5.3 will conclude on the findings and enumerate key recommendations for formulating rules under comprehensive franchise law.

3.3.5.2 Comparison and analysis

– Similarity

The DCFR, the USA, and Australia seem to regard the duty to provide complete, current and accurate information as a sub-duty of the franchisor's disclosure obligation. In other words, the chosen legal systems seem to contemplate this duty as a manner in which the franchisor performs the pre-contractual disclosure obligation. Under the DCFR, the drafters comment on IV.E. – 2:101 that the pre-contractual information to be provided must be current, complete, and accurate. Besides, a franchisor has an obligation in good faith and fair dealing to ensure that the information is correct, complete, and transparent. Accordingly, when performing the pre-contractual obligation, the franchisor must ensure

that the informational items required to provide a prospective franchisee contain current, complete, and accurate information.

In America, the FTC Rule requires a franchisor to disclose pre-sale information accurately. This conclusion holds true for the state franchise sale laws. For example, the Illinois franchise disclosure law requires that all statements in a disclosure document must be accurate, complete, and not misleading. In addition, the FTC Rule and state franchise sale statutes require a franchisor to furnish the franchisee with information, which is current as of the close of the franchisor's most recent fiscal year. In Australia, the Franchising Code of Conduct requires a franchisor to create a disclosure document containing the information, which is up-to-date. Furthermore, the Code imposed on the franchisor the obligation to act in good faith, which would obligate the franchisor to ensure that the information included in a disclosure document is current and accurate.

– *Difference*

The DCFR markedly differs from the US and Australian legal systems in the following two aspects.

First, the DCFR does not offer model rules on updating pre-contractual information, as do the USA and Australia. As can be seen in the descriptive sections, America and Australia require franchisors to make an annual update. In the USA, a franchisor must revise a disclosure document within 120 days after the close of its fiscal year. Likewise, in Australia, a franchisor is required to update a disclosure document and a key facts sheet within four months after the end of its financial year. In terms of updating requirements, Australia slightly differs from the USA in that the Australian Franchising Code of Conduct does not stipulate the rule concerning a quarterly update to reflect any changes to the disclosure document as the US franchise disclosure laws do. Despite the lack of this requirement, the obligation to act in good faith under the Australian Code would require the franchisor to revise its documents addressing any changes before delivering the documents to a prospective franchisee.

Unlike the USA and Australia, no franchise law rule of the DCFR requires a franchisor to make annual and quarterly updates.¹⁶⁷ Unfortunately, the

¹⁶⁷ It should be noted that franchise-specific laws of some European countries, such as France, Spain, and Italy, do not impose either annual updating requirements or quarterly updating requirements. See Rémi Delforge and Gilles Menguy, 'France' in Andrew P Loewinger and Michael K Lindsey (eds), *International Franchise Sale Laws* (2nd edn, American Bar Association 2016) 184; Alberto Echarri and Gonzalo Ulloa, 'Spain' in Andrew P Loewinger and Michael K Lindsey (eds), *International Franchise Sale Laws* (2nd edn, American Bar Association 2016) 446; Aldo Frignani and Francesca Turitto, 'Italy' in Andrew P Loewinger and Michael K

drafters of the DCFR do not explain the absence of updating mechanisms. In my opinion, the probable explanation might be that the DCFR is drafted based on the code-like structure, employing a comprehensive approach similar to civil codes of civilian systems.¹⁶⁸ In this respect, the DCFR's franchise law in Part E of Book IV would focus on laying down specific contract law rules creating rights and obligations for the parties to the contract. In other words, the DCFR's franchise law might not aim to regulate the parties' conduct closely to the same degree as industry-specific regulations do. Thus, imposing updating requirements might be deemed redundant in the eye of the drafters of the DCFR.

Second, unlike the US and Australian laws, the DCFR does not contain model antifraud provisions that can be utilized to prevent the dissemination of misleading pre-contractual information. In the USA, both federal and state disclosure laws contain provisions regulating misleading or deceptive conduct by a franchisor. For example, at the federal level, the FTC Rule makes it unlawful for a franchisor to make any verbal, visual, and written claim or representation that contradicts the information required to be disclosed. Furthermore, state franchise sale statutes typically have antifraud provisions prohibiting the franchisor's misleading or deceptive behaviors. For instance, the Californian franchise law prohibits a franchisor from willfully making any untrue statement of a material fact in a disclosure document. In Australia, the Australian Consumer Law's rules can be used to govern some fraudulent practices by a franchisor. This consumer regulation would prohibit a franchisor from engaging in misleading or deceptive conduct or conduct that is likely to mislead or deceive.

In contrast, the DCFR's franchise law in Part E of Book IV does not have any equivalent antifraud rules. The plausible explanation would be the same as is in the former case; that is to say, the law may not primarily intend to regulate unlawful conduct of the parties to a franchise contract. Consequently, the DCFR may hesitate to enumerate antifraud provisions under franchise law. Nevertheless, it does not mean that the DCFR does not contain rules addressing fraudulent conduct. In the DCFR, the contract and tort law rules may establish *ex-post* sanctions against any misleading or deceptive conduct by a franchisor. In contract law, II. – 7:205(1) would permit the franchisee to avoid a franchise contract if the franchisor induced the former party to conclude the agreement by fraudulent misrepresentation or fraudulent non-disclosure. In tort law, a franchisor may be held responsible for reparation under tort law for fraudulent misrepresentation by virtue of VI. – 1:101, in conjunction with VI. – 2:210.

Lindsey (eds), *International Franchise Sale Laws* (2nd edn, American Bar Association 2016) 253.

168 Esther van Schagen, 'The Draft Common Frame of Reference and Multilevel Governance' (2010) 1 *Edinburgh Student Law Review* 74, 76.

– *Discussion*

From the comparison, the DCFR, the USA, and Australia constitute the franchisor's disclosure obligation to facilitate a prospective franchisee to acquire some essential information about a franchise that enables the franchisee to make a reasonably informed decision in the sales process. The comparison of the franchise legal frameworks conducted in this section shows that providing pre-contractual information, which is current, complete, and accurate, is imperative to get franchise prospects well informed about a franchise under consideration. This acknowledgment implies that a franchisor should be required to ensure the integrity and currentness of the pre-sale information. As an underlying policy, I suggest that comprehensive franchise law contains disclosure provisions establishing the franchisor's duty to provide complete, current and accurate information to prevent a prospective franchisee from receiving false, misleading, or out-of-date information. Without that duty, I am inclined to believe that the franchisee could not make a reasonable investment decision on whether to purchase a franchise.

The underlying policy mentioned above raises a question of the nature and contents of the franchisor's duty to provide complete, current and accurate information under comprehensive franchise law. As can be seen, the comparison shows that the DCFR, the USA, and Australia do not establish the duty to provide complete, current and accurate information as a self-contained obligation. In my view, comprehensive franchise law should contain a provision establishing a distinct obligation that requires a franchisor to exercise a certain degree of truthfulness when disclosing pre-contractual information in light of the law. In performing the duty, the comprehensive franchise law's rule should require the franchisor to ensure that the information to be provided is qualified. That is, the disclosures must be current, complete, and accurate at the date of the disclosure. This proposal would be advantageous to a prospective franchisee as it helps the franchisee undertake pre-purchase due diligence more effectively.¹⁶⁹ Imposing the franchisor's duty to provide complete, current and accurate information would also enable the franchisee to examine whether the franchisor has exercised due care up to a point. In this case, any franchisor's performance that falls short of the required standard would entitle the franchisees to civil remedies under the law.

The selected legal systems assure that a franchisor will have to ensure that the information to be disclosed is current, accurate, and complete in several ways. From my perspective, some approaches could be utilized to strengthen the franchisor's compliance with the duty proposed in the preceding paragraph.

169 For example, Buchan says that due diligence will be restrained if the disclosures are inaccurate. See Jenny Buchan, 'Franchising: A Honey Pot in a Bear Trap' (2014) 34 *Adelaide Law Review* 283, 312.

Firstly, the DCFR and Australia illustrate that the obligation to act in good faith can be imposed on parties in a pre-sale relationship. This obligation would establish a standard of conduct that would require a franchisor to act honestly and cooperatively towards a prospective franchisee in negotiation for a franchise sale. For example, an Australian commentator exemplifies that the obligation of good faith under the Australian Franchising Code of Conduct would require a franchisor to inform any material changes to the disclosures provided to a prospective franchisee.¹⁷⁰ In short, the franchisor would have a duty of good faith to ensure the currentness of the disclosures. Thus, I recommend that comprehensive franchise law also contain a provision establishing the duty to act in good faith and fair dealing that applies to a pre-contractual relationship. The law should also provide criteria that can be used to determine whether the parties act in good faith.

Secondly, the USA and Australia show the incorporation of antifraud provisions in the laws applicable to franchising. For instance, some US state franchise sale laws contain statutory provisions prohibiting a franchisor from making any untrue statement of material facts that could mislead a prospective franchisee. In my opinion, these prohibitive rules would help create *ex-ante* disincentives that deter the franchisor from engaging in any opportunistic conduct associated with the disclosure of pre-sale information. Among other things, the franchisor will have to avoid providing information, which is false or inaccurate. In reality, the antifraud provision can be drafted variously. In other words, there is no uniformity in stipulating this kind of provision. If comprehensive franchise law embraces antifraud provisions, I suggest that the law precisely specifies what types of the franchisor's conduct will be prohibited.¹⁷¹

3.3.5.3 Conclusions

– Concluding remarks

The comparative examination finds that the duty to provide complete, current and accurate information is not regarded as a distinct obligation under the DCFR, the USA, and Australia's franchise legal framework. Nevertheless, the selected legal systems provide certain rules to ensure that a franchisor cannot disregard the truthfulness and currentness of pre-contractual information to be disclosed. As can be seen, the franchise legal framework of the selected legal systems regards the duty to provide complete, current and accurate information as a sub-duty of the disclosure obligation. Performing this duty

¹⁷⁰ See subsection 3.3.4.3.

¹⁷¹ Taking an antifraud provision of the California franchise investment law as an example, the statute makes it unlawful for a franchisor to willfully make any untrue statement of a material fact in a disclosure document.

is considered a manner in which the franchisor executes the pre-contractual disclosure duty. In addition, the DCFR, the USA, and Australia have several law rules that would implicitly constitute the franchisor's duty to provide complete, current and accurate information, such as the rules governing the obligation to act in good faith, the duty to update a disclosure document, and prohibitions against deceptive or misleading conduct. These rules would ensure that a prospective franchisee will receive pre-sale information, which is current, complete, and accurate.

– *Key recommendations*

(1) *Establishment of the duty to provide complete, current and accurate information*

Comprehensive franchise law should ensure that a prospective franchisee gets current, complete, and truthful pre-contractual information. In this respect, the law should contain disclosure provisions constituting the duty that requires a franchisor to provide a prospective franchisee with the pre-contractual information, which is current, complete, and accurate at the date of the provision of the information. This duty should be obligatory in the sense that some private law remedies may follow the non-performance of the obligation.

(2) *Reinforcing mechanisms*

Comprehensive franchise law may contain provisions establishing legal mechanisms that would strengthen the performance of the duty to provide complete, current and accurate information. These reinforcing mechanisms may include the requirement of good faith and fair dealing and the prohibitions against fraudulent conduct. First, the law may require parties in a sale process to act in accordance with good faith and fair dealing. Second, the law may impose prohibitions that would prevent a franchisor from impairing the integrity of pre-contractual information.

3.4 PRIVATE LAW REMEDIES

3.4.1 Introduction

The preceding sections 3.2 and 3.3 demonstrate that the franchise legal framework of the DCFR, the USA, and Australia regulate the franchisor's pre-contractual duties to redress information asymmetry between a franchisor and a prospective franchisee. Some franchisors may fail to perform the pre-contractual obligations imposed by the franchise legal frameworks. In these cases, the question shifts from what the franchisors were supposed to perform to what sanctions are imposed against the breaching franchisors. One would question: what are private law remedies that enable an aggrieved franchisee

to compel the franchisor's performance, claim monetary compensation, and cancel a franchise relationship? Section 3.4 will examine the remedial system under the franchise legal framework of the DCFR, the USA, and Australia in sections 3.4.2, 3.4.3, and 3.4.4, respectively. Section 3.4.5 will compare, contrast, and discuss the remedies under the chosen legal systems to formulate advice on constructing a remedial regime under comprehensive franchise law.

3.4.2 The Draft Common Frame of Reference (DCFR)

3.4.2.1 Introduction

The DCFR contains rules offering private law remedies for a (prospective) franchisee in the case of the franchisor's non-performance of the disclosure duty and the duty to provide complete, current and accurate information. Under the DCFR, the potential remedies are essentially threefold; the franchisee may enforce the franchisor's specific performance, claim damages, and cancel a franchise contract. This section will examine the rules governing three types of private law remedies in subsections 3.4.2.2, 3.4.2.3, and 3.4.2.4, respectively. Subsection 3.4.2.5 will conclude on the remedial regime of the DCFR that would enable the franchisee to seek the three private law remedies in the case of the franchisor's non-performance of the pre-contractual obligations.

3.4.2.2 Enforcement of performance

In theory, a prospective franchisee may resort to III. – 3:302 to enforce a franchisor to disclose pre-contractual information or to provide the information, which is correct, complete, and transparent. Paragraphs (1) and (2) of III. – 3:302 formulate a fundamental principle that the creditor is entitled to enforcing specific performance of a non-monetary obligation if the debtor fails to comply with the terms regulating an obligation. According to III. – 1:102(5), the terms regulating an obligation may be derived from law. Under the DCFR, the disclosure duty and the duty to provide complete, current and accurate information are created by IV.E. – 2:101, in conjunction with IV.E. – 4:102(1). Thus, the franchisor's non-performance of these duties would permit the franchisee to enforce specific performance under III. – 3:302(1) and (2).

In enforcing the franchisor's performance, a prospective franchisee may have to prove that the franchisor fails to provide all or part of informational items or provides out-of-date or inaccurate information. In doing so, the prospective franchisee needs not to prove the franchisor's fault in the non-performance of these obligations as the DCFR does not require this internal element for the recourse to this remedy. Furthermore, the prospective franchisee needs not to demonstrate its losses as the right to enforce specific performance is not conditional upon loss or damage suffered by the creditor.

In sum, the prospective franchisee only has to constitute that the franchisor owes the franchisee the pre-contractual information obligations, and the franchisor fails to perform these duties.

It should be mentioned that the right to enforce specific performance may be excluded under certain circumstances. This exclusion of the right to specific performance is enumerated by paragraphs (3) and (4) of III. – 3:302. For example, under III. – 3:302(3)(a), a prospective franchisee may not compel a franchisor to perform the disclosure obligation if the performance of this duty would be unlawful or impossible. Under III. – 3:302(4), a prospective franchisee may not enforce the franchisor's performance if the franchisee does not request the performance within a reasonable time after the franchisee has become, or could reasonably be expected to have become, aware of the franchisor's non-performance. In any event, a franchisee may be entitled to a remedy to damages as the exclusion of the right to enforce specific performance does not preclude the monetary remedy.¹⁷²

3.4.2.3 *Monetary compensation*

A prospective franchisee who suffers any loss or damage caused by the franchisor's non-performance of the disclosure duty and the duty to provide complete, current and accurate information may claim monetary compensation in the form of damages. Under the DCFR, the franchisee may resort to some contract law rules in seeking an award of damages. In particular, the franchisee may claim damages for the franchisor's non-compliance with the pre-contractual duty of information under IV.E. – 4:102(2), in conjunction with II. – 7:214(2) and (3). Requirements for recovery of damages and principles governing a measure of damages under those model rules will be addressed in the following two italicized headings.

– *Requirements for recovery of damages*

IV.E. – 4:102(2) formulates a fundamental principle that a prospective franchisee may claim damages if the franchisor fails to comply with the pre-contractual information obligation. In seeking an award of damages under that provision, the franchisee must generally satisfy the following three conditional elements.

First, a prospective franchisee must establish the franchisor's non-compliance with the pre-contractual duty to provide information. In this case, the franchisee may claim that the franchisor failed to perform a disclosure obligation by not providing adequate and timely information on the items listed in IV.E. – 4:102(1).¹⁷³ For example, the prospective franchisee may allege that

¹⁷² The DCFR, III. – 3:303.

¹⁷³ Bar and Clive (n 4) 2390.

the franchisor did not provide the franchisee with the informational items wholly or partly. The franchisee may also allege that the franchisor did not furnish the franchisee with the required information within a reasonable time before the conclusion of a franchise contract. Additionally, the prospective franchisee may claim that the franchisor furnishes incorrect or out-of-date information on the required items in IV.E. – 4:102(1).

Second, a prospective franchisee must demonstrate its loss suffered due to the franchisor's non-compliance with the pre-contractual duty to provide information. This element can be drawn by reading IV.E. – 4:102(2) and II. – 7:214(1) collectively. Thus, the right to damages under IV.E. – 4:102(2) presupposes the existence of loss suffered by a prospective franchisee. According to the Comments to II. – 7:214, the term 'loss' covers both economic and non-economic loss. The commentaries further explain that economic loss includes lost income or profits, burdens incurred, and a reduction in the value of the property. Moreover, non-economic loss includes pain and suffering and impairment of the quality of life.¹⁷⁴

Third, there must be a causal link between the franchisor's non-compliance with a pre-contractual information obligation and the loss sustained. According to IV.E. – 4:102(2) and II. – 7:214(1), a prospective must prove that it suffers loss or damage as a consequence of the franchisor's failure to perform the duty. In this case, the franchisee cannot recover damages for any loss, which does not attribute to the franchisor's non-performance of the duty. Concerning the proximity of damage, there may be a question of whether an aggrieved franchisee can recover damages for the loss of chance or opportunity. To put it differently, it is questionable whether the franchisee can argue that the franchisor's non-performance of the pre-contractual information obligations causes the franchisee to lose an opportunity to get a favorable franchise contract from other franchisors.

No commentaries to IV.E. – 4:102 nor the comments to II. – 7:214 addresses the loss of chance issue. Accordingly, it remains unclear whether a prospective franchisee may establish a link to recover damages for the lost chance under the DCFR's contract law. Nevertheless, the drafters of the DCFR seem to concede that courts may characterize the loss of chance as a special form of damage reparable under the law of contract, as well as the law relating to non-contractual liability, under the DCFR.¹⁷⁵ In any case, the loss of chance issue is among the topics left for further discussion and development.¹⁷⁶

¹⁷⁴ Bar and Clive (n 122) 530.

¹⁷⁵ Bar and Clive (n 4) 3195.

¹⁷⁶ Christian von Bar, 'Chapter 16: The Notion of Damage' in Arthur S Hartkamp and others (eds), *Towards a European Civil Code* (4th edn, Kluwer Law International 2011) 399.

– *Principles governing a measure of damages*

IV.E. – 4:102(2) refers to II. – 7:214(2) and (3) when it comes to measuring recoverable damages. The rules under these paragraphs can be summarized as follows.

Firstly, II. – 7:214(2) prescribes a general rule that damages are compensatory. This paragraph provides that an award of damages must place an aggrieved party as nearly as possible in the position in which that party would have been if the contract had not been concluded. I conceive that this underlying principle should be re-formulated so that it fits the franchising context. That is, in the context of the disclosure in franchising, an award of damages must place an aggrieved franchisee as nearly as possible in the position in which the franchisee would have been if the franchisor had, adequately and timely, furnished the franchisee with pre-contractual information or provided current and accurate information.

Secondly, II. – 7:214(3) provides that the rules on damages for non-performance of a contractual obligation apply with any appropriate adaptation. For example, III. – 3:701(3) will be referred to define the word ‘Loss’ since II. – 7:214 does not define that term. The franchisee may not claim damages for positive loss, such as the lost profits or incomes, because the aim of II. – 7:214(2), in conjunction with IV.E. – 4:102(2), is to put the party in the same position as if the franchisor has performed the disclosure duty. Thus, the recovery of damages for loss of expectation, which is a normal case in the event of non-performance, would not be permitted.¹⁷⁷ In addition, III. – 3:705 will also be applied to reduce damages by virtue of II. – 7:214(3).¹⁷⁸ According to III. – 3:705(1), an amount of monetary compensation to be awarded to an aggrieved franchisee may be reduced to the extent that the franchisee could have reduced the loss by taking reasonable steps. Furthermore, the franchisee would not recover any expenses reasonably incurred in attempting to reduce the loss as a result of paragraph (2) of III. – 3:705.

3.4.2.4 Cancellation of a contract¹⁷⁹

The fact that a franchisor does not perform the disclosure duty or the duty to provide complete, current and accurate information may provide a basis for a franchisee to cancel a franchise contract. Under the DCFR, the franchisee may have to resort to the rules governing vitiated consent in Book II to avoid

¹⁷⁷ Bar and Clive (n 122) 529.

¹⁷⁸ Ibid 531.

¹⁷⁹ The DCFR provides the franchisee with special remedies upon the cessation of a franchise relationship. Strictly speaking, the DCFR allows the franchisee to get compensation for a transfer of goodwill and to reimburse for stock, spare parts and materials. These special remedies will be explored in subsection 5.5.2.5 in chapter 5 of the book.

a franchise agreement. Because of the franchisor's non-disclosure or the franchisor's disclosure of incorrect or out-of-date information, the franchisee may conclude the contract under misapprehension. If this is the case, the franchisee may choose to invalidate the franchise agreement on the ground of mistake under II. – 7:201 or fraud under II. – 7:205.¹⁸⁰ This subsection will examine the essential prerequisites for avoiding a franchise contract for mistake and fraud. This subsection will also make remarks on particular rules related to avoiding a franchise contract.

– *Avoidance of a franchise contract for mistake*

Kronman provided that information is the antidote to the mistake.¹⁸¹ This idea implies that the franchisor's non-disclosure of pre-sale information or providing inaccurate or outdated information would induce the franchisee's mistake. Under the DCFR, the franchisee may avoid a franchise agreement for a mistake by satisfying the prerequisites set out in II. – 7:201(1). These conditions are as follows.

First, according to paragraph (a) of II. – 7:201(1), the franchisee needs to plead that it has concluded a franchise contract by serious mistake. Initially, the franchisee must demonstrate that it mistakes the facts or the laws affecting the franchise contract. More importantly, the misapprehension must be serious or material in the sense that, without mistake, the franchisee would not have entered into a franchise agreement or would have done so on fundamentally different terms. In this case, the franchisee also has to prove that the franchisor knew or could reasonably be expected to have known that the franchisee made a material mistake.

Second, according to paragraph (b) of II. – 7:201(1), the franchisee shall demonstrate that the franchisor caused it to make a serious mistake. In the context of disclosure, the franchisee may show that the franchisor caused the franchisee to conclude a franchise contract under a serious misapprehension by failing to comply with the pre-contractual information duty imposed by IV.E. – 2:101, in conjunction with IV.E. – 4:102(1). For example, the franchisee may avoid a franchise contract for mistake, claiming that the franchisor caused

180 In some European countries, courts may determine the validity of a franchise contract based on rules concerning defective consent. For example, in France, the French Supreme Court (*Cour de Cassation*) decided that the franchisor's failure to provide the required information could render a franchise contract void because of a defect in the franchisee's consent. See Cass, com, Dec 5, 2000, pourvoi n°97-21.631. Furthermore, some commentators suggest that an ill-informed party may avoid a contract for mistake and fraud in the case of non-performance of the disclosure duty. See Nils Jansen and Reinhard Zimmermann (eds), *Commentaries on European Contract Laws* (Oxford University Press 2018) 499-500.

181 Anthony T Kronman, 'Mistake, Disclosure, Information, and the Law of Contracts' (1978) 7(1) *The Journal of Legal Studies* 1, 4.

the franchisee to enter into a franchise agreement by furnishing the franchisee with untrue statements about profit projections.

It should be noted that the franchisee's right to avoid a franchise contract may be excluded in two following cases under II. – 7:201(2). First, the franchisee cannot avoid a franchise agreement if the mistake was inexcusable under the circumstances.¹⁸² In other words, the franchisee would not be able to avoid the contract for its careless mistakes.¹⁸³ Second, the franchisee cannot avoid the contract if it assumed the risk of the mistake or, in the circumstances, the mistake should be borne by the franchisee.¹⁸⁴ The drafters of the DCFR exemplify that a party may not be able to avoid a contract if it willingly concludes a contract without knowledge of an important matter surrounding the agreement.¹⁸⁵

– *Avoidance of a franchise contract for fraud*

The franchisor's non-disclosure or disclosure of incorrect or out-of-date information could be fraudulent. Under the DCFR, the franchisee may avoid a franchise agreement for fraud by satisfying the requirements prescribed in II. – 7:205. According to II. – 7:205(1), the franchisee may avoid the franchise contract by showing that the franchisor induced the conclusion of the contract by fraudulent non-disclosure of any information which the disclosure duty requires the franchisor to disclose. The franchisee may avoid the franchise agreement by proving that the franchisor induced the conclusion of the contract by fraudulent misrepresentation. II. – 7:205(2) further elaborates that, in the former case, the non-disclosure is fraudulent if it is intended to induce the person from whom the information is withheld to make a mistake. In the latter case, the misrepresentation is fraudulent if it is made with knowledge or belief that the representation is false and is intended to induce the franchisee to make a mistake.¹⁸⁶ Thus, the right to avoid a contract for fraud under II. – 7:205 would suitably be exercised in the cases of non-performance of the disclosure duty and the duty to provide complete, current and accurate information.

182 The DCFR, II. – 7:201(2)(a).

183 The drafters of the DCFR suggest that the careless mistake should not prevent the avoidance if it is not bothersome for the second party to point out the mistake. *See* Bar and Clive (n 122) 462-63.

184 The DCFR, II. – 7:201(2)(b).

185 Bar and Clive (n 122) 463.

186 The drafters of the DCFR seem to adopt reliance as another prerequisite in the case of fraudulent misrepresentation. Thus, a franchisee can avoid a franchise contract for fraudulent misrepresentation if the franchisee has relied on incorrect information given, thereby deciding to conclude the agreement. In other words, the franchisee may not be able to avoid the contract if the franchisee has never read the fraudulent statement provided before entering into the contract. *See* *ibid* 494.

– *Remarks on particular rules relating to avoidance of a franchise contract*

There are some remarks as regards exercising the right of avoidance, partial avoidance, effects of avoidance, and election of remedies as follows.

(1) *Exercise of the right of avoidance*

According to II. – 7:209, a franchisee may avoid a franchise contract by giving the franchisor notice of avoidance. In this case, the commentaries to this article explain that the franchisee needs not to bring a lawsuit against the franchisor for a judicial order of avoidance.¹⁸⁷ Pursuant to II. – 7:210, the notice of avoidance must be given within a reasonable time, with due regard to the circumstances, after the franchisee knew or could reasonably be expected to know of mistake or fraud. During that reasonable period, II. – 7:211 prevents the franchisee from avoiding a franchise contract if the franchisee confirms the continuation of the contract expressly or impliedly.

(2) *Partial avoidance*

In theory, a franchisee may be confined to avoid particular terms of the agreement. According to II. – 7:213, if a ground of avoidance affects particular terms of a franchise contract, an aggrieved franchisee cannot avoid the entire contract. Suppose the franchisor provides false or incorrect information that causes the franchisee to agree to specific terms of a franchise agreement by misapprehension. In this case, the franchisee can only avoid those affected clauses. Nevertheless, II. – 7:213 makes some exceptions, which allows the avoidance of the entire franchise contract. For instance, the franchisee may avoid an entire franchise contract if it is unreasonable to uphold the remaining contract, giving due consideration to all the circumstances of the case. According to the Comments to II. – 7:213, a fraud case may be considered reasonable to allow an aggrieved party to avoid the whole contract.¹⁸⁸ In my view, partial avoidance of a franchise contract would be scarce as a franchisee typically concludes a franchise agreement in its entirety. Thus, a situation that the franchisee's mistake affects particular clauses of the agreement would be unlikely.

(3) *Effects of avoidance*

In general, the effects of avoidance, as prescribed by II. – 7:212, are threefold.

Firstly, avoiding a franchise contract or particular clauses of a franchise contract will invalidate the contract or the clauses with a retrospective effect.¹⁸⁹ In other words, the avoidance will cancel the contract or those clauses as if they had not been concluded.¹⁹⁰ In this case, a franchise contract

187 Bar and Clive (n 122) 494.

188 Ibid 527.

189 The DCFR, II. – 7:212(1).

190 Bar and Clive (n 122) 524.

or the terms of a contract, which has been avoided by a franchisee, will be set aside at the beginning.

Secondly, the rules on unjustified enrichment will regulate the parties' right to the return of whatever has been transferred or supplied under an avoided contract.¹⁹¹ For example, when avoiding the entire franchise agreement, a franchise relationship is dissolved. In this case, a franchisee may claim a return of an initial fee paid under a franchise contract by virtue of VII. – 1:101, in conjunction with VII. – 5:101.

Thirdly, the transfer of property rules will apply to the ownership of property which has been transferred under an avoided contract.¹⁹² For instance, after avoiding the whole franchise agreement that ends a franchise relationship, the ownership of property will be treated as never having passed to the transferee as a result of VIII. – 2:202(2).

(4) *Election of remedies*

In some cases, the franchisor's conduct that allows avoidance may inflict loss or damage to the franchisee. For example, the franchisor's fraudulent non-disclosure under II. – 7:205(1) may cause financial loss to the franchisee. One may raise the question of whether the franchisee can avoid an entire franchise contract for fraud and concurrently claim damages suffered as a result of fraud. In this case, II. – 7:214(1) makes clear that a franchisee who has the right to avoid the contract is entitled to damages, whether the agreement is indeed avoided or not. Thus, the franchisee needs not to elect one of these possible remedies in the event of the franchisor's non-performance of the disclosure duty or the duty to provide complete, current and accurate information. To put it another way, the franchisee may avoid an entire franchise contract and claim damages for any loss arising out of the mistake or fraud.¹⁹³

3.4.2.5 *Conclusions*

Contract law rules of the DCFR offer three types of civil law remedies in the occurrence of the franchisor's non-performance of the disclosure duty and the duty to provide complete, current and accurate information. Under the remedial regime, a prospective franchisee may compel a franchisor to provide current and transparent information on the required items before entering into a franchise contract. After a franchise agreement is concluded, a franchisee may cancel a franchise contract by avoiding the agreement, entirely or partially, based on mistake or fraud. In either case, the (prospective) franchisee is not

¹⁹¹ The DCFR, II. – 7:212(2).

¹⁹² The DCFR, II. – 7:212(3).

¹⁹³ According to II. – 7:214(2), an amount of monetary compensation will be awarded to place an aggrieved franchisee as nearly as possible in the position that the franchisee would have been if the contract had not been concluded.

precluded from claiming monetary compensation for any loss caused by the franchisor's failure to perform the obligations. Nevertheless, a general principle for calculating damages differs slightly when the franchisee decides to enforce specific performance or avoid an entire franchise contract. In the former case, the franchisee will be placed as nearly as possible in the position in which the franchisee would have been if the franchisor had performed the duties correctly. In the latter case, damages will put the franchisee as nearly as possible in the position in which the franchisee would have been if the contract had not been concluded.

3.4.3 The United States of America (USA)

3.4.3.1 Introduction

In case of non-performance of the franchisor's pre-contractual information duties, a franchisee may bring an action against a franchisor for civil law remedies under state laws.¹⁹⁴ In the sixteen franchise sale states, the franchisee may resort to the rules of franchise sale law and common law for private law remedies. Strictly speaking, the franchisee may rely on the rules on the following types of civil law relief: the enforcement of the franchisor's performance, monetary compensation, and cancellation of a franchise contract. This section will explore the rules governing those threefold remedies in subsections 3.4.3.2, 3.4.3.3, and 3.4.3.4, respectively. Conclusions about the US remedial regime will be provided in subsection 3.4.3.5.

3.4.3.2 Enforcement of performance

State franchise sale statutes ordinarily offer two types of private law remedies: damages and rescission of a contract.¹⁹⁵ For example, in Michigan, the court in *Coffee Beanery v Albert* upholds that Michigan franchise investment law only

¹⁹⁴ At the federal level, the Federal Trade Commission Act (FTCA) provides a wide range of civil actions for a violation of the FTC Rule. According to section 19(b) of the FTCA, the available relief includes, but shall not be limited to, rescission or reformation of contracts, the refund of money and return of the property, the payment of damages, and public notification respecting the rule violation or the unfair or deceptive act or practice. Nevertheless, an individual franchisee cannot bring a lawsuit under the FTCA for those remedies as the US courts have correspondingly held that the FTCA exclusively delegates the right to commence a civil action to the Federal Trade Commission. See eg *Holloway v Bristol-Myers Corp*, 485 F.2d 986, 991, 158 US App DC (CADDC 1973) 212; *Friend v Fryberger, Buchanan, Smith & Frederick, PA*, 2012 WL 503796, (D Minn, 2012) 4; *Nixon v Brent Manning's Quality Preowned, Inc*, 2016 WL 6090735 (W D Ark, 2016) 3. Thus, the examination of private law remedies under federal regulation will be omitted in this section.

¹⁹⁵ Joseph J Fittante, Jr and Suzanne Trigg, 'Chapter 4: Registration', in Rupert M Barkoff et al (eds), *Fundamentals of Franchising* (4th edn, American Bar Association 2016) 171.

permits two types of remedies for a violation of the law: the remedies of damages and rescission.¹⁹⁶ Thus, no special relief is made available that permits a prospective franchisee to enforce the disclosure duty under the disclosure laws.¹⁹⁷ Strictly speaking, no specific remedy would enable the franchisee to compel the franchisor's disclosure of pre-sale information.

In Hawaii, Minnesota, North Dakota, and Washington, the franchise sale statute contains a remedial provision offering catch-all relief. Under the rule, a franchisee may sue a franchisor for other relief as the court may deem appropriate.¹⁹⁸ However, state courts in those jurisdictions have not yet clarified the expression 'other relief as the court may deem appropriate'.¹⁹⁹ Nor do commentaries on this remedial provision provide further explanation. Thus, a series of sanctions that the court may order remains questionable. In my view, this catch-all relief could be interpreted to compel the franchisor to provide pre-sale information or to ensure the truthfulness of the information. This interpretation is given to effectuate the goal of the sale law that aims to equip a prospective franchisee with essential information before concluding a franchise contract. Without this specific way of interpreting, the franchisee would never get the information for deciding whether to enter into a franchise agreement in reality.

It should be noted that the proposed franchise bill could warrant enforcement of specific performance at a state-wide level. Currently, a new Bill cited as 'Fair Franchise Act of 2017' has been introduced to the House of Representatives. The Bill aims to establish certain standards of fair conduct in franchise business relationships.²⁰⁰ Under the Bill, private rights of action are provided in section 11. Unlike the existing disclosure laws, section 11 expressly provides that a franchisee has the right to be awarded injunctive relief in case of a violation of sections of the Bill and the FTC Rule. Since the injunctive relief is used to enjoin any violation or threatened violation of the mentioned statutes, it would employ to enforce a franchisor to comply with the disclosure

196 *Coffee Beanery, Ltd v Albert*, 2006 WL 1330326, (Mich App, 2006) 2.

197 As can be seen, the disclosure duty is not the duty created by an agreement. Instead, it is the legal duty constituted by franchise-specific regulation. Therefore, a remedy of specific performance in contract law would not be applicable as the non-performance of the statutory duty does not amount to a breach of contract that is an important ground for an order of specific performance. See E Allen Farnsworth, 'Legal Remedies for Breach of Contract' (1970) 70(7) *Colum Law Review* 1145, 1149-151; Alan Schwartz, 'The Case for Specific Performance' (1979) 89(2) *Yale Law Journal* 271, 272.

198 Hawaii: HI ST, § 482E-9(b); Minnesota: MN ST, § 80C.17(Subd.1); North Dakota: ND ST, 51-19-12(1); Washington: WA ST, 19.100.190(2).

199 The court in Minnesota has ever denied a claim for punitive damages relying upon this remedy. However, this court has not taken this opportunity to elaborate the scope of the relief. See *Cherrington v Wild Noodles Franchise Company, LLC*, 2006 WL 8443100 (D Minn, 2006) 3.

200 The text of the Bill and its summaries can be retrieved at <<https://bit.ly/3k1k1cC>>.

rules; for example, to provide a disclosure document or update the document.²⁰¹

3.4.3.3 Monetary compensation

A franchisee may sue a franchisor for damages based on several counts under state franchise sale law and common law. This subsection will elaborate on the legal bases on which the franchisee may request an award of damages. This subsection will also address some principles relating to a measure of damages under statutory and common laws.

– Statutory claims

Under state franchise sale laws, a franchisee may claim damages for a violation of disclosure rules and antifraud rules by a franchisor.

(1) Violation of disclosure rules

In twelve franchise sale states, a franchisee may claim damages alleging that a franchisor has violated the disclosure rules.²⁰² In demanding an award of damages, a franchisee must establish that a franchisor did not furnish pre-contractual information in a manner required by the disclosure rules. For example, in *Chicago Male Medical Clinic v Ultimate Management*, the court found that the franchisor violated the rule of the Illinois Franchise Disclosure Act as it failed to deliver a disclosure document containing required informational items to the franchisee.²⁰³ Besides the violation of the disclosure rules, the franchisee must prove that the franchisor's alleged conduct has caused the franchisee to suffer loss or damage.²⁰⁴ In the case *Coffee Beanery*, the court

201 This approach is not a brand-new concept. Injunctions, either preliminary or permanent injunctions, are now made available under section 13(b) of the FTCA. The Federal Trade Commission may file a complaint to seek an injunction that would bar a franchisor from violating the FTC Rule. Since the FTCA does not grant a private right of action to individual franchisees, an aggrieved franchisee must complain to the Commission about potential conduct by a franchisor in violation of the FTC Rule. This complaint would persuade the Commission, upon a reasonable belief, to take a legal action against the franchisor under section 13(b) to enjoin the franchisor's unlawful conduct.

202 California: CA CORP, § 31300; Hawaii: § 482E-9(b); Illinois: IL ST CH 815, § 705/26; Michigan: MI ST, 445.1531; Minnesota: MN ST, § 80C.17(Subd.1); New York: NY GEN BUS, § 691; North Dakota: ND ST, 51-19-12(1); Oregon: OR ST, § 650.020; Rhode Island: RI ST, § 19-28.1-21; South Dakota: SD ST, § 37-5B-49; Virginia: VA ST, § 13.1-571(a); Washington: WA ST, 19.100.190(2).

203 The franchisor will be liable for damages only in the case of non-disclosure of the required items of information. In *Dunkin' Donuts v HWT*, the franchisee's claim for damages was dismissed because the franchisor is not required to disclose the location of competing franchises. See *Dunkin' Donuts v HWT Associates*, No 91-08312, 181 AD 2d 711, 712, 581 NYS 2d 363, 364, 1992 WL 43611, (NY AD 2 Dept, Mar 09, 1992) 712.

204 *RWJ Management Co, Inc v BP Products North America, Inc*, 2011 WL 101727, (ND Ill, 2011) 3.

held that the franchisees failed to show that the franchisor's late disclosure inflicted damage by pointing out that the franchisor tried to enforce unsavory and unanticipated contractual clauses.²⁰⁵ Without the loss sustained, the franchisee would not secure an award of damages.

In terms of culpability, it should be noted that a claimant franchisee may not have to prove that a franchisor intended to violate the disclosure rules. For example, in California, the California Court of Appeals in *Dollar Systems v Avcar Leasing Systems* affirms the district court's judgment holding that there is no requirement of culpability or scienter under the remedial rule. That is, section 31300 of the California Franchise Investment Law does not require a violation of the statute's provisions was made with an intent to violate the law, to injure the franchisee, or to acquire any undue advantage.²⁰⁶ Nevertheless, the district court in the case *Dollar Systems* stated that the franchise investment law required the violation was made knowingly and intentionally. Thus, in recovering damages under the law, the franchisee may have to show that the franchisor's contravention of the disclosure rules was willful.

(2) *Violation of antifraud rules*

A franchisee may also seek an award of damages claiming that a franchisor has violated the antifraud rules. As can be seen in subsection 3.3.3.4, state franchise sale laws' antifraud rule typically prohibits a franchisor from making misrepresentations or untrue statements. In this respect, a franchisee may claim damages alleging the franchisor of making untrue statements of material facts. In doing so, it is said that the franchisee shall demonstrate the following two conditional elements: (1) the franchisor made an untrue statement of a material fact, and (2) the franchisee suffered loss or damage caused by having relied on that statement.²⁰⁷

The first element of the formulation is the franchisor's misrepresentation of a material fact. The franchisee must prove that the franchisor made false statements, not merely predictions and opinions collectively called puffery. For instance, in *Teng Moua v Jani-King of Minnesota*, the Minnesota court held that the franchisor's statements that a franchise was a good business that would continue for a long time were puffery; hence, these statements could not be regarded as untrue.²⁰⁸ However, predictions and opinions can establish misrepresentations in some exceptional cases. For example, in *Governara v. 7-Eleven*, the New York court provided that statements of prediction, such as projections of potential earnings, could be considered misrepresentations if

205 *Coffee Beanery* (n 196) 3.

206 *Dollar Systems, Inc v Avcar Leasing Systems, Inc*, 890 F 2d (CA9 (Cal), 1989) 173.

207 See eg *Enservco, Inc v Indiana Securities Div*, 623 NE 2d 416 (Ind, 1993) 425; *Samica Enterprises LLC v Mail Boxes Etc, Inc*, 460 Fed Appx 664, 665, 2011 WL 6000718, (CA9 (Cal), 2011)1; *Governara v 7-Eleven, Inc*, 2014 WL 4476534 (SDNY, 2014) 4; *Coraud LLC v Kidville Franchise Co, LLC*, 121 F Supp 3d (SDNY, 2015) 393.

208 *Teng Moua v Jani-King of Minnesota, Inc*, 810 F Supp2d (D Minn, 2011) 890.

they implied present facts. In this case, the franchisor had conducted its own analysis of the store's potential earnings, and the estimated annual sales were consistent with these projections. Thus, the court decided that the projections of potential earnings were construed as misrepresentations.

In recovering damages based on the allegation of making misrepresentations, a plaintiff franchisee may not have to demonstrate the franchisor's culpability. For instance, in Indiana, the Supreme Court in *Enservco, Inc v Indiana Securities* concluded that there was no requirement about culpability when alleging the franchisor of making untrue statements of a material fact because the rule focuses on prohibiting the nature of the conduct or its effect, rather than the mind of the violator.²⁰⁹ Likewise, in New York, the court in *Governara v 7-Eleven* provided that the plaintiff franchisees did not have to prove that the misrepresentation or omission of a material fact was made with knowledge of falsity.²¹⁰

Secondly, a franchisee must prove that it suffers loss or damage because of reliance on false statements. Apart from damage suffered, the proof of reliance is a pre-requisite for an award of damages even though franchise disclosure laws do not expressly provide in an antifraud provision.²¹¹ In practice, state courts typically require a claimant franchisee to show that it reasonably relied upon false statements made in the disclosure document.²¹² In deciding whether the franchisee's reliance is reasonable, state courts may take different viewpoints. For example, the court in *Coraud v Kidville* provided that New York adopts a contextual view. That is, the courts will take into account some determinative factors associated with a franchisee, including the acceptance of a clear and direct sign of falsity, the ability to access relevant information, the delivery of written confirmation of the representations' truthfulness, and the franchisee's sophistication.

– Common law claims

In common law, tort law could be resorted to for civil law remedies.²¹³ One of the remedies available under common tort law is monetary compensation

209 *Enservco* (n 207) 422-25. The other Indiana court has affirmed this Supreme Court's decision in the subsequent. See *Gre-Ter Enterprises, Inc v Management Recruiters International, Inc*, 329 F Supp 3d (SD Ind, 2018) 679.

210 *Governara* (n 207) 4.

211 *Simos v Embassy Suites, Inc*, 983 F 2d (CA7 (Wis), 1993) 1410.

212 See eg *Lee v General Nutrition Cos, Inc*, 2001 WL 34032651, (CD Cal, 2001) 6; *U-Bake Rochester, LLC v Utecht*, 2014 WL 223439, (D Minn, 2014) 8.

213 It should be noted that, in the USA, common tort law is the law of the state. Thus, state tort law's rules or theories may vary from state to state. See H Beau Baez III, *Tort Law in*

for damage caused by another.²¹⁴ In claiming damages in tort, an aggrieved franchisee may constitute several causes of action. In the context of violation of franchise sale regulations, the franchisee may claim damages alleging the franchisor of committing fraudulent concealment by silence and fraudulent misrepresentations.

(1) *Fraudulent concealment or deceit by silence*

The first possible cause of action is fraudulent concealment. A franchisee may sue a franchisor based on this theory in some states. For example, in Maryland, the court in *Hanley v Doctors Express Franchising* held that the franchisee might claim damages for the franchisor's fraudulent concealment.²¹⁵ According to the court, the theory of fraudulent concealment encompasses intentional failure to disclose facts that the defendant is legally required to disclose. In claiming damages based on this theory, the plaintiff franchisee needs to plead that the defendant franchisor owed the franchisee the duty to disclose a material fact but failed to disclose that fact with an intention to defraud or deceive the plaintiff.²¹⁶ The franchisee must also show that it took action in justifiable reliance on the concealment, thereby suffering damages as a result of the defendant's concealment.²¹⁷

(2) *Fraudulent misrepresentations*

A franchisee may seek an award of damages alleging a franchisor of engaging in fraudulent misrepresentations. In this case, the plaintiff franchisee must plead that the defendant franchisor misrepresented a material fact, and the franchisor knew that representation was false. Furthermore, the franchisee must demonstrate that the franchisor made that false representation to induce the franchisee's reliance, and the franchisee did reasonably rely upon that

the United States (3rd edn, Kluwer Law International, 2020) 29-30. One example of the variation is that the Virginia courts provided that the state does not recognize any tort liability for negligent misrepresentation. See *Haigh v Matsushita Elec Corp of America*, 676 F Supp (ED Va, 1987) 13; *Joyce v Lincoln Nat Life Ins Co*, 845 F Supp (ED Va, 1993) 354; *Bentley v Legent Corp*, 849 F Supp (ED Va, 1994) 434. Thus, this subsection will not generalize tort rules or theories to represent American tort law of all states. Instead, this subsection will examine these rules or principles by way of example, showing how tort law rules or principles would operate in the franchising context.

214 Sylvia A Law, 'Torts' in Alan B Morrison (ed), *Fundamentals of American Law* (Oxford University Press, 1996) 239.

215 *Hanley v Doctors Exp Franchising, LLC*, 2013 WL 690521, (D Md, 2013) 21-23.

216 One may raise a question as to how to plead the franchisor's culpability. According to the court in *Silvercreek Management v Citigroup*, a plaintiff must state sufficient facts to give rise to a strong inference of fraudulent intent. In establishing that strong inference, the plaintiff may show the facts constituting strong circumstantial evidence of conscious misbehavior or recklessness. See *Silvercreek Management, Inc v Citigroup, Inc*, 248 F Supp 3d (SDNY, 2017) 438-39.

217 *Hanley* (n 215) 21-23.

misrepresentation.²¹⁸ In this case, the franchisee has to state a respondent franchisor's scienter; that is to say, the respondent had knowledge of the falsity of the statement made and an intent to defraud.²¹⁹ More importantly, the franchisee must show that it has suffered injury as a result of the reliance on the misrepresentation.²²⁰

– *Principles governing a measure of damages*

This subsection examines two following rules or principles associated with a measure of damages.

First, under state franchise sale statutes, the nature of damages is twofold: compensatory and punitive damages. In general, damages are of compensatory character as they are awarded to compensate loss or damage sustained by an aggrieved franchisee. In some franchise sale states, courts are confined to award compensatory damages. For example, in New York, the court in *Coraud v Kidville* held that the New York Franchise Sale Act did not permit a franchisee to seek punitive damages because the law was not designed to punish a franchisor.²²¹

Some franchise sale states make an exception to the general principle mentioned above. In Hawaii, South Dakota, and Washington, franchise sale laws introduce the treble-damages scheme, which is a specific form of punitive damages.²²² Under the treble-damages regime, the court may, in its discretion, increase the award of damages to an amount not to exceed three times the actual damages sustained. Nonetheless, it is said that a mere violation of the franchise laws may not warrant the imposition of punitive damages. In some cases, the court may require the franchisor to commit tort involving willful misconduct.²²³

In common tort law, damages can be compensatory, nominal, and punitive.²²⁴ In general, damages are of compensatory character; they are awarded to redress the loss or injury sustained by a plaintiff.²²⁵ In an exceptional case,

218 *Schwartzco Enterprises LLC v TMH Management, LLC*, 60 F Supp3d (EDNY, 2014) 344.

219 See eg *Schlaifer Nance & Co v Estate of Warhol*, 119 F 3d (CA2 (NY), 1997) 98; *Crigger v Fahnestock and Co, Inc*, 443 F 3d (CA2 (NY), 2006) 234; *Silvercreek Management* (n 216) 438.

220 *Whitestone Sav & Loan Ass'n v Allstate Ins Co*, 34 AD2d 787, 787, 311 NYS 2d (NYAD 2 Dept, May 04, 1970) 77.

221 *Coraud* (n 207) 625.

222 Hawaii: HI ST, § 482E-9(c); South Dakota: SD ST § 37-5B-49; Washington: WA ST 19.100.190(3).

223 Mark McLaughlin and Javier H Rubinstein, 'Addressing the Threat of Punitive Damages Claims in Franchise and Dealer Litigation' (1995) 15(1) *Franchise Law Journal* 11, 11. See also *Tom Pappas Toyota, Inc v Toyota Motor Distributors, Inc*, 729 F Supp 71 (ED Mo, 1990) [72].

224 See eg *Murphy v United Steelworkers of America Local No 5705, AFL-CIO*, 507 A2d (RI, 1986) 1346; *Calise v Hidden Valley Condominium Ass'n, Inc*, 773 A 2d (RI, 2001) 839.

225 Richard A Epstein, *Torts* (Aspen Law & Business, 1999) 436.

damages may not be compensatory; they may be awarded as nominal or punitive damages. In the former case, nominal damages will be awarded when the plaintiff shows that it has suffered loss but cannot provide evidence to ascertain the volume of the damage sustained. In the latter case, punitive damages will be awarded to punish a wrongdoer who acted with malice and deter future misconduct. In some states, a claimant may recover punitive damages in fraud claims. For example, in Kentucky, the courts accepted that punitive damages were recoverable if a party had been induced by fraud to conclude a contract.²²⁶ In my view, these revealed principles would be applicable in the franchising context too.

Second, under the statutory and common laws, a general principle of measurement of compensatory damages is that damages will be awarded to recover the actual loss. In general, damages will recover the actual loss, including reliance loss or out-of-pocket loss. This principle can be observed in several state court decisions. For example, in Minnesota, the Supreme Court in *Hughes v Sinclair Marketing* held that the actual damages for misrepresentation to be awarded under the disclosure statute were ordinarily confined to the loss of out-of-pocket, which was compensable under common law misrepresentation. The court provided that it aimed to avoid speculative damages and assured that the damages were measured by the natural and proximate loss suffered by the defrauded party.²²⁷

In exceptional cases, damages may be awarded to recover the expectation loss. In *Hughes v Sinclair Marketing*, the court provided that damages for loss of future profits might be awarded when damages for reliance loss could not return a party to *status quo*.²²⁸ As can be implied from the court decision, if the misrepresentation made by the franchisor caused damage to the franchisee's business, the franchisee may recover damages for the loss of future profits, as the actual loss for fraud, under the franchise statute. This exception would be the same in common law as it is said that most American states allow a plaintiff to recover expectation loss in case of deceit.²²⁹

Regarding recoverable loss, a question arises whether an aggrieved franchisee can recover damages for the lost opportunity. In some cases, the franchisee may argue that it suffers the loss of chance because the franchisee would have chosen another favorable franchise business if, for example, the franchisor had provided the franchisee with a disclosure document containing pre-contractual information. In this case, the recourse will be made to the

226 See eg *Wiley v Adkins*, 48 SW 3d (Ky, 2001) 23; *Raleigh v Edgewood Mobile Homes, Inc*, 2014 WL 505579 (Ky App, 2014) 5; *Karon v Elliott Aviation*, 937 NW 2d 334, 349 (Iowa, 2020) 349.

227 *Hughes v Sinclair Marketing, Inc*, 389 NW 2d (Minn, 1986) 199.

228 *Ibid*.

229 Victor E Schwartz, Kathryn Kelly, and David F Partlett, *Prosser, Wade and Schwartz's Torts* (14th edn, Foundation Press 2020) 1074.

doctrine of loss of chance.²³⁰ In general, the loss of chance doctrine is an approach to causation that is regularly utilized in medical malpractice cases. This doctrine allows a plaintiff to recover damages even though the party cannot prove causation between the defendant's negligence and damage suffered so long as the claimant establishes that the respondent's negligence reduced the chance to recover from the illness.²³¹ In reality, it would seem that courts are reluctant to extend the application of the doctrine in other contexts than medical malpractice cases.²³² Thus, it remains nebulous whether the lost chance doctrine can be applied to lessen the proximate cause in tort lawsuits in the franchising context.

3.4.3.4 Cancellation of a contract

A franchisee may cancel a franchise contract by way of rescission under the state franchise sale statutes and common contract law.²³³ This subsection will address the rescission of a franchise contract based on statutory and common law claims and make remarks on particular rules concerning the rescission relief.

– Statutory claims

Under the franchise sale laws, a franchisee may bring an action against a franchisor to rescind a franchise contract for the two following reasons.

(1) Breach of disclosure rules

Except for Florida, Indiana and Maryland, thirteen franchise sale states recognize a private right of action for rescission for the franchisor's violation of disclosure rules.²³⁴ In this case, a franchisee generally has to plead that a franchisor violated the rules concerning the disclosure of pre-sale information.

230 It should be noted that some states, such as Indiana, has not adopted the theory of the loss of chance. See *McKain v Bisson*, 12 F 3d (CA7 (Ind), 1993) 696.

231 *Crosby v US*, 48 F Supp 2d 924, 926 (D Alaska, 1999) 926; *Hancock v Diamond Offshore Drilling, Inc.*, 2008 WL 3501015, (ED La, 2008) 3; *Mann v United States*, 300 F Supp 3d (NDNY, 2018) 422.

232 See eg *Hancock*, *ibid*; *Lyons v American College of Veterinary Sports Medicine and Rehabilitation, Inc.*, 997 F Supp 2d (D Mass, 2014) 115.

233 Rescission is defined to mean a party's unilateral unmaking of a contract for a legally sufficient reason. This definition is adopted under both statutory and common law. See *Cusamano v Norrell Health Care, Inc.*, 607 NE 2d 246, 250, 180 Ill Dec 352, 356, 239 Ill App 3d 648 (Ill App 4 Dist, 1992) 653; *Jensen v Quik Intern*, 820 NE 2d 462, 466, 289 Ill Dec 686, 690, 213 Ill 2d (Ill, 2004) 127.

234 California: CA CORP, § 31300; Hawaii: HI ST, § 482E-5(b); Illinois: IL ST CH 815, § 705/26; Michigan: MI ST, 445.1531; Minnesota: MN ST, § 80C.17; New York: NY GEN BUS, § 691; North Dakota: ND ST, 51-19-12; Oregon: OR ST, § 650.020(1); Rhode Island: RI ST, § 19-28.1-21; South Dakota: SD ST, § 37-5B-49; Virginia: VA ST, § 13.1-565; Washington: WA ST, 19.100.190; Wisconsin: WI ST, 553.51.

For example, the franchisee may rescind a franchise contract by alleging that the franchisor did not provide the franchisee with a disclosure document before concluding the contract. In other cases, the franchisee may rescind a franchise contract by claiming that the franchisor furnished the franchisee with a disclosure document, which was not amended to reflect material changes in the information contained in the document.

Besides the franchisor's violation, state franchise sale laws may require a franchisee to prove some additional elements when seeking an order of rescission of a franchise contract. For instance, California and New York franchise disclosure laws require the franchisee to show that the franchisor's contravention of disclosure rules is willful. The definition of willfulness in these state laws is identical. In California, the courts provide that the franchisor's violation is willful if the franchisor committed an act or made an omission knowingly and intentionally.²³⁵ Likewise, in New York, the courts understand the term 'willfulness' to mean voluntary and intentional, as opposed to inadvertent.²³⁶

In addition, New York and Wisconsin franchise sale statutes require the franchisee to illustrate that the franchisor's contravention of disclosure rules is material. Under the laws, the materiality requirement entails a significant effect on the franchisee's purchase decision. In New York, the court provided that the materiality test is satisfied if the franchisee can prove that the franchisor's violation of the disclosure rule had an important effect on the franchisee's investment decision. That is, the franchisee must prove that the franchisee would not have gone forward with the franchise sale if he had known the fact of the violation.²³⁷ Thus, the court would dismiss the case if the franchisee cannot show the materiality of the franchisor's violating conduct.²³⁸ This consideration is the same in Wisconsin; the franchisor's contravention must be material to the franchisee when making a decision to buy a franchise.²³⁹

It should be noted that courts would not permit the rescission of a franchise contract if the franchisor's violation of the disclosure rules is technically marginal. For example, in *Two Men and a Truck*, the Michigan court held that the franchisees were not entitled to rescinding the franchise agreement even though the franchisor failed to comply with the disclosure rule by providing

235 *Dollar Systems* (n 206) 172-73; *Migliore* (n 25) 7.

236 *Reed v Oakley*, 661 NYS 2d 757, 759, 172 Misc 2d 655, (NY Sup, 1996) 658; *Mister Softee, Inc v Amanollahi*, 2014 WL 3110000 (DNJ, 2014) 10.

237 *BMW Co, Inc v Workbench, Inc*, 1988 WL 45594, (SDNY, 1988) 2.

238 *A Love of Food I, LLC v Maoz Vegetarian USA, Inc*, 70 F Supp 3d 376, 409 (DDC, 2014) 412.

239 *Braatz, LLC v Red Mango FC, LLC*, 2015 WL 1893194, (ND Tex, 2015) 4-5; *Burger Dynasty, Inc v Bar 145 Franchising, LLC*, 2019 -Ohio- 4006, ¶ 37, 2019 WL 4757420, (Ohio App 6 Dist, 2019) 6.

an offering circular of less than ten business days before the franchise sale.²⁴⁰ In a similar vein, the court in *A Love of Food I v Maoz Vegetarian USA* contended that rescission would be inappropriate if the franchisor's eventual disclosure is a minor deviation from the disclosure timing required under the statute and causes no damage to the franchisee.²⁴¹

(2) *Breach of antifraud rules*

In some franchise sale states, such as Maryland, a franchisee may also rescind a franchise contract for statutory fraud under the franchise sale statutes.²⁴² In Maryland, a statutory misrepresentation claim is considered a fraud claim. Thus, a franchisee may allege the franchisor's fraud or misrepresentation under franchise sale law for a judgment of rescission of a franchise contract. In holding the franchisor liable for rescission under the Maryland franchise law, the court states that the claimant franchisee must prima facie demonstrate that the respondent franchisor made a false or untrue statement, which was material to the franchisee's decision to purchase the franchise. Furthermore, the franchisee must prove that it reasonably relied on that misrepresentation without knowing that the misstatement was false or misleading.²⁴³

– *Common law claims*

In some exceptional cases, a franchisee may cancel a franchise agreement by rescission under common contract law. In contract law, a contract induced by misrepresentation, regardless of whether that misrepresentation is fraudulent, is voidable.²⁴⁴ In the franchising context, if the franchisor's non-performance of pre-contractual duties misled and induced the franchisee to conclude a franchise agreement, the franchisee could avoid or rescind the contract for

240 *Two Men and a Truck/International Inc v Two Men and a Truck/Kalamazoo, Inc*, 949 F Supp (WD Mich, 1996) 506. It should be mentioned that, in drawing such a conclusion, the court considered the other two factors: (1) the franchisees failed to rescind the agreement in a timely manner, and (2) the franchisees were in default of the contract when they tried to avoid the agreement.

241 *A Love of Food I* (n 238) 413.

242 In other franchise sale jurisdictions, such as Illinois, Indiana, Rhode Island, South Dakota, and Wisconsin, the sale laws do not confer the remedial right of rescission on an aggrieved franchisee in the case of violation of antifraud provisions. In this event, the franchisee may only seek the recovery of damages under the statutory laws. However, it might be viable that the franchisee resorts to the right of rescission under contract law rules.

243 *A Love of Food I* (n 238) 404.

244 Marvin A Chirelstein, *Concepts and Case Analysis in the Law of Contracts* (7th edn, Foundation Press, 2013) 88. See also *Russell v Industrial Transp Co*, 258 SW 462, 462, 113 Tex 441 (TEX 1924) 450; *First Nat Bank in Lenox v Brown*, 181 NW 2d 178 (Iowa 1970) 182; *Citizens Standard Life Ins Co v Muncy*, 518 SW 2d 391 (Tex Civ App, 1974) 394; *Matter of Topco, Inc*, 894 F2d 727, 739 (CA5 (Tex), 1990) 739.

fraudulent and innocent misrepresentation.²⁴⁵ For example, the Texas court provided that the franchisee might avoid its obligations under the franchise agreement if the franchisor negligently misrepresented facts in a disclosure document.²⁴⁶

In rescinding a contract for fraudulent and innocent misrepresentation, the franchisee has to prove the elements of both misrepresentations imposed by state law. For example, under Michigan law, the franchisee must prove that the franchisor made false representations of past or existing facts.²⁴⁷ Furthermore, the franchisee must show that it relied on these misrepresentations when concluding a contract.²⁴⁸ In case of fraud, the franchisee must also prove that the franchisor knew or should have known that the representations were false and the franchisor intended the franchisee to act upon them.²⁴⁹ Ultimately, the franchisee must demonstrate that it has suffered an injury because of reasonable reliance on the franchisor's misrepresentation.²⁵⁰

– *Remarks on particular rules concerning rescinding a contract*

There are some remarks as regards exercising the power of rescission and avoidance, rescission and avoidance for parts of a contract, effects of rescission and avoidance, and election of remedies.

(1) *Exercise of the right of statutory and common law rescission*

The requirements for rescinding a franchise contract under state disclosure laws may vary from state to state. Some franchise sale states may allow a franchisee to rescind or avoid a franchise contract at its option. In Virginia, the Virginia Retail Franchising Act permits the franchisee to declare a franchise contract void if the franchisor acted in contravention of the law's rules.²⁵¹ In this case, the franchisee must send a written declaration of avoidance to

²⁴⁵ In this case, the terms 'rescission' and 'avoidance' have the same sense; they are remedies for common law misrepresentation that cancel a contract or agreement from its inception. See *Dow Chemical Co v US*, 226 F 3d 1334, 1345 (CA Fed, 2000) 1345.

²⁴⁶ *Carousel's Creamery, LLC v Marble Slab Creamery, Inc*, 134 SW 3d 385 (Tex App Houston [1 Dist], 2004) 404.

²⁴⁷ See eg *Hi-Way Motor Co v International Harvester Co*, 247 NW 2d 813, 816, 398 Mich 330, 336 (Mich 1976) 336; *Marrero v McDonnell Douglas Capital Corp*, 505 NW 2d 275, 279, 200 Mich App 438 (Mich App, 1993) 444; *Cook v Little Caesar Enterprises, Inc*, 210 F 3d 653, 658 (CA6 (Mich), 2000) 658; *Bucciarelli v Nationwide Mut Ins Co*, 662 F Supp 2d 809, 815 (ED Mich, 2009) 815; *Fuller v Shell Point Mortgage Servicing*, 2017 WL 4326100 (WD Mich, 2017) 9.

²⁴⁸ See eg *Nieves v Bell Industries, Inc*, 517 NW 2d 235, 238, 204 Mich App 459 (Mich App, 1994) 464; *Fuller*, *ibid*.

²⁴⁹ See eg *Novak v Nationwide Mut Ins Co*, 599 NW 2d 546, 553, 235 Mich App 675 (Mich App, 1999) 688; *Fuller*, *ibid*.

²⁵⁰ See eg *State-William Partnership v Gale*, 425 NW 2d 756, 761, 169 Mich App 170 (Mich App, 1988) 178; *Novak*, *ibid* 688; *Fuller*, *ibid*.

²⁵¹ VA ST, § 13.1-565.

the franchisor via registered or certified mail to avoid a franchise contract.²⁵² Conversely, other states seem to require a franchisee to bring a rescission claim to courts. For example, the North Dakota franchise investment law states that a franchisee may bring an action for rescission for the franchisor's violation of the law.²⁵³ According to the North Dakota Supreme Court, the franchisee is not entitled to automatic rescission of a franchise agreement.²⁵⁴ In other words, the franchisee must bring the claim to the court for an award of rescission of a franchise contract.

Unlike the franchise sale regulations, the requirements for rescinding a contract under state common law seem to be identical; a franchisee may not be able to rescind a franchise contract *ex curia*. For example, in Michigan, rescission for misrepresentation is an equitable remedy.²⁵⁵ Thus, the Michigan courts have correspondingly contended that rescission is not a matter of right. Instead, rescission is a remedy that a court may grant within its discretion. In this case, the court must balance the equities to determine if the claimant is entitled to an award of rescission. In other words, the court is not required to grant the relief, but it must determine if a grant of rescission is sound and proper under the circumstances of each particular case.²⁵⁶

(2) *Partial rescission and avoidance*

Neither state franchise sale statutes nor judicial decisions on the laws mention the possibility of partial rescission of a franchise agreement. In my view, the rules in this regard might follow common contract laws, which seem to address the partial rescission issue in a similar fashion. For example, in California, a general rule is that the rescission of a contract must be total; an aggrieved party must rescind an entire contract and cannot reserve any favorable right under the contract. The total rescission requirement will be exempted in the case of the severability of contractual terms. An aggrieved party may rescind a contract partially if an agreement is severable and divisible. The test for determining the severability is that a contract is not divisible if the parties intend to treat

252 The franchisee is confined to certain temporal limitations. Suppose the franchisee aims to declare a franchise contract void because the franchisor failed to furnish a disclosure document at least 72 hours before the conclusion of a franchise contract. In that case, the franchisee has to send a written declaration of avoidance within 30 days after the execution of the contract. See VA ST, § 13.1-565(3).

253 ND ST, 51-19-12(1).

254 *Peck of Chehalis, Inc v C K of Western America, Inc*, 304 NW 2d 91 (ND, 1981) 98.

255 *Titan Ins Co v Hyten*, 817 NW 2d 562, 569, 491 Mich 547 (Mich, 2012) 558; *Northland Radiology, Inc v USAA Casualty Insurance Company*, 2020 WL 3394549, (Mich App, 2020) 3.

256 *Amster v Stratton*, 244 NW 201, 202, 259 Mich 683 (Mi 1932) 687; *Bazzi v Sentinel Insurance Company*, 919 NW 2d 20, 30, 502 Mich 390 (Mich, 2018) 409; *Northland Radiology*, *ibid*.

the agreement as an entire contract.²⁵⁷ Likewise, in Iowa, the Supreme Court stated the rules that, in general, rescission must be of the entire contract. However, partial rescission may be made in the case of severable provisions, which depend upon the parties' intention.²⁵⁸

(3) *Effects of rescission and avoidance*²⁵⁹

Both statutory and common law rescission produce the same effects; they will annul a franchise relationship as if it never exists and restore the parties to their initial status.²⁶⁰ For example, in Illinois, the court in *Cusamano v Norrell Health Care* defined the word 'rescission' under the Franchise Disclosure Act of 1987 to mean the cancellation of a contract and restoration of the parties to their initial status.²⁶¹ In this case, the rights of the parties under the agreement will be vitiated or invalidated after the rescission of the contract takes place.²⁶² Besides, the parties have to make the restoration; they will be required to return any consideration received and set off any benefits received under the contract.²⁶³ In common, it is widely accepted that the rescission or avoidance for misrepresentation will revoke a contract and restore the parties to *status quo ante*. In this respect, both parties are entitled to the restitution of any benefits received under the agreement.²⁶⁴

(4) *Election of remedies*

In some cases, particularly fraud cases, an aggrieved party may be entitled to concurrent private law remedies: damages and rescission. In these events, a classical rule of common law is that an injured party has to make a prompt election because the party cannot seek both damages and rescission awards for the same alleged conduct. For instance, in *Merritt v Craig*, the court affirmed the election rule that, upon the discovery of fraud, the party must either choose to seek rescission and restoration or ratify the contract and claim damages.²⁶⁵

257 *Simmons v California Institute of Technology*, 209 P2d 581, 587, 34 Cal 2d 264 (CAL 1949) at 275; *Yeng Sue Chow v Levi Strauss & Co*, 122 Cal Rptr. 816, 822, 49 Cal App3d 315 (Cal App 1975) 326; *IMO Development Corp v Dow Corning Corp*, 185 Cal Rptr 341, 345, 135 Cal App 3d 451 (Cal App, 1982) 458.

258 *Karon* (n 226) 349.

259 Some franchise relationship states offer a franchisee the auxiliary remedies upon the cessation of a franchise relationship. These remedies will be explored in subsection 5.5.3.5 in chapter 5.

260 See eg *Horan v Blowitz*, 148 NE 2d 445, 449, 13 Ill 2d (Ill 1958) 132; *Rudman v Cowles Communications*, 330 NY S2d (NY, Feb 09, 1972) 43; *Damon v Groteboer*, 937 F Supp 2d (D Minn, 2013) 1087; *Pardo v Mecum Auction Inc*, 77 F Supp 3d (ND Ill, 2014) 711.

261 *Cusamano* (n 233).

262 *Koretz v All Am Life & Cas Co*, 243 NE 2d 586, 589, 102 Ill App 2d 197 (Ill App 1968) 203.

263 *Felde v Chrysler Credit Corp*, 580 NE 2d 191, 199, 162 Ill Dec 565, 573, 219 Ill App 3d 530 (Ill App 2 Dist, 1991) 542.

264 Williston on Contracts (4th ed), § 69:47, West Law, May 2021 Update.

265 *Merritt v Craig*, 746 A 2d 923, 927, 130 Md App (Md App, 2000) 358.

In the context of franchise sale regulation, courts seem to adopt the rule of the election of remedies as well.²⁶⁶ Thus, if the franchisee retains the right to damages and rescission for the franchisor's violation of the franchise sale statute, the franchisee must elect to affirm the agreement and claim damages or rescind the contract and claim restitution.

3.4.3.5 Conclusions

In the USA, the remedial regime that permits an aggrieved franchisee to seek private law remedies can be divided into statutory and common law regimes. In franchise sale states, the franchisee may seek certain civil law relief under the state statutes. Generally, the franchisee may recover damages and rescind a franchise contract if the franchisor violates the rules of franchise sale laws. In some jurisdictions, the franchise sale statute offers a catch-all remedy, which would enable the franchisee to apply for the remedy of enforcement of performance. Nevertheless, this assumption has not been affirmed by state courts yet. Additionally, an aggrieved franchisee may resort to common law rules to recover tort law damages and rescind a franchise contract for misrepresentation. The franchisee may do so since the franchise sale statutes do not exclude the possibility of recourse to other remedial regimes. Resorting to the common law remedies would also be a conventional approach in other states that have not introduced their franchise sale law.

3.4.4 Australia

3.4.4.1 Introduction

The franchisor's non-performance of pre-contractual duties under the Franchising Code of Conduct permits an aggrieved franchisee to resort to private law remedies under the Competition and Consumer Act 2010 (CCA) and the Australian Consumer Law (ACL). This inference is affirmed by the High Court of Australia in *Master Education Service v Ketchell* providing that a contravention of the Franchising Code of Conduct gave rise to remedies under the Trade Practices Amendment (Fair Trading) Act 1998 (Cth).²⁶⁷ Under the CCA and the ACL, the franchisee may seek remedies to compel the franchisor's action, claim monetary compensation, and set aside a franchise contract. Furthermore,

266 *Geri's West, Inc v Ferrall*, 505 NE 2d 1348, 1351, 106 Ill Dec 557, 560, 153 Ill App 3d 579 (Ill App 2 Dist, 1987) 584; *WW, LLC v Coffee Beanery, Ltd*, 2013 WL 3776944, (D Md, 2013) 10.

267 This statute is the predecessor of the CCA and the ACL.

common law would secure the latter two remedies.²⁶⁸ This section will examine the possibility of seeking the three mentioned remedies in subsections 3.4.4.2, 3.4.4.3, and 3.4.4.4. Subsection 3.4.4.5 will conclude on the remedial system under the Australian legal system.

3.4.4.2 *Enforcement of performance*

A franchisee may seek an order of injunctions under the CCA and the ACL to compel the franchisor's action and inaction.

– *Injunctions under the CCA*

Section 80 of the CCA empowers the court to grant, upon application, an injunction in such terms as the court determines to be appropriate in case of actual and anticipated contraventions of provisions of the CCA. According to Bruce, the court may grant a mandatory injunction that requires a person to engage in certain conduct, according to paragraph (5) of section 80.²⁶⁹ In the context of disclosure, a prospective franchisee may seek an order under section 80 to compel the franchisor's specific actions before the conclusion of a franchise agreement. For example, a prospective franchisee may enforce a franchisor to perform the disclosure duty by providing the franchisee with some missing items of information in the disclosure document. Moreover, a prospective franchisee may enforce the franchisor to furnish the franchisee with the most updated and accurate pre-sale information.

In seeking the injunctive relief in the cases exemplified above, the prospective franchisee needs to ensure that it satisfies the constituent element prescribed by paragraph (1)(ii) of section 80. That is, the applicant franchisee must demonstrate that the alleged franchisor has engaged or is proposing to engage in conduct that constitutes or would constitute a contravention of section 51ACB prohibiting a corporation from infringing an applicable industry code in trade or commerce. As the Code is a mandatory industry code made by virtue of section 51AE, a franchisor's violation of the Code would, in turn, violate section 51ACB of the CCA. Thus, the franchisor's non-performance of the disclosure duty and the obligation of good faith imposed by the Code will be considered a contravention of section 51ACB. In this case, the franchisee may compel the franchisor by an injunction to provide the franchisee with the missing

²⁶⁸ Since the disclosure duties of information are not contractual obligations, the franchisee may not seek an order of specific performance and injunctions under common contract law. See J W Carter, *Contract Law in Australia* (7th edn, LexisNexis 2018) 923.

²⁶⁹ Alex Bruce, *Australian Competition Law* (4th edn, LexisNexis 2021) 349.

informational items.²⁷⁰ The franchisee may also compel the franchisor by injunctive relief to provide the informational items, which are current and accurate.

However, if a prospective franchisee seeks a grant of interim or interlocutory injunctions under section 80(2), the franchisee must also satisfy additional threshold requirements to secure the interlocutory injunctions.²⁷¹ As far as case law is concerned, Australian courts have not laid down any specific requirements in the context of non-performance of the disclosure duties. In this case, it could be argued that the court decisions articulating the general requirements for seeking interim injunctive relief can be utilized by analogy. For example, the requirements summarized by Digby J in *Delahunt v Swim Loops* could be followed.²⁷² In summary, an applicant franchisee must, in general, demonstrate the existence of a serious issue, a likelihood of success at trial in respect of the issue, the injury to be suffered, which damages would not adequately redress, and the balance of convenience that favors the grant of the injunction.²⁷³

– *Injunctions under the ACL*

In practice, it would seem that franchisor's certain conduct towards its franchisees may fall within the ambit of prohibitions by the ACL. For example, a franchisor can be alleged of misleading prospective franchisees in violation of the ACL.²⁷⁴ Thus, the civil sanctions imposed by the ACL may apply in the context of negotiation for a franchise agreement. In this case, a prospective franchisee may compel the franchisor's action by applying for a grant of an

270 It should be noted that there has been no case where a potential buyer of a franchise applies for injunctions to enforce the execution of the franchisor's duty of disclosure. Nevertheless, the injunctive relief has been applied by the Australian Competition and Consumer Commission (ACCC) to compel the franchisor to include some mandatory items of information in the disclosure document. For example, in *ACCC v Morild*, the respondent franchisor was ordered to include information about the relevant business experience of the franchisor's officers in its future disclosure documents. See *Australian Competition and Consumer Commission v Morild Pty Ltd*, [2017] FCA 1308 [161].

271 *Castlemaine Tooheys Limited v The State of South Australia* (1986) 161 CLR 148, 153; *Australian Broadcasting Corporation v Lenah Game Meats Pty Limited* (2001) 208 CLR 199 [9]–[13]; *W Hoy Pty Ltd v WTH Pty Ltd*, [2018] FCA 310 [4]; *ACCC v Ultra Tune Australia Pty Ltd* [2019] FCA 12.

272 In this case, the franchisees were seeking interlocutory injunctions because the franchisor terminated the franchisee and license deeds and re-possessed the franchise business.

273 *Delahunt* (n 156) [39]. See also *Girchow Enterprises Pty Ltd v Ultimate Franchising Group Pty Ltd* [2021] FCA 1579, citing Gummow and Hayne JJ in *Australian Broadcasting Corporation v O'Neill* [2006] HCA 46; (2006) 227 CLR 57 [65].

274 ACCC, '\$4.2 million in penalties ordered against former car wash franchisor Geowash and two executives' (ACCC, 24 January 2020) <<https://bit.ly/3hkvZKo>> accessed 21 January 2022; ACCC, 'Geowash franchise appeal dismissed' (ACCC, 22 June 2021) <<https://bit.ly/3hkvZKo>> accessed 21 January 2022.

injunction under section 232 of the ACL. In obtaining the injunctive relief under section 232, the franchisee must allege that the franchisor's conduct constitutes or would constitute, among other things, a contravention of a provision of Chapter 2, 3, or 4 of the ACL. In this regard, one possible legal basis is section 18 of the ACL prohibiting misleading or deceptive conduct in trade or commerce.

In applying for injunctive relief based on section 18, a prospective franchisee must pointedly plead that the franchisor engaged in conduct in trade or commerce. For example, the franchisee may allege that the franchisor omitted from providing the franchisee with certain informational items in a disclosure document. As far as case law is concerned, the franchisor's deliberate omission from disclosing the information would establish the element of engaging in conduct in trade or commerce.²⁷⁵ The franchisee needs to demonstrate that the franchisor's intentional omission was misleading or deceptive or was likely to mislead or deceive. Australian courts seem to have a common precept that silence can constitute misleading or deceptive conduct. In particular, the failure to perform the duty to disclose information would be considered misleading after having regard to all the relevant circumstances.²⁷⁶ This tenet would arguably be applied in the context of non-disclosure in franchising. Thus, in theory, it would be said that the franchisee may compel the franchisor by an injunction under the ACL to disclose information so that the franchisee is not misled or deceived.

3.4.4.3 Monetary compensation

In the case of non-performance of the disclosure duty and the duty to provide complete, current and accurate information, a franchisee may hold a franchisor accountable for damages under the CCA and the ACL. The franchisee may also claim damages under common tort and contract law since the specific legislation does not preclude the application of the pre-existing civil remedies.²⁷⁷ This subsection will examine legal bases on which the franchisee may seek an award of damages. This subsection will also address some principles governing a measure of damages under statutory and common laws.

– Statutory claims

An injured franchisee may recover damages by virtue of section 82 of the CCA, as well as section 236 of the ACL. These two provisions constitute an action

²⁷⁵ *Spedley Securities Ltd (in liq) v Bank of New Zealand* (1991) 26 NSWLR 711.

²⁷⁶ *Rhone-Poulenc Agrochimie SA v UIM Chemical Services Pty Ltd* (1986) 12 FCR 477; *Australian Competition and Consumer Commission v CC (NSW) Pty Ltd*, [1999] 92 FCR 375 [205]; *National Australia Bank Ltd v Meeke*, [2003] WASC 235 [13].

²⁷⁷ *Giles and Ward* (n 75) 27.

for damages that allows a person to recover the amount of loss or damage sustained as a result of a contravention of a provision of the statutes. In seeking an award of damages, the claimant franchisee must satisfy the conditional elements of the provisions. Under section 82 of the CCA, the franchisee needs to prove that the franchisor's contravention of provisions of the Franchising Code of Conduct occurs, thereby inflicting the loss or damage to the franchisee. Under section 236 of the ACL, the franchisee must demonstrate that the franchisor violated provisions of the ACL, such as section 18, resulting in the franchisee's loss or damage. As can be seen, the loss or damage sustained is the gist of an action for monetary compensation. The claimant franchisee must prove a causal link between the franchisor's contravening conduct and the loss or damage suffered.²⁷⁸

– *Common law claims*

An injured franchisee may bring an action for deceit or fraudulent misrepresentation to claim tortious damages in some exceptional cases. In common law, the franchisee must demonstrate that the franchisor made false representations of material facts by not performing the duty to disclose facts or affirmatively misrepresenting facts to induce the franchisee to conclude a franchise agreement. More importantly, the franchisee has to prove that the franchisor made those false representations of facts fraudulently. That is to say, the franchisee made representations without belief in the truth of the representations, or the franchisor made representations by not caring whether the representations were true. In this case, the franchisee needs to prove the franchisor's state of mind.²⁷⁹ Eventually, the franchisee must show that it has suffered loss or damage due to the reliance on the franchisor's fraudulent misrepresentations.²⁸⁰

The franchisee may bring an action for breach of contract to claim damages. Claiming damages on this basis is feasible if pre-contractual representations are subsequently incorporated into the terms of a franchise contract. In *Alati v Kruger*, the High Court held that the plaintiff might sue for damages for breach of contract if the pre-contractual statement was clearly formed one of the terms of the contract.²⁸¹ In this case, the franchisee needs to plead that the franchisor makes a representation in the course of negotiation and that representation forms part of a franchise agreement as a clause or term of the agreement. For example, a franchisor may describe that a franchisee will conduct a franchised business in an assigned territory without other competing franchised businesses. If that representation is also assured in a franchise

278 *Multigroup Distribution Services Pty Ltd v TNT Australia Pty Ltd*, [1996] WL 34917309.

279 *Carter* (n 268) 376-88.

280 *Clancy v Prince*, [2001] NSWSC 85 [61].

281 *Alati v Kruger* [1955] HCA 64; 94 CLR 216.

contract, the franchisee may plead that the assurance is false to claim damages for breach of warranty, which is a breach of contract.

– *Principles governing a measure of damages*

This subsection examines the principles associated with the aims and measure of damages as follows.

First, concerning the aims of damages, statutory and common law damages are compensatory; the money will be awarded to compensate for actual loss or damage sustained.²⁸² Nevertheless, the statutory and common law damages differ in terms of awarding punitive damages. Under Australian common law, damages in tort law can be awarded as exemplary damages to punish a defendant.²⁸³ This type of damages is said to be available when the defendant's conduct is malicious and shows a contumelious disregard of the plaintiff's rights. Accordingly, exemplary damages are frequently awarded for intentional torts, such as the tort of deceit. Additionally, punitive damages can be granted if the defendant has intentionally or recklessly infringed the plaintiff's rights to make profits or to cut expenses.²⁸⁴ In contrast, the CCA and the ACL do not permit courts to award punitive damages for any violation of the laws.

Second, statutory and common law damages may differ regarding a measure of damages. In common law, a measure of tortious damages is well established; it is said that damages in tort intend to put the plaintiff as nearly as possible into the same position as the plaintiff would have been if the wrongful conduct had not been done.²⁸⁵ In contract law, damages will be awarded to put the injured party in the same position as he or she would have been in had the contract been performed.²⁸⁶ Conversely, section 82 of the CCA and section 236 of the ACL do not lay down a standard for measuring statutory damages. Taking the CCA as an example, Gaudron J in *Marks v GIO Australia Holdings* articulates that an action for damages in the CCA is not confined by analogy with actions in tort.²⁸⁷ This articulation implies that a measure of damages in tort law may not necessarily be utilized to calculating

282 *Wardley Australia Ltd v Western Australia*, (1992) 175 CLR 514, 526.

283 *XL Petroleum (NSW) Pty Ltd v Caltex Oil (Aust) Pty Ltd* (1985) 155 CLR 448, 472.

284 Joanna Kyriakakis and others, *Contemporary Australian Tort Law* (Cambridge University Press 2020) 501-04.

285 *Ibid* 498. See also *Registrar of Titles (WA) v Spencer* (1909) 9 CLR 641, 645.

286 See eg *Wenham v Ella*, [1972] HCA 43, per Gibbs J; *Commonwealth v Amann Aviation Pty Ltd* [1991] 174 CLR 64, 98; *Darmody v National Centre Automotive* [2003] FMCA 358 [a]; *Roluke Pty Ltd v Lamaro Consultants Pty Ltd* [2008] NSWCA 323 [78].

287 *Marks v GIO Australia Holdings Ltd* [1998] 196 CLR 494 [17] per Gaudron J.

statutory damages.²⁸⁸ In this case, courts may arguably find a proper measure for the damages.²⁸⁹

Concerning the calculation of damages, a question arises as to whether a claimant franchisee can recover damages for the loss of chance under the statutes and tort law. From a statutory viewpoint, it remains uncertain whether an injured party may be awarded damages for the lost chance by virtue of section 82 of the CCA and section 236 of the ACL. As mentioned in the preceding paragraph, courts may find an appropriate measure to calculate damages. In this respect, the recovery of damages for the lost chance would be possible. In tort law, it is said that the loss of the chance of the better outcome, which is valuable, can be recoverable.²⁹⁰ Thus, it would be likely that the franchisee recovers damages for the loss of opportunity under tort law rules.

3.4.4.4 Cancellation of a contract

A franchisee may cancel a franchise contract by way of rescission under the CCA and the ACL, and common contract law. This subsection will address the rescission of a franchise contract based on statutory and common law claims and offer remarks on particular rules concerning the relief.

– Statutory claims

Under section 87 of the CCA and section 238 of the ACL, a franchisee may seek an order declaring a contract to be void. Taking the CCA as an example, paragraph (2) of section 87 provides that a court has authority to order a wide range of orders, including a rescission order declaring the whole or any part of a contract to be void.²⁹¹ In seeking the declaration of avoidance under the CCA, the franchisee has to demonstrate that the franchisor violates the Franchising Code of Conduct's provisions. For example, the Full High Court of Australia in *SPAR Licensing v MIS QLD* decided that the franchisor contravened the Franchising Code of Conduct by failing to give the franchisee a disclosure document at least 14 days before the entry into a franchise contract. In this case, the court held that setting aside a franchise agreement was an appropriate

288 In case of statutory misrepresentation, some courts may regard a measure of damages in the tort of deceit as a proper measure that will be used by analogy. See eg *Argy v Blunts & Lane Cove Real Estate Pty Ltd*, [1990] 26 FCR 112 per Hill J.

289 Arlen Dukes, *Corones' Competition Law in Australia* (7th edn, Thomson Reuters 2018) at [18.230].

290 Caroline Sappideen and Prue Vines (eds), *Fleming's The Law of Torts* (10th edn, Thomson Reuters 2011) 239-41.

291 In avoiding a contract, the court may, if it thinks fit, order that the contract is void *ab initio* or at all times on and after the specific date. See The CCA, s. 87(2)(a).

remedy for the breach of the Code, and the contract was rescinded from the date of judgment on appeal.²⁹²

Under both statutes, an applicant franchisee must also demonstrate its actual or anticipated suffering of loss or damage caused by the franchisor's contravening conduct. Taking the CCA as an illustration, the court can declare a franchise contract to be void in whole or in part only if the declaration will compensate, prevent, or reduce the franchisee's loss or damage.²⁹³ In the CCA, section 87(1A)(c) provides that the court must consider that an order concerned will compensate the claimant in whole or in part for the loss or damage or prevent or reduce the loss or damage. In this case, the court may issue an order under section 87 insofar as the order will compensate, prevent, or reduce the identified or future loss or damage.²⁹⁴ That formulation applies to the issuance of the declaration of avoidance under section 87(2)(a) as well.

– *Common law claims*

A franchisee may rescind a franchise contract for misrepresentation as it renders a contract voidable. In this case, rescission is considered the main remedy for that misrepresentation.²⁹⁵ In rescinding a contract for misrepresentation, it is accepted that an aggrieved party may rescind a contract for either a fraudulent or innocent misrepresentation.²⁹⁶ In any case, a plaintiff franchisee needs to satisfy the elements of the misrepresentation, which ordinarily include a false statement of facts; the intention to induce reliance, and materiality. From these conditions, the non-performance of the duty of disclosure required by law could amount to a misrepresentation.²⁹⁷

– *Remarks on particular rules concerning rescinding a contract*

(1) *Exercise of the right of rescission*

The rules on rescission under the CCA and the ACL and common law may differ in some cases. On the one hand, statutory rescission is considered rescission

292 *SPAR Licensing* (n 82) [161]-[165].

293 In ordering rescission under section 87, the court may consider some equitable principles as guidelines for the exercise of its discretion. However, it is said that those equities are not necessarily exclusive. For example, in *Munchies Management v Belperio*, the court concluded that the presence or absence of fraudulent conduct might be vital when it comes to ordering rescission at common law. Nevertheless, those matters may not be significant in the exercise of the power to order an appropriate remedy under section 87. See *Munchies Management Pty Ltd v Belperio* [1988] 58 FCR 274.

294 See eg *Deane v Brian Hickey Invention Research Pty Ltd* [1988] ATPR 49,608, [17]; *Rafferty and Another v Madgwicks* [2012] 203 FCR 1 [225].

295 *Carter* (n 268) 374.

296 *Nadinic v Drinkwater*, [2017] NSWCA 114 [23]-[33].

297 *Carter* (n 268) 376-86.

in equity.²⁹⁸ Thus, in rescinding a franchise contract under the CCA and the ACL, a franchisee needs to apply for the court's declaration of avoidance. On the other hand, common law rescission for fraudulent misrepresentation is regarded as rescission at law.²⁹⁹ In this case, an aggrieved party may disaffirm a contract.³⁰⁰ This statement implies that rescission at law is a self-help remedy, meaning the innocent party may elect to rescind a contract on his/her own.³⁰¹ Based on this notion, the franchisee will not have recourse to a court judgment declaring that the election of rescission is effective.³⁰² In electing to rescind a franchise contract, the franchisee would have to manifest its intention to rescind and communicate that intention to the franchisor.³⁰³ For example, in the case *Blow Dry Bar Franchising*, the franchisee alleged the franchisor of inducing the conclusion of a franchise agreement by misrepresentations about the profitability of a franchised business. Because of false representations, the franchisee rescinded the franchise agreement, and the court affirmed that the franchisee was entitled to rescind the agreement.³⁰⁴

(2) Partial rescission

In principle, statutory and common law rescission will set aside or annul an entire franchise contract.³⁰⁵ However, avoiding parts or specific terms of a franchise contract seems to be allowable by partial avoidance under statutory laws. Section 87(2) of the CCA and section 243(a) of the ACL identically state that the court can declare the whole or any part of a contract to be void. In this respect, upon the application, the court may avoid a franchise contract partially. In practice, Australian courts may avoid a particular contractual clause on the basis of an unfair contract term. In this case, the rest of the terms remain applicable.³⁰⁶ In addition, partial rescission of a contract is possible under common contract law. Nevertheless, the partial rescission can be made

298 *Carbone v Metricon Homes Pty Ltd*, [2018] NSWCA 296 [39].

299 *Nadinic* (n 296) [28].

300 See eg *Alati* (n 281) 223-24; *Munchies Management Pty Ltd v Belperio*, (1988) 58 FCR 274; *Highfield Property Investments Pty Ltd v Commercial & Residential Developments (SA) Pty Ltd*, [2012] SASC 165 [284]; *Gutnick v Indian Farmers Fertiliser Cooperative Ltd*, [2016] VSCA 5 [21].

301 Janet O'Sullivan, 'Rescission as a Self-Help Remedy: A Critical Analysis' (2000) 59 Cambridge Law Journal 509, 511-12.

302 *Carter* (n 268) 394-95.

303 See eg *Car and Universal Finance Co Ltd v Caldwell* [1965] 1 QB 525, 550; *Wagdy Hanna and Associates Pty Ltd v National Library of Australia* (2012) 267 FLR 356, 373; *Highfield Property Investments* (n 300) [284].

304 *Carazi* (n 165) [2],[30],[40], and [49].

305 *Gutnick* (n 300) [24].

306 ACCC, 'Contracts' <<https://bit.ly/3YBkTnC>> accessed 19 December 2022. An example of an unfair contract term in a franchise agreement can be found in the case *Back In Motion Physiotherapy*. See ACCC, 'Back In Motion Physiotherapy to remove alleged unfair contract terms for franchisees' (ACCC, 21 September 2020) <<https://bit.ly/3YLkxLx>> accessed 19 December 2022.

in limited cases where the affected contract terms are severable and justice so demands.³⁰⁷

(3) *Effects of rescission*

Statutory and common law rescission of an entire franchise contract will similarly annul the contract. After a contract is rescinded, *restitutio in integrum* is required; the parties are to be rehabilitated and restored, as far as may be, to the position they occupied before the contract was made.³⁰⁸ Moreover, statutory and common law rescission will generally avoid the contract at its inception or *ab initio*.³⁰⁹ Section 87(2) of the CCA and section 243(a) of the ACL concurrently provide that the court may declare the contract to be void *ab initio*. Nevertheless, the statutes permit the court to declare the avoidance of the contract as it thinks appropriate against the person who engaged in the conduct that infringed the laws. For example, the court may declare the agreement to have been void at a specified date.³¹⁰ In some cases, therefore, the agreement may not be avoided at the beginning.

(4) *Election of remedies*

In common contract law, if a claimant may rescind a contract and claim damages for breach of contract under the circumstances, the principle seems to be settled by the Australian court decisions that these two remedies are alternative. That is, the claimant needs to either set aside the contract or affirm the contract and claim monetary compensation for the loss suffered. In other words, the plaintiff cannot seek a combination of both remedies unless the plaintiff can establish a claim on the basis of tort of fraudulent misrepresentation.³¹¹ This election principle also applies in the case of the election of statutory rescission and damages.³¹² In *Argy v Blunts & Lane Cove Real Estate*, the Federal Court discussed the election of rescission and damages under the former Trade Practices Act. The court maintained that the doctrine of election applied where the rights to both damages and to rescind were made available to the applications. Thus, the applications needed to choose to pursue either of the two inconsistent rights.³¹³

307 M W Bryan, V J Vann, and S Barkehall Thomas, *Equity and Trusts in Australia* (2nd edn, Cambridge University Press 2017) 70-74. See also *Vadasz v Pioneer Concrete (SA) Pty Ltd*, [1995] 184 CLR 102, 105.

308 *A H McDonald and Company Pty Ltd v Wells* (1931) 45 CLR 506, 512-513 per Rich, Starke, and Dixon JJ; *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457, 476-77 per Dixon J.

309 *Highfield Property Investments* (n 300) [283].

310 The CCA, s. 87(2); The ACL, s. 243(a).

311 *Carter* (n 268) 374.

312 *Sibley v Grosvenor*, [1916] 21 CLR 469 per Griffith CJ; *Brown v Smitt*, [1924] 34 CLR 160 per Knox CJ, Gavan Duffy and Starke JJ.

313 *Argy* (n 288).

3.4.4.5 Conclusions

The private law regime, in the case of the franchisor's non-performance of the disclosure duty and the duty to provide complete, current and accurate information, is fundamentally a statutory regime. As the non-performance of these duties is customarily considered a violation of the provisions of the Franchising Code of Conduct, this contravention lays a basis for resorting to private law actions under the CCA. Under the CCA, an aggrieved franchisee may seek a court decree to enforce the franchisor's action, recover damages, and declare a franchise contract to be void. Suppose the non-performance of these duties amounts to misleading or deceptive conduct. In that case, the franchisee may resort to those three statutory remedies under the ACL, which arguably applies to franchise relationships. In addition to the competition and consumer statutes, a franchisee may seek some civil law remedies under common law. In theory, the franchisee can claim damages for the tort of misrepresentation or breach of contract. Alternatively, the franchisee may elect to rescind the franchise agreement based on the theory of innocent or fraudulent misrepresentation.

3.4.5 Comparative analysis

3.4.5.1 Introduction

The descriptive examinations show that the DCFR, the USA, and Australia have the legal frameworks offering private law remedies for an aggrieved franchisee in the event of the franchisor's non-performance of the disclosure duty and the duty to provide complete, current and accurate information. Under the selected legal systems, the franchisee may resort to remedial rules of the legal frameworks for enforcing the franchisor's performance, recovering monetary compensation, and cancelling a franchise agreement. However, the selected legal systems' remedial rules vary. Thus, this section will compare, contrast, and discuss the rules governing the three civil law remedies in subsection 3.4.5.2. Subsection 3.4.5.3 will offer concluding remarks on the remedial regime under the chosen legal systems and key recommendations for constructing a remedial system under comprehensive franchise law.

3.4.5.2 Comparison and analysis

– Enforcement of performance

(1) Similarity

The DCFR and Australia are similar in the sense that both legal systems have a legal basis that would permit an aggrieved franchisee to seek the enforcement

of the franchisor's pre-contractual duties of information. Under the DCFR, the disclosure obligation and the duty to provide complete, current and accurate information are obligatory under IV.E. – 2:101, in conjunction with IV.E. – 4:102(1). In this case, any non-performance of these obligations would allow the franchisee to enforce the franchisor's performance under III. – 3:302. According to the drafters of the DCFR, this provision is a catch-all rule governing the non-performance of both a contractual obligation and a pre-contractual obligation.

In Australia, it could be argued that a prospective franchisee may enforce the franchisor's performance of the pre-contractual duties under the Franchising Code of Conduct by way of injunctions under the CCA and the ACL. Under the statutes, a court may, upon an application, grant the injunctive relief ordering the franchisor to engage in certain conduct, such as disclosing some informational items required by the Code or updating its disclosure document. This assumption is drawn from theoretical inference. In other words, enforcing the franchisor's pre-contractual duties of information might be rare in reality as many potential franchisees would resort to other appropriate remedies or sanctions against the franchisor, such as damages or administrative penalties.

(2) *Difference*

It is uncertain that the enforcement of the franchisor's disclosure duty is doable under the US state franchise sale regulations. This uncertainty results from the fact that the state franchise sale laws do not explicitly provide a mechanism that could be used to enforce the performance of the pre-sale obligations. However, some state sale laws offer a catch-all remedy, which could be interpreted to allow the court to order the execution of the disclosure duty. Despite the existence of a catch-all remedy, there has been no court decision showing the acceptance of that interpretation.³¹⁴ In my view, the absence of the prospective franchisee's claim to enforce the franchisor's performance of pre-contractual duties under the statutes might result from two factors.

Firstly, bringing lawsuits to obtain pre-sale information required by the franchise legislation may be hindered due to financial reasons attributed to two peculiar practices in the USA. The first reason is that, under the American Rule, a private litigant is typically responsible for its own litigation costs and legal fees.³¹⁵ These expenses can be very costly. For instance, the hourly fees rate of a senior partner in the law firm may exceed 500 US dollars.³¹⁶ The high fees rate could dissuade a franchisee from bringing its claim to courts. Second, US attorneys might be unwilling to take the job because of the slight possibility of arranging contingent fees. This contingency-fee arrangement

³¹⁴ See subsection 3.4.3.2.

³¹⁵ Arthur T von Mehren and Peter L Murray, *Law in the United States* (2nd edn, Cambridge University Press 2007) 268.

³¹⁶ Peter Hay, *The Law of the United States: An Introduction* (Routledge 2017) 65.

allows a lawyer to share some portion of compensation awarded by the court. Thus, this arrangement relies heavily upon a claim for considerable amount of damages, particularly in personal injury actions.³¹⁷

Secondly, bringing lawsuits to obtain pre-sale information required by the franchise legislation may be constrained by time and agreement. First, it would be too late to bring a lawsuit to acquire the pre-contractual information. In many instances, a franchisee may uncover the franchisor's non-disclosure or misleading conduct after a franchise contract has been concluded. For example, in *Coraud v Kidville*, the court decision demonstrated that the franchisee discovered that the estimation of the expenses was misleading after the conclusion of a franchise agreement.³¹⁸ This example shows that it would not be possible to enforce the performance of the pre-contractual information duties before the sale of a franchise is made. Second, many franchisees may be barred by the terms of a franchise contract from suing a franchisor. In some cases, a franchise contract may prohibit a franchisee from engaging in a class action litigation, which usually is affordable to the franchisees, against a franchisor.

(3) Discussion

From the comparison, the right to enforcement of the franchisor's pre-contractual duties of information seems to be a mystery in the realm of the franchise sale law. Strictly speaking, no franchise legal framework of the DCFR, the USA, and Australia explicitly provides for a mechanism to compel the franchisor's performance of the obligations. Instead, several rules have to be employed to confer the right to enforce the performance to a prospective franchisee to acquire some informational items before concluding a franchise agreement. For example, under the DCFR, the rule on enforcing specific performance of a non-monetary obligation has to be argued to apply in this context.

In my view, comprehensive franchise law should resolve such a mystery by establishing private law relief, enabling a prospective franchisee to enforce the franchisor's performance of the disclosure duty and the duty to provide complete, current and accurate information. For example, under the law, the franchisee should have the right to compel the franchisor to provide the required information or to disclose current and accurate information. This idea would not be strange as one commentator says that an obligation must be enforceable to be truly effective, whether it is a contractual obligation or not.³¹⁹ Thus, pre-contractual duties of information should equally be enforced

317 Stephen Gillers, 'The American Legal Profession' in Alan B Morrison, *Fundamentals of American Law* (Oxford University Press 1996) 169.

318 *Coraud* (n 207) 393.

319 Oliver Remien, 'Enforced Performance in European Contract Law: The Story of the Poor Banabans and the Hope for Happier Europeans' in Katharina Boele-Woelki and William Grosheide (eds), *The Future of European Contract Law* (Kluwer Law International 2007) 321.

in the same manner as the enforcement of contractual obligations. However, there may be a question of why the remedy should have a place in comprehensive franchise law.

In my opinion, this specific relief would help effectuate the franchisor's disclosure of pre-sale information, which is the central goal of all franchise sale laws. As can be seen, this chapter proposes that comprehensive franchise law should regulate the pre-contractual stage of making a franchise contract. One of the proposed regulations is that the law should establish disclosure duties obligating a franchisor to provide pre-sale information, which is transparent, accurate, and current. This regulation aims to enable a prospective franchisee to acquire qualified information from the franchisor prior to the conclusion of a franchise agreement.³²⁰ Thus, comprehensive franchise law should provide a mechanism that would help achieve that goal; that is to say, a remedy of enforcement of performance in kind.

It would seem that the remedy of enforcement of performance in kind is not an unusual remedy in the field of private law. Many legal systems seem to have profoundly established the enforcement of performance as a civil law remedy, particularly under the law of obligations or the law of contract.³²¹ For example, this relief has been made available in jurisdictions, such as France, Germany, and The Netherlands.³²² In those countries, an aggrieved party may bring a claim for performance of an obligation under article 1143 of the French Civil Code, section 241 of the German Civil Code, and section 3:296(1) of the Dutch Civil Code. Furthermore, in common law countries, such as the USA, specific performance has been developed to be one of the common law remedies for breach of contract claims.³²³ Therefore, legal systems would not face many hurdles when incorporating this enforcement remedy into comprehensive franchise law, which governs private aspects of a franchise relationship.

Based on the abovementioned idea, I suggest that comprehensive franchise law contains the rule governing the remedy of enforcement as a standalone

320 See sections 3.2 and 3.3.

321 Hein Kötz, *European Contract Law* (Gill Mertens and Tony Weir trs., 2nd edn, Oxford University Press 2017) 198, 202.

322 Janwillem Oosterhuis, *Specific Performance in German, French and Dutch Law in the Nineteenth Century: Remedies in an Age of Fundamental Rights and Industrialisation* (Martinus Nijhoff Publishers 2011) 221.

323 See eg *Berryhill v Hatt*, 428 NW 2d 647 (Iowa, 1988) 657; *Clemente v Pearle Vision Inc* 762 F Supp 1518 (D Me, 1991) 1519; *Reed v Triton Servs, Inc*, 15 NE 3d 936, 938, 2014 -Ohio- 3185, (Ohio App 12 Dist, 2014) 938-39; *Minnesota Vikings Football Stadium, LLC v Wells Fargo Bank, National Association*, 193 F Supp 3d 1002, (D Minn, 2016) 1014; *H B Fuller Co v Hamm*, 2018 WL 4047122 (D Minn, 2018) 4; *Homeland Energy Solutions, LLC v Retterath*, 938 NW 2d 664 (Iowa, 2020) 693. It should be noted that a grant of specific performance in the USA will be subject to several tests as it is regarded as an equitable remedy. Thus, the availability of this remedy in common law countries will be limited compared to that in civil law systems.

remedial mechanism under the law. The incorporation of this remedial rule would enable a prospective franchisee to compel the delivery of pre-sale information on the required items without having recourse to other remedial regimes, such as contract law regimes. Resorting to the remedy of specific performance under contract law would be improper when enforcing pre-sale disclosure obligations because these information duties are typically created by specific legislation, not by contracts. Thus, the enforcement of specific performance, which is regarded as a remedy for breach of contract or non-performance of a contractual obligation, would not apply.³²⁴

In incorporating the remedy of enforcement of performance in kind, I suggest that the factual requirements for non-performance of the disclosure obligations are transparent and coherent. In this regard, the disclosure rules establishing the information duties must be precise enough to help a prospective franchisee ascertain the point at which a non-compliance of the obligations accrues. For example, I have proposed in this chapter that the rules should explicitly require that a franchisor must disclose pre-contractual information to a prospective franchisee by providing the franchisee with a disclosure document including some informational items.³²⁵ This duty will be considered an obligation of result. Thus, the prospective franchisee would be allowed to initiate a claim for performance if the franchisor did not provide the disclosure document or omitted to disclose some informational items in the document.

Additionally, I have suggested that the timing for disclosure is fixed. In this case, it would economically be viable for a prospective franchisee to identify the franchisor's failure to perform the disclosure duties for the sake of litigation. As can be seen, I have proposed a one-month waiting period.³²⁶ For example, if a franchisor sets to sign a franchise contract on 30 April 2023, the franchisor must provide a disclosure document no later than 31 March 2023. Suppose the signing date has passed, and the franchisee has received nothing from the franchisor. In that case, the prospective franchisee may, at its option, choose to compel the delivery of the disclosure document. In the meantime, the parties may extend the signing of the franchise contract to another day. Enforcing the franchisor's performance in this hypothetical situation would be possible when a franchise contract to be concluded is a lucrative agreement where a prospective franchisee is unwilling to leave the negotiation just because of the franchisor's non-disclosure.

324 Kötz (n 321) 197; Hugh Beale and others, *Cases, Materials and Text on Contract Law* (3rd edn, Hart Publishing 2019) 840.

325 See subsection 3.2.5.2.

326 See subsection 3.2.5.2.

– *Monetary compensation*

(1) *Similarity*

The DCFR, the USA, and Australia are similar in four aspects as follows.

First, the chosen legal systems make available for a franchisee a remedy of damages in the event of the franchisor's non-compliance with pre-contractual information duties. To put it differently, if the franchisor breached the disclosure rules under franchise sale law, the franchisor might be held liable for damages for the loss caused to the franchisee. Under the DCFR, the franchisee may resort to specific contract law rules in Part E of Book IV for the right to claim damages. In America, the franchisor's contravention of the disclosure and anti-fraud rules typically lays a basis for an action for statutory damages under the state sale statutes. Likewise, in Australia, the franchisor's violation of the Franchising Code of Conduct would permit an aggrieved franchisee to claim statutory damages under the CCA and the ACL.

Second, the selected legal systems commonly accept that a remedy of damages serves a compensatory purpose. That is, this monetary compensation aims to redress loss or damage sustained by a franchisee as a result of the franchisor's breaching conduct. Under the DCFR, damages are compensatory since they will be awarded to place an aggrieved party as nearly as possible in the position in which the franchisee would have been if the franchisor had performed the duty of disclosure or the duty to provide complete, current and accurate information satisfactorily. In the USA, the court contended that damages must be awarded to compensate the franchisor for the loss suffered; hence, the franchisee will not be permitted to seek punitive damages from the franchisor. Similarly, Australian laws provide that damages will be awarded to compensate for actual loss or damage sustained by the franchisee. Thus, the three legal systems generally do not allow an injured franchisee to claim punitive or exemplary damages from a franchisor.

Third, the selected legal systems would generally agree that an injured franchisee may recover damages for reliance or out-of-pocket loss caused by the franchisor's non-performance of pre-contractual information duties. Under the DCFR, the compensable loss includes economic loss, which is meant to cover burdens incurred. It could be said that this specific category of economic loss is identical to reliance loss. In the USA, some state courts, such as the Minnesota Supreme Court in *Hughes v Sinclair Marketing*, implicitly held that the recoverable loss under the disclosure statute typically included the reliance damage.³²⁷ In Australia, it is accepted that the court may find a proper measure of damages under the CCA and the ACL. The flexibility in assessing damages would allow the court to award damages to redress the franchisee's reliance loss.

327 *Hughes* (n 227) 199.

Fourth, it is unlikely that the loss of chance is recoverable in the chosen legal systems. Under the DCFR, the recovery of damages for the lost chance is not extensively discussed. Moreover, the drafters of the DCFR seem to wait for courts to materialize this issue. Thus, whether a franchisee can be compensated for the loss of opportunity must follow one of the underlying principles for recovering damages; the loss must be caused by the failure to perform. If there is no causation between the failure in performance and the loss suffered, the injured party would not be able to claim damages.³²⁸ Likewise, in the USA and Australia, the loss of chance is a matter of causation. In theory, a franchisee will recover damages insofar as it proves that the franchisor's breaching conduct causes the franchisee's injury or damage. However, recovering damages for the lost chance in the franchising context remains questionable because the US and Australian courts seem to allow the recovery of damages for the lost chance in medical and professional malpractice tort cases.³²⁹

(2) *Difference*

The DCFR differs from the US and Australian legal systems in the following two cases.

First, the DCFR does not allow an injured franchisee to resort to the law on non-contractual liability as an alternative basis for recovering damages. Under the DCFR, the right to claim damages is constituted under contract law rules. In this case, the right to seek damages in tort will be excluded by virtue of VI – 1:103. Paragraph (c) of this provision provides that the non-contractual liability rule in VI – 1:101 does not apply if its application would contradict the purpose of the other private law rules. According to the commentaries to VI – 1:103, this paragraph (c) implies the priority of contract law liability over tort law liability in case of a conflict in value between those remedial regimes.³³⁰ In my opinion, IV.E. – 4:102(2) aims to establish a special basis for recovering damages in the case of non-performance of a pre-contractual information duty.³³¹ In this case, the value of contractual liability would contradict that of non-contractual liability, thereby excluding the recourse to non-contractual liability rules for recovering damages.³³²

In contrast, the USA and Australia would, at least in theory, permit an injured franchisee to seek common law damages if the franchisor does not perform the disclosure duty or the duty to provide complete, current and accurate information. In America and Australia, the possible common law

328 See subsection 3.4.2.3.

329 See subsections 3.4.3.3 and 3.4.4.3.

330 Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.4, Oxford University Press 2010) 3119.

331 See subsection 3.4.2.3.

332 It should be noted that the drafters of the DCFR do not have a clear explanation for this issue. Thus, this paragraph reflects my own view on the issue.

cause of action for damages is identical; the franchisee may claim tort law damages by alleging the franchisor of fraudulently misrepresenting facts.³³³ In claiming damages based on the tort of deceit, the claimant franchisee usually needs to prove that the defendant franchisor misrepresented material facts to induce the franchisee's reliance. Moreover, the franchisee must show that it reasonably relied upon that misrepresentation when concluding a franchise contract. Additionally, the heart of a fraudulent misrepresentation claim is the representor's state of mind. The US and Australian legal systems would require the franchisee to demonstrate the franchisor's dishonesty in misrepresenting the facts.

Second, the DCFR does not permit a court to award punitive damages. This conclusion is apparent when considering a general measure of damages under II. – 7:214(2) indicating that an award of damages aims to compensate for the loss sustained, not to punish an injuring party. Conversely, this type of damages would be allowable in the USA and Australia. As mentioned in the preceding paragraph, the two legal systems would permit a claim for damages based on the tort of fraudulent misrepresentation. In the realm of common tort law, a court may award punitive or exemplary damages in some exceptional cases where the defendant committed wrongful conduct maliciously.³³⁴ In the USA, some franchise sale states also permit an award of statutory punitive damages. In Hawaii, South Dakota, and Washington, punitive damages can be awarded in the form of treble damages in the case of a willful violation of the franchise sale statutes.³³⁵

(3) *Discussion*

From the comparison, the recovery of damages is a private law remedy common among the chosen legal systems. This remedy is vital to redress any detriment sustained by a franchisee because of the franchisor's conduct. Thus, I propose that comprehensive franchise law adopts this common approach and makes available the remedy of damages that allows an aggrieved franchisee to recover money for the loss or damages sustained as a result of the franchisor's contravention of the franchise sale rules. As underlying principles for recovering damages, I suggest that comprehensive franchise law embraces a compensatory characteristic of damages, which is also widely accepted by the selected legal systems. Thus, the function of damages under comprehensive franchise law should focus on compensating for the loss or damage suffered by the franchisees.

From a theoretical perspective, the compensatory character of damages serves the idea of corrective justice, which focuses on what is morally required

³³³ See subsections 3.4.3.3 and 3.4.4.3.

³³⁴ See subsections 3.4.3.3 and 3.4.4.3.

³³⁵ Hawaii: HI ST, § 482E-9(c); South Dakota: SD ST § 37-5B-49; Washington: WA ST 19.100.190(3).

concerning wrongful conduct and harm caused thereby.³³⁶ Inspired by the Aristotelian concept of justice, some scholars, such as Coleman, claim that compensation is a form of justice that eliminates unjustifiable gains and losses.³³⁷ Suppose a franchisee suffers any loss or damage due to the franchisor's wrongful conduct. In that case, the franchisor should compensate the franchisee in order to remedy the loss or damage suffered. Therefore, compensating for loss or damage should be a primary goal of the remedial system under comprehensive franchise law.

One may raise a further question of whether an award of punitive or exemplary damages should be introduced under the remedial regime of comprehensive franchise law. Can deterrence be the secondary character of the remedy of damages under the law? In my view, this question may not be answered from a theoretical standpoint as it is frequently a matter of legal policy. As a policy, some legal systems may introduce this deterrent-based monetary compensation. In this case, courts may be able to award damages up to hundreds of millions of dollars or euros under the circumstances of the case.³³⁸ Awarding a huge amount of damages would discourage any person from deciding to engage in any opportunistic conduct. In particular, franchisors would be forced to think carefully before behaving opportunistically towards franchisees, as punitive damages would make the franchisors insolvent. Thus, the deterrent function of punitive damages would be argued to support the goal of preventing a franchisor from behaving opportunistically.

One might argue that an award of compensatory damages could play a preventive role, as do punitive damages. In practice, courts in some jurisdictions seemingly adopt this idea. For example, in *Royal Bank of Canada v W Got Associates Electric Ltd*, the Supreme Court of Canada held that the award of compensatory damages could be used as a deterrence.³³⁹ Franchise-specific regulations typically impose administrative penalties or criminal offenses for a violation of provisions of the laws. These sanctions could be argued to be much more effective than the imposition of punitive damages. In these cases, the availability of punitive damages might not be very demanding insofar as other remedial mechanisms can play a prohibitive or preventive role. Regarding this punishment issue, I am inclined to believe that punishing opportunistic

336 According to Weinrib, the concept of corrective justice, introduced by Aristotle, underpins private law relationships. See Ernest J Weinrib, 'Corrective Justice' (1992) 77 Iowa Law Review 403, 425. Thus, this moral concept of corrective justice could provide a foundation for establishing the compensatory system of damages.

337 Richard A Posner, 'The Concept of Corrective Justice in Recent Theories of Tort Law' (1981) 10 The Journal of Legal Studies 187, 197.

338 Tina Bellon, 'Missouri judge affirm \$4.69 billion talc verdict, J&J vows to appeal' (REUTERS, 22 August 2018) <<https://reut.rs/3yHiDgU>> accessed 21 January 2022; Holly Yan, 'Jurors give \$289 million to a man they say got cancer from Monsanto's Roundup weedkiller' (CNN, 12 August 2018) <<https://cnn.it/3AIVu4e>> accessed 21 January 2022.

339 *Royal Bank of Canada v W Got Associates Electric Ltd*, [1999] 3 SCR 408 [28].

franchisors should rely on public law sanctions such as imposing penalties for violating conduct. In my view, these sanctions are typically supervised by public authorities who could employ them more readily and effectively. Thus, I suggest that, from a private law perspective, comprehensive franchise law does not permit the recovery of punitive damages.

– *Cancellation of a contract*

(1) *Similarity*

The DCFR, the USA, and Australia similarly offer some contract law mechanisms that permit an aggrieved franchisee to revoke a franchise relationship in the case of the franchisor's non-performance of the disclosure duty or the duty to provide complete, current and accurate information. Under the DCFR, a franchisee may resort to contract law provisions concerning vitiated consent or intention. Under the rules, the franchisee may avoid a franchise contract for mistake or fraud, upon the satisfaction of the pre-requisites for the avoidance. Likewise, in the USA and Australia, the franchisee may avoid or rescind a franchise agreement based on the theory of misrepresentation. As can be seen, a ground for avoiding or rescinding a franchise contract is, though not identical, much the same. The franchisee is allowed to avoid the franchise agreement if it concluded the agreement based on a misapprehension caused by the franchisor.

In addition, the DCFR, the USA, and Australia are similar in terms of partial avoidance or rescission and the effects of the avoidance or rescission. Under the selected legal systems, a franchise contract can be avoided or rescinded partially. In some exceptional cases, the franchisee may avoid or rescind particular terms of a franchise contract if the terms of the agreement are severable, and the affected terms can be separated from the rest. Besides, the avoidance or rescission will annul a franchise contract at its inception or *ab initio*. In other words, a franchise contract will be annulled as if it never existed. Furthermore, the avoidance or rescission of a franchise agreement will take a retrospective effect. The valid avoidance or rescission will follow the restoration of the parties to their initial status. In principle, both parties will be obliged to return the properties and benefits received under the agreement to the other party.

(2) *Difference*

The USA and Australia differ from the DCFR in two aspects as follows.

First, the US and Australian legal systems make an action for rescission for a violation of disclosure rules available for an aggrieved franchisee. In the USA, most state franchise sale laws provide that a franchisee may bring an action to rescind a franchise contract because of the franchisor's violation of disclosure provisions under the statutes. In Australia, the franchisor's contravention of disclosure rules under the Franchising Code of Conduct lays the

ground for an action for private remedies under the CCA. Among other things, an aggrieved franchisee may ask the court to declare a franchise contract void. The franchisee may apply for a declaration of avoidance of a franchise agreement under the ACL by satisfying a court that the franchisor engaged in misleading or deceptive conduct in violation of the ACL. In contrast, the DCFR does not provide a specific right to avoid a franchise contract based on a violation of the franchise-specific rules. In this case, the franchisee needs to resort to general rules of contract law that would entitle the franchisee to invalidate the agreement.

Australia differs from the USA in terms of the requirement of actual or anticipated loss under statutory laws. In Australia, the competition and consumer statute require that an applicant franchisee must suffer, or is likely to suffer, the loss or damage when applying for a declaratory order. In contrast, the US franchise sale laws do not require this element. The imposition of this requirement implies that Australia regards a declaration of avoidance as a remedial order to redress the actual and anticipated damage. Thus, it would be more challenging to rescind a franchise contract in Australia than in the USA, as the US state sale laws do not embrace this equivalent concept. In any case, rescinding a franchise contract under the US franchise sale statutes may not be effortless because some franchise sale statutes require the franchisor's violation of the laws to be material. In other words, the franchisor's marginal violation of the laws would not provide a basis for the franchisee to bring an action for rescission.

Second, an aggrieved franchisee needs a court order when rescinding a franchise contract under the US and Australian statutory laws. In other words, the franchisee cannot effectively rescind a franchise contract by notice of rescission. Instead, the franchisee must sue the franchisor in court for an award of rescission of a franchise agreement. In contrast, the franchisee may avoid a franchise contract for mistake and fraud under the DCFR merely by giving the franchisor the notice of avoidance. The main reason underlying this difference could be that the rescission in the USA and Australia is regarded as an equitable remedy. In principle, the court will play a significant role in determining whether it is fair under the circumstances of the case to order a contract to be rescinded. On the other hand, the avoidance of a contract under the DCFR is a matter of right. The franchisee would enjoy this right without having recourse to judicial intervention.

(3) Discussion

From the comparison, the chosen legal systems commonly allow an aggrieved franchisee to escape a franchise relationship if a franchisor failed to comply with the duty of disclosure and the duty to provide complete, current and accurate information. In doing so, the franchisee may resort to the general contract law rules or sector-specific law rules, such as the rules of the franchise sale law. Rescinding or avoiding a franchise contract under general contract

laws and statutory laws may be based on different concepts. In contract law, a franchisee usually has to prove its vitiated consent. That is, the franchisor must demonstrate that it concluded a franchise contract because of a mistake induced by the franchisor. Conversely, a common ground for rescinding a franchise agreement under the statutes is the franchisor's violation of the disclosure rules. In sum, rescission in contract law focuses on an internal element of defective consent, while statutory rescission pays attention to an external element of the violation of the laws.

In this case, I propose that comprehensive franchise law provides mechanisms that allow a franchisee to cancel a franchise contract if the franchisor violates the rules regulating the disclosure duty and the duty to provide complete, current and accurate information. The establishment of the statutory mechanism would be useful for an aggrieved franchisee as it will ease the burden of proof of some subjective requirements that usually is required in contract law systems. For example, under the DCFR, suppose a franchisee seeks to avoid a franchise contract for a mistake. In this case, the franchisee must prove that the franchisor caused the franchisee to make a material mistake, and the franchisor knew or could reasonably be expected to have known that fact. Likewise, suppose the franchisee will rescind a franchise contract for fraudulent misrepresentation in the USA and Australia. The franchisee must prove that the franchisor knowingly or recklessly misrepresented facts intending to induce the franchisee's reliance. In some cases, demonstrating the franchisor's internal mind would be cumbersome for a plaintiff franchisee. In contrast, in Australia, the franchisee does not have to prove the franchisor's intention if the franchisee brings a statutory action to avoid a franchise agreement under the CCA.

Conversely, comprehensive franchisee law could surmount the difficulty by not requiring proof of that subjective element. In other words, comprehensive franchisee law may require the demonstration of the objective components. For instance, in the case of non-compliance with the duty of disclosure, the franchisee may be required to show that the franchisor failed to comply with one or all of the disclosure requirements before entering into a franchise agreement. In this case, the franchisee will only have to prove the fact that the franchisor did not comply with the disclosure requirements; the franchisee may have to demonstrate that the franchisor omitted disclosing information on certain required disclosures in a disclosure document. Alternatively, the franchisee may provide evidence indicating that some information in the disclosure document is inaccurate or out-of-date.³⁴⁰ As can be seen, no proof of the franchisor's intent to defraud is demanded.

340 Utilizing this approach would be more effective if it is reinforced by other approaches, such as enabling a franchisee to verify the provided information from public records or other fellow franchisees in the franchise system by public law. However, discussing these approaches is beyond the scope of this thesis and would be useful for future research.

There may be cases where a franchisee alleges a franchisor of failing to comply with insignificant requirements. In these cases, I suggest that comprehensive franchise law requires the element of materiality as some US state franchise sale laws do. In this case, the franchisee may have to show that the franchisee's violation of the disclosure requirements materially affected the franchisee's decision to conclude a franchise contract. To put it another way, the franchisee may have to prove that it would not have concluded the agreement had the franchisor correctly performed the disclosure duty or the duty to provide complete, current and accurate information. For example, the franchisee may rescind a franchise contract if the franchisee can demonstrate that it would not have entered into a franchise contract with the franchisor if the franchisor had disclosed accurate and current information about the franchisor's financial performance in the course of the COVID-19 pandemic.³⁴¹

3.4.5.3 Conclusions

– Concluding remarks

The DCFR, the USA, and Australia provide an aggrieved franchisee with a set of three private law remedies – enforcement of performance, damages, and rescission or avoidance – in the event of the franchisor's non-performance of the pre-contractual duties of information. The DCFR, the USA, and Australia are similar in that they provide the remedies of damages and rescission or avoidance. These civil remedies are *ex-post* sanctions in the sense that they can be resorted to after a franchise contract was concluded. In terms of the enforcement remedy, only the DCFR and Australia provide legal mechanisms that would allow the franchisee to compel the franchisor's performance before the conclusion of a franchise contract.

– Key recommendations

(1) Remedial regime

For the purpose of protecting the franchisee's rights to the franchisor's performance of pre-contractual obligations, comprehensive franchise law should introduce a remedial system that enables an aggrieved franchisee to seek three private law remedies as follows: enforcement of the franchisor's performance

³⁴¹ During the pandemic of the COVID-19 in some countries, many franchisee businesses may have adversely been affected by the outbreak of the disease. In this case, a disclosure document may not contain accurate data on the franchisor's financial status at the time of disclosure. Thus, in some countries such as the USA, an accurate account of the franchisor's financial performance representations is considered important in the time of the pandemic. See The NASAA Franchise Project Group, 'Disclosing Financial Performance Representations in the Time of COVID-19' <<https://bit.ly/3xAbeQf>> accessed 21 January 2022.

of pre-contractual information duties, recovery of damages, and cancellation of a franchise contract.

(2) *Enforcement of performance in kind*

The first private law remedy should facilitate the actual acquisition and utilization of the pre-contractual information. This remedial function would enable a prospective franchisee to make a reasonably informed decision whether or not to buy a franchise. The franchisee's ability to resort to the enforcement of performance would help avoid any dispute arising after a franchise contract is concluded.

(3) *Recovery of damages*

The second remedial mechanism aims to redress the franchisee's loss or damage caused by the franchisor's non-performance of the pre-contractual information obligations in money form. Under the remedial regime, comprehensive franchise law should allow the recovery of damages that serve a compensatory purpose. That is, an award of damages should primarily aim to redress the franchisee's actual loss or damage.

(4) *Cancellation of a contract*

The third private law remedy intends to provide a franchisee with a chance to escape an undesirable franchise relationship because of the franchisor's non-compliance with the information duties. Comprehensive franchise law should constitute a legal mechanism that allows the franchisee to cancel a franchise contract. Comprehensive franchise law should insert the element of materiality by requiring that the franchisor's non-performance of the obligations be material to the franchisee. That is, the franchisee would not have concluded a franchise contract if the franchisor had performed the duties duly.

3.5 CONCLUSIONS

Chapter three has examined the franchise legal framework of the DCFR, the USA, and Australia regulating a pre-contractual franchise relationship and found that the disclosure rules of the franchise legal frameworks similarly establish the franchisor's pre-contractual disclosure duty requiring a franchisor to provide a prospective franchisee with material information about a franchise business before the conclusion of a franchise contract. Nevertheless, the selected legal systems' disclosure rules vary in detail. The third chapter has explored that the franchise legal framework of the DCFR, the USA, and Australia does not constitute the franchisor's duty to provide complete, current and accurate information as an independent obligation. Despite the absence of this obligation, the legal frameworks contain several rules requiring the franchisor to ensure that a prospective franchisee acquires qualified information that would

enable the franchisee to make an informed decision before concluding a franchise contract.

In the context of private law remedies, chapter three has discovered that an aggrieved franchisee may seek the three private law remedies in the case of the franchisor's failure to comply with the franchise disclosure rules. First, the franchise legal framework of the DCFR, the USA, and Australia similarly permits an aggrieved franchisee to recover damages and discharge a franchise relationship. However, the source of remedial rules may differ from legal system to legal system. In addition, the franchise legal framework of the DCFR and Australia seems to enable the franchisee to enforce the franchisor's performance of pre-contractual duties. Despite this similarity, the DCFR differs from Australia in that the enforcement of specific performance is a contract law remedy. In contrast, the enforcement remedy is a statutory, discretionary remedy under the Australian competition and consumer legislation.

4 | Regulation of the franchisor's ongoing obligations

4.1 INTRODUCTION

Once a franchise relationship is established, a franchisee expects a franchisor to be trustworthy and supportive. During an ongoing relationship, the franchisee would expect no intra-brand competition triggered by the franchisor in the franchisee's marketing area. The franchisee would also hope that the franchisor lends the franchisee support to operating a franchised business. However, not every franchisor maintains a relationship of trust and cooperation with franchisees. Some franchisors behave opportunistically toward franchisees that cause troubled franchise relationships, putting franchisees at a disadvantage. A franchisor may market its products or license other franchisees to do so through traditional or non-traditional channels of distribution in franchisees' marketing areas. A franchisor may not render franchisees with appropriate and necessary assistance in opening and operating a franchised business.

The relational problems mentioned above lead to the following three questions: how is the franchisor required not to encroach upon the franchisee's business? how is the franchisor required to assist the franchisee in the opening and operation of a franchised business? what are private law remedies for the franchisor's failure to perform these duties? Chapter four will examine the franchise legal framework of the Draft Common Frame of Reference (DCFR), the United States of America (USA), and Australia to answer these three questions. The examination of the franchise legal framework of the DCFR, the USA, and Australia regulating the franchisor's duty not to encroach and the duty to assist will be conducted in sections 4.2 and 4.3, respectively.¹ In addition, section 4.4 will explore if the franchise legal framework of the DCFR, the USA, and Australia provides an aggrieved franchisee with remedial rules to which the franchisee may resort to enforce the franchisor's performance, claim monet-

¹ For the sake of clarity, this chapter will synonymously use the terms 'obligation' and 'duty'. These two terms will be used interchangeably, meaning action or inaction that a person is legally bound to perform towards the other person.

ary compensation, and cancel a franchise contract.² Section 4.5 will summarize the findings of chapter four.

4.2 DUTY NOT TO ENCROACH

4.2.1 Introduction

Section 4.2 will conduct descriptive and comparative examinations on the regulation of the franchisor's encroachment. This section will examine if and how the franchise legal framework of the DCFR, the USA, and Australia requires a franchisor to refrain from engaging in both traditional and non-traditional encroachment in sections 4.2.2, 4.2.3, and 4.2.4, respectively. In other words, these three sections will examine how the rules of law and the terms of a franchise contract in each legal system prevent the franchisor from placing a company-own store, licensing another franchisee to open a franchised outlet, and distributing its goods or services through other alternative distribution channels, such as online sales, in the vicinity of the franchisee's distribution area. Then, section 4.2.5 will compare, contrast, and discuss the regulatory approaches taken by the selected legal systems to offer guidelines for formulating anti-encroachment rules under comprehensive franchise law.

4.2.2 The Draft Common Frame of Reference (DCFR) *cum annexis*

4.2.2.1 Introduction

The DCFR does not contain franchise-specific rules regulating encroachment by a franchisor. In this case, general contract law provisions will play a central role in governing the franchisor's obligation not to encroach. Under the DCFR's contract law regime, the franchisor's duty may be established by the express and implied terms of a franchise agreement. This section will examine the extent to which the franchisor's obligation not to compete with the franchisee is constructed by an express agreement in subsection 4.2.2.2. Subsection 4.2.2.3 will explore the requirements of the implication of a contractual term generating the franchisor's duty not to encroach. Subsection 4.2.2.4 will conclude on the central feature of the regulatory system under the DCFR.

2 For the sake of clarity, this chapter intends the phrase 'cancelling a franchise contract' to mean putting an end to a franchise relationship utilizing certain legal mechanisms. After a franchise contract is legally canceled, a franchise relationship will be dissolved or annulled.

4.2.2.2 Regulation by the express terms of a franchise contract

– Incorporation of an exclusivity clause

The express terms of a franchise contract may constitute a franchisor's obligation not to compete. It should be noted at the outset that the DCFR recognizes the principle of freedom of contract.³ Paragraph (1) of II. – 9: 101 expressly recognizes that the contractual terms can be made by express agreement. Thus, a franchise contract may contain the term creating the duty of the franchisor concerning territorial exclusivity. In practice, inserting a contractual clause on territorial exclusivity into a franchise contract is not uncommon.⁴ In Europe, it is claimed that a franchise agreement usually contains the designation of an exclusive territory that the franchisor agrees not to encroach upon the franchisee's business.⁵ The DCFR also contemplates this exclusivity agreement. According to IV.E. – 4:102, a franchisor is obliged to disclose information concerning the terms of the franchise contract, which may include the term regarding an exclusive territory.⁶

Exclusivity clauses may be drafted from a different standpoint. Some clauses may protect the franchisor's interests. Others may safeguard those of the franchisee. In the latter case, the International Chamber of Commerce (ICC) offers the Model International Franchising Contract (Model Contract), illustrating how an exclusivity provision in a franchise agreement plays a vital role in protecting the franchisee's legitimate interests against the franchisor's encroachment. Under article 7 of the Model Contract, the franchisor is barred from engaging in both geographic-based and non-geographic-based encroach-

3 Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.1, Oxford University Press 2010) 38.

4 Some self-regulatory organizations' code of conduct recommends the establishment of an exclusive area of a franchisee's business. For example, Associazione Italiana del Franchising (AIF), an Italian non-profit association whose members are mainly Italian franchisors, has introduced the code of conduct called 'Codice Deontologico Soci'. In the code, article 9 provides that a franchise contract must incorporate the term indicating the scope of territorial exclusivity both in relation to other franchisees and in relation to channels and sales units directly managed by the franchisor. The Italian text of Codice Deontologico Soci can be accessed at <<https://bit.ly/3r8ov01>>.

5 Vivien Rose and David Bailey (eds), *Bellamy & Child European Union Law of Competition* (8th edn, Oxford University Press 2018) 496.

6 Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.3, Oxford University Press 2010) 2387, 2390. It should be noted that the franchisor has to disclose such information if the contract contains the exclusivity agreement. In other words, the rule does not require the franchisor to incorporate that term into the contract. Under the principle of freedom of contract, it is up to the parties to determine whether a franchise contract grants the franchisee an exclusive territory or whether a franchisor is prohibited from engaging in conduct that encroaches that exclusive area.

ing conduct. First, the franchisor is prevented from operating, or licensing other franchisees to operate, a franchise business within the granted territory of the incumbent franchisee.⁷ Second, the franchisor shall omit to sell any products associated with the brand to customers within the area.⁸ Furthermore, the franchisor may not actively solicit or provoke the sales of products to the customers in order to circumvent the franchisee's right to exclusivity.

– *Implications of European competition laws for an exclusivity clause*

The drafters of the DCFR acknowledge that, in some circumstances, competition law may affect a franchise agreement. Since an exclusivity provision restricts competition within a franchise network, it would be wise to examine whether and to what extent competition law rules may affect the incorporation of that provision in a franchise contract. Nevertheless, the DCFR does not contain any model rules on competition. In Europe, competition laws can be national competition laws and European laws. For the sake of illustration, European competition law will be examined to see how a competition law regime affects the validity of an exclusivity clause. The reason for the choice of a European legal regime is that, apart from the fact that most national competition laws in Europe follow the model of European competition laws, many agreements or arrangements can be found to affect interstate trade in the European Union. Thus, the European competition law seems to play a dominant role in addressing competition law issues in Europe. Based on this view, the EU competition law would be a better choice for examining the effects of competition rules on a franchise agreement under the DCFR.

For the sake of specificity, the following two EU competition law instruments will be briefly examined. First, the Treaty on the Functioning of the European Union (TFEU) will be examined in consultation with the decision of the Court of Justice of European Union (CJEU) in the case *Pronuptia*. The decision of the court in *Pronuptia* is worth the attention as it has set a leading precedent that provides useful guidelines in the case of compatibility with the EU rules on competition of franchising arrangements. Second, the Block Exemption Regulation (BER) will also be reviewed in consultation with the Commission's Guidelines on Vertical Restraints since a franchise contract is typically regarded as a vertical agreement in light of the BER. In light of the selected European competition laws, an exclusive arrangement under a franchise contract that prevents a franchisor from competing with a franchisee within a specified territorial area would be effective in three situations as follows.

Firstly, an exclusive agreement is not considered restrictive of competition under Art. 101(1) of the TFEU. In principle, Art. 101(1) of the TFEU would prohibit a franchise agreement, which may affect interstate trade and that has

7 The Model Contract, art. 7.1.

8 The Model Contract, art. 7.2.

the object of, or effect on, prevention, restriction, or distortion of competition within the European Union.⁹ According to case law in *Pronuptia*, the European Court elaborated on the circumstances under which franchise arrangements fell outside the scope of Art. 85(1) of the EEC Treaty, the predecessor of Art. 101(1) of the TFEU.¹⁰ Nevertheless, the court decided that any clause in a franchise contract that aimed to share markets between the franchisor and the franchisee or between franchisees would restrict competition within the franchise network.

However, the court in *Pronuptia* did not conclude that the market partitioning *per se* did infringe the competition law rule. Thus, there may be room for a franchise contract with a territorial clause to survive the application of Art. 101(1) of the TFEU. For example, the territorial clause may not be considered a restraint on competition under Art. 101(1) of the TFEU if it has been agreed upon by the SMEs or local entrepreneurs. This conclusion is based on the assumption that the agreement made by the small businesses would not appreciably affect trade between the Member States or appreciably restrict competition in the light of Art. 101(1) of the TFEU.¹¹

The second scenario is that a franchise contract containing an exclusive territorial provision finds a safe harbor under the Block Exemption Regulation (BER).¹² Under the EU competition law regime, the BER applies to preclude the application of Art. 101(1) of the TFEU on vertical agreements.¹³ In some cases, a franchise contract with an exclusivity clause may be entitled to the presumption of legality by virtue of article 2(1) of the BER. However, three pre-conditions must be satisfied.

First, the market share of the franchisor and the franchisee must not exceed 30% of the relevant market.¹⁴ In this case, it could be inferred from the Guidelines on Vertical Restraints that, on an individual basis, a franchise agreement may survive Art. 101(1) of the TFEU.

Second, a franchise contract under consideration has no hardcore restrictions prescribed by article 4(a)-(e). For example, a franchise contract will

9 A franchise agreement, which is incompatible with Art. 101(1) of the TFEU, will be void automatically by virtue of paragraph (2) of Art. 101.

10 Case 161/84, 28 January 1986.

11 The European Commission takes this presumption. See the Commission Notice on Guideline on Vertical Restraints, at 5-6. The electronic version of the Notice can be accessed at <<https://bit.ly/2zd7qrQ>>.

12 The denomination 'Block Exemption Regulation (BER)' is shortened from Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices. The English text of the BER can be accessed at <<https://bit.ly/3hHKS pW>>.

13 The BER, art. 2(1).

14 The BER, art. 3(1).

be deemed to have a hardcore restriction in light of article 4(b)(i) if the territorial clause restricts passive selling into any exclusively allocated territory.¹⁵

Third, a territorial clause itself does not establish an obligation prohibited by article 5(1)(a)-(c). At a glance, the exclusivity clause in this context would not fall within the greylisted clauses enumerated by article 5(1)(a)-(c). Thus, a franchise contract with a territorial clause that meets the three criteria would be enforceable in light of the EU competition law regime.

Lastly, a franchise contract containing an exclusive territorial provision benefits from an individual exemption prescribed by Art. 101(3) of the TFEU. In this case, the four conditions set out by Art. 101(3) of the TFEU must be met. In practice, the satisfaction of the four criteria will be determined on an individual basis. The Commission provided in the Guidelines that a franchise contract with the following goals is likely to meet the conditions for an individual exception under Art. 101(3) of the TFEU. First, the franchise contract intends the territorial provision to create prospective franchisees' incentive to invest in a franchise business. Second, the franchise contract intends the exclusivity clause to balance the loss of intra-brand competition, which could, at least, help maintain the common identity of the network.¹⁶

4.2.2.3 Regulation by the implied terms of a franchise contract

Under the DCFR, a court may imply the terms governing the franchisor's duty not to encroach. In this case, the court may interpret an existing clause of the contract or fill a gap in the contract to establish the franchisor's obligation.

First, the franchisor's duty not to encroach may be established by way of interpreting the express terms through the rules of interpretation under II. – 8:101. In some cases, the exclusivity clause of a franchise contract may grant a franchisee an exclusive territory for operating a franchised business, but it is silent on whether the franchisor must refrain from competing with the franchisee in this area. Suppose the parties' common intention cannot be ascertained by II. – 8:101(1) and (2). In this case, II. – 8:101(3) provides that the court must interpret the contract according to the meaning which a reasonable person would give to it. Accordingly, the court may interpret the exclusivity clause in that the franchisor must not jeopardize the franchisee's interests in operating a franchised business in the exclusive area.

The way of interpretation mentioned in the preceding paragraph seems to be plausible in reality. In Austria, for example, the Supreme Court of Austria (OGH) concluded in 1991 that the franchisor had a fiduciary duty not to jeopardize the franchisee's legitimate interests because a franchise relationship was considered a strong relationship of trust. In this case, although the franchisor reserved the right to operate an online franchise business in the franch-

15 The Commission Notice on Guideline on Vertical Restraints, at [51] – [52].

16 Ibid, at [55] – [57].

isee's protected area, the franchisor was required to exercise the right with due regard to the franchisee's equitable interests. Thus, the court held that the franchisor breached the franchisee's trust because it competed with the franchisee in the sale area by offering end customers the goods at more favorable conditions.¹⁷ In Italy, an arbitral award in the case *Coin Store v Gruppo Coin* in 2004 provided that the territorial exclusivity clause had to be interpreted in accordance with good faith. Thus, the franchisor, who undertook under the territorial exclusivity clause not to supply the goods to the third parties' store in the franchisee's exclusive territory, could not supply the products to the stores belonging to the franchisor because those stores were considered the third parties under the exclusivity clause.¹⁸

Second, the franchisor's duty not to encroach may be established by way of implication. Under the DCFR, II. – 9:101(2) authorizes a court to imply additional terms into a contract when a noticeable gap in the agreement exists.¹⁹ In constructing the implied terms, the court needs to identify a clear gap in a contract. According to II. – 9:101(2), there will be a gap in the contract to which the court may imply terms if the parties to the agreement have not foreseen or provided for a matter.²⁰ In the context of intra-brand competition, the court must determine whether the franchisor and franchisee have not foreseen the likelihood of the intra-brand competition in a specific marketing area. Alternatively, the court must determine whether the parties have not deliberately accepted the risks by not providing the solutions on the competition issue. If the answers to both questions are affirmative, it could be said that the gap in a franchise contract exists.

In any case, the court may imply the terms into a franchise contract when filling the gap is necessary. According to the drafters of the DCFR, the court may have to make sure that other sources of the contractual term have not already dealt with the gap. For example, the court needs to consider if the term can be established by the rules of law. Furthermore, the court may have to ponder if filling the gap will render the contract workable.²¹ When the court is convinced that it is necessary to do so, the court may imply the term by taking into account (a) the nature and purpose of the contract; (b) the circumstances in which the contract was concluded; and (c) the requirement of good faith and fair dealing.²² These three factors provide a basis for

17 The German version of this court decision can be accessed at <<https://bit.ly/2DNECc2>>.

18 Aldo Frignani, 'Italian Case Law after Three Years since the Enactment of Law, 6 May, 2004, No. 129' (2007) 5 International Journal of Franchising Law 17, 19-20.

19 This implication procedure is said to resemble the German *ergänzende Vertragsauslegung* or constructive interpretation. See Bar and Clive (n 3) 553.

20 According to II. – 9:101(4), the court may not imply an additional term if the parties have foreseen a matter, but they have deliberately left the matter unprovided for, accepting the consequences of their choice.

21 Bar and Clive (n 3) 578.

22 The DCFR, II.- 9:101(2)(a)-(c).

concretizing the additional term, which must be determined on a case-by-case basis. In practice, many franchise contracts explicitly do not grant a franchisee an exclusive territory and allow a franchisor to market its products in the franchisee's location. In this case, there should be no room for courts to fill a gap in the contract. In some exceptional cases, I reckon that courts may add the terms into a franchise contract requiring a franchisor to refrain from competing with a franchisee in the franchisee's marketing area, provided that the parties are involved in an unforeseen dispute regarding the absence of the exclusivity and good faith is so required to solve the issue.

4.2.2.4 Conclusions

Under the DCFR, the franchisor's obligation to refrain from encroaching upon the franchisee's business is contractual-based because the DCFR does not offer model rules regulating the franchisor's duty not to encroach. Instead, the DCFR offers contract law rules facilitating the franchisor and franchisee to conclude a franchise contract with an exclusivity clause prohibiting the franchisor from competing with the franchisee in an exclusive area. This exclusivity provision seems to be enforceable in light of European competition law rules. The DCFR provides the interpretation rules that allow a court to interpret an existing clause of a franchise contract to constitute the franchisor's duty not to encroach. The DCFR also offers the gap-filling rules that authorize a court to imply an additional term into a contract to establish the franchisor's duty. In some exceptional cases, the franchisor can be required to avoid jeopardizing the franchisee's interests by operating a company-own outlet or enabling other franchisees to operate a franchised unit in competition with the existing franchisee's franchised store.

4.2.3 The United States of America (USA)

4.2.3.1 Introduction

In America, state franchise-specific law plays a significant role in regulating franchisor encroachment.²³ Currently, five relationship states – Hawaii, Indiana, Iowa, Minnesota, and Washington – regulate the franchisor's practice of encroaching upon a geographical territory of the existing franchisee through

23 Despite several attempts to propose the bills, no franchise-specific legislation has so far been enacted to govern an encroachment issue in a franchise relationship at the federal level. See Roger D Blair and Francine Lafontaine, *The Economics of Franchising* (2nd edn, Cambridge University Press 2011) 228; Uri Benoliel, 'Criticizing the Economic Analysis of Franchise Encroachment Law' (2011) 75(1) Albany Law Review 205, 211-12.

franchise relationship law rules.²⁴ Apart from franchise regulations, a franchise contract may contain the express or implied terms governing the franchisor's encroachment upon the franchisee's business. This section will examine the franchise relationship law rules regulating franchisor encroachment in subsection 4.2.3.2. After that, subsections 4.2.3.3 and 4.2.3.4 will explore the contractual approaches to regulating franchisor encroachment. Subsection 4.2.3.5 will conclude on the main approaches to regulating franchisor encroachment in the USA.

4.2.3.2 Regulation by the rules of franchise relationship law

Franchise relationship laws rules regulating the franchisor's encroaching conduct can be categorized into (1) anti-encroachment rules and (2) anti-unfair competition rules. This subsection will examine the extent to which two types of franchise rules address franchisor encroachment.

– Anti-encroachment rules

Iowa regulates franchisor encroachment through anti-encroachment rules.²⁵ In this state, anti-encroachment rules regulating the franchisor's encroachment are established under two legislative acts – chapters 523H and 537A.²⁶ In terms of regulation, the encroachment rule of the 1992 and 2000 Acts similarly imposes liability for damages against a franchisor for geographically encroaching upon the existing franchisee's business.²⁷ Under the rules, the franchisor will be liable for damages if the franchisor develops or grants a new franchisee the right to develop a new outlet or location, which sells essentially the same goods or services under the same trademark, service mark, trade name, logo-type, or other commercial symbols as the existing franchisee.

In holding the franchisor liable for damages, the 1992 and 2000 anti-encroachment rules similarly require the element of an adverse effect, meaning the new franchise outlet or location must have an adverse effect on the gross

24 In this sense, franchise relationship law means a franchise-specific statute regulating a contractual relationship between the franchisor and franchisee.

25 Benoliel (n 23) 209.

26 Those two statutes are commonly called the 1992 Act and 2000 Act, respectively. Nevertheless, those two Acts apply to franchise contracts that are concluded at a different point in time. While the 1992 Act applies to franchise contracts entered into before 1 July 2000, the 2000 Act governs those that are entered into on and after 1 July 2000. See Nancy L Lochner Howard, 'Iowa' in W Michael Garner (Ed), *Franchise Desk Book: Selected State Laws, Commentary and Annotations* (Vol 1, 3rd edn, American Bar Association 2019) [IA-27]. However, the 1992 Act does not have a retroactive effect and applies to franchise contracts entered into before the effective date of the 1992 legislation. See *GPP, Inc v Guardian Protection Products, Inc*, 2015 WL 3992878, (ED Cal, 2015) 12, citing *Holiday Inns Franchising, Inc v Branstad*, 29 F 3d (CA8 (Iowa), 1994).

27 IA ST, § 523H.6(1); IA ST, § 537A.10(6)(a).

sales of the existing franchisee. However, no court decision seems to have interpreted or clarified the phrase 'adverse effect'. Despite the lack of clarification, the terms 'adverse effect' could be said to resemble financial damage caused to the existing franchisee's business. For example, the lost profits calculated by the formula under the 1992 and 2000 Acts could be indicative of an adverse effect of the franchisor's encroachment upon the franchisee's existing business.

The 2000 Act's anti-encroachment rule differs from the rule of the 1992 Act in that the former requires the new franchise outlet to be located in unreasonable proximity to the existing franchisee's outlet.²⁸ However, the 2000 Act's rule does not offer a method for measuring unreasonable proximity. In my view, the 1992 Act, before its amendment in 1995, may offer some helpful guidelines for interpreting the phrase.²⁹ In the 1992 Act, the anti-encroachment rule offered two indecisive calculating methods for measuring unreasonable closeness. First, the distance may be unreasonable if it is the shortest distance measured by a three-mile radius, using a straight-line measurement, from the center of an already existing franchise. Second, the shortest distance, which is considered unreasonable, may be measured by a circular radius, using a straight-line measurement, from an existing franchise business, which comprises a population of thirty thousand or greater.³⁰

In some exceptional cases, the franchisor may escape the liability for damages for encroaching upon the existing franchisee's outlet. For example, the liability for damages is excused if the franchisor offers the existing franchisee the right of a first offer. According to the anti-encroachment rules, before placing a new franchise outlet or location, the franchisor must first offer the new outlet or location to the existing franchisee on the same basic terms and conditions available to other potential franchisees. Besides, in the case the franchisor will own that new outlet or location, the franchisor has to first offer the new outlet or location to the existing franchisee on the terms and conditions that would ordinarily be offered to a franchisee for a similarly situated outlet or location.³¹ In those cases, the franchisor will not be liable

28 Therefore, under the 2000 Act, a franchisor will be liable under two conditions. First, the franchisor places a new franchised outlet in unreasonable proximity to the incumbent franchisee's store. Second, the new store has an adverse effect on the gross sales of the existing franchisee. Suppose the franchisor licenses a new franchisee to open a franchised store on the other side of the highway by which an existing franchisee's outlet is located. In this case, the franchisor will be deemed to place a new franchised outlet in unreasonable proximity to the existing franchisee's store. However, the franchisor will not be liable if it can prove that the franchisee's gross sales are not adversely affected because the road creates a barrier that clearly divides potential customers of the franchisees.

29 Under the 1992 Act, the requirement of 'unreasonable proximity' was included in the anti-encroachment rule. However, that requirement has been pulled out of the 1992 statute because of the amendment in 1995.

30 HF 2362 (Iowa, 1992). The electronic file of HF 2362 is at the author's possession.

31 IA ST, § 523H.6(1)(a); IA ST, § 537A.10(6)(a)(1).

for damages for placing the new franchise outlet, which has an adverse effect on the existing franchisee's business.

– *Anti-unfair competition rules*

Besides Iowa, four relationship states – Hawaii, Indiana, Minnesota, and Washington – regulate franchisor encroachment through the franchise rules on the prohibition against unfair competition. In those jurisdictions, the contents of anti-unfair competition provisions vary. In Hawaii, a franchisor is prohibited from establishing a similar business or granting another franchisee to establish a similar business within an existing franchisee's exclusive territory.³² In Indiana, it will be unlawful for a franchisor to establish its own outlet engaged in a substantially identical business to a franchisee's business within the exclusive territory granted to the franchisee.³³ In Minnesota and Washington, it will be unlawful for a franchisor to compete with a franchisee or grant competitive franchises within an exclusive territory granted to the franchisee.³⁴

As can be seen in the preceding paragraph, the designation of an exclusive territory for a franchisee is a conditional element for the proscription of the franchisor encroachment. Accordingly, if a franchise contract does not grant a franchisee an exclusive territory, a franchisor will not be prevented from internally competing with the franchisee's business. However, there is an exception in Indiana. In this state, the anti-competition rule in franchise relationship law deals with the situation where a franchise agreement does not designate the franchisee's exclusive marketing area. Although a franchisor does not grant an exclusive area to a franchisee, it remains unlawful for the franchisor to compete unfairly with the franchisee within a reasonable area.³⁵ Whether the franchisor's conduct is regarded as unfair or whether the franchisee's area is considered reasonable may vary from case to case.

4.2.3.3 *Regulation by the express terms of a franchise contract*

– *Incorporation of an exclusivity clause*

In general, a franchise contract is a vital instrument that regulates an ongoing franchise relationship.³⁶ In the contractual freedom principle, the franchisor

32 HI ST, § 482E-6(e).

33 IN ST, 23-2-2.7-2(4).

34 MN ADC, 2860.4400(c); WA ST, 19.100.180(2).

35 IN ST, 23-2-2.7-2(4).

36 Robert W Emerson, 'Franchise Encroachment' (2010) 47(2) American Business Law Journal 191, 234 and 244.

and the franchisee can freely conclude a franchise contract for particular terms.³⁷ In some cases, the parties may conclude the franchise contract's terms governing the franchisor's duty not to encroach. In practice, that obligation is typically included in an exclusivity clause, granting a franchisee an exclusively protected area.³⁸ In America, some franchisee associations may play a vital role in encouraging the incorporation of an exclusivity provision into a franchise agreement to protect a franchisee's interests. For example, the American Association of Franchisees and Dealers (AAFD) promulgates the Fair Franchising Standards (Standards) to set fair franchising practices.³⁹

Under the AAFD's Standards, it is suggested that a franchisee has the right to reasonable market protection.⁴⁰ According to the commentary to the standard, reasonable market protection means a market opportunity, including 'multiple avenues' that are sufficient to provide the franchisee with a fair and adequate return on the investment. Moreover, the commentary advises that the franchisee's protected area should be free from the franchisor's cannibalization; the franchisor should avoid adversely impacting the franchisee's market or jeopardizing the franchisee's fair and adequate return. Nevertheless, the AAFD's Standards merely suggest the principles underlying an equitable franchise agreement. Accordingly, drafting the franchisor's duty not to encroach may be far from concrete from a practical viewpoint.

With that concern in mind, it may be advisable to have recourse to publications of some organizations that provide practical examples of drafting an exclusivity clause in a franchise contract. In the USA, the American Bar Association (ABA) is one institution that offers those objects. In the context of drafting a franchise agreement, the ABA offers a non-exhaustive list of sample franchise contract provisions in the book – Annotated Franchise Agreement.⁴¹

37 See eg *Consumers Intern, Inc v Sysco Corp*, 951 P 2d 897, 899, 191 Ariz 32 (Ariz App Div 1, 1997) 34; *Wisconsin Auto Title Loans, Inc v Jones*, 714 NW2d 155, 163, 290 Wis 2d 514, 530, 2006 WI 53 (Wis, 2006) 27; *CAS Severn, Inc v Awalt*, 75 A3d 382, 388, 213 Md App 683 (Md App, 2013) 693; *Gries v Plaza Del Rio Management Corp*, 335 P 3d 530, 535, 236 Ariz 8 (Ariz App Div 1, 2014) 13.

38 Robert W Emerson, 'Franchise Contract Clauses and the Franchisor's Duty of Care toward Its Franchisees' (1994) 72(4) North Carolina Law Review 905, 943-44. Furthermore, some empirical studies support this assumption. For instance, the 2002 study showed that the majority of the 114 sampled American franchisors assign the territorial right to their franchisees. See Mika Tuunanen, 'Exploring the Anatomy of Franchising: A Cross-National Examination of US and Finnish Franchise Contract Provisions' in Josef Windsperger and others, *Economics and Management of Franchising Networks* (Physica-Verlag 2004) 301-03.

39 The text of the AAFD's Fair Franchising Standards can be downloaded at <<https://bit.ly/3xUDHAA>>.

40 The AAFD's Fair Franchising Standards, standard 3.1.

41 This book is said to present common terms and conditions that can be drawn from typical franchise agreements. This publication aims to provide guidelines specifically designed for practitioners who are inexperienced in drafting franchise contracts. Nevertheless, there is a caution; the book aims to offer the sample clauses suitable for restaurant franchising.

In that publication, the model provisions concerning grant and reservation of rights deal with various issues relating to encroachment by a franchisor. These model contract terms are elaborated in section IV of Chapter 1.

According to section IV(B)(1), if a franchise agreement designates an exclusive territory for the franchisee, the franchisor may agree not to operate or authorize other franchisees to open a franchised store from a physical location within the protected area. The franchisor may be prevented from doing so on the condition that the franchisee fully complies with the franchise agreement and all other agreements between the franchisor and the franchisee.⁴² It should be noted that this provision merely prohibits the franchisor from engaging in traditional encroachment. In other words, the model clause does not regulate the franchisor's non-traditional encroachment by internet sales or distribution through other retail stores. This exclusion is attributable to the ABA authors' intention that this anti-encroachment provision is limited to the prohibition against traditional or geographical encroachment by a franchisor.⁴³

– *Implications of US antitrust laws for an exclusivity clause*

It should be borne in mind that some franchising arrangements can be subject to the reach of American antitrust laws. For instance, non-price intra-brand distribution restraints created by an exclusive territory and location agreement may have to survive the federal antitrust law rules.⁴⁴ In particular, a restraint of trade under an exclusivity clause needs to be valid in light of section 1 of the Sherman Act of 1890 because this provision constitutes a general rule prohibiting agreements that is an unreasonable restraint of trade or commerce.⁴⁵ According to case law, territorial restrictions are considered vertical restraints, which are subject to the justification under the rule of reason.⁴⁶

See Nina Greene, Dawn Newton, and Kerry Olson (eds), *The Annotated Franchise Agreement* (2nd edn, American Bar Association 2021) at xxi-xxvi.

42 Robert A Lauer and Larry Weinberg, 'Introductory Terms, Grant, Territory, and Reservation of Rights' in Nina Greene, Dawn Newton, and Kerry Olson (eds), *The Annotated Franchise Agreement* (2nd edn, American Bar Association 2021) 18.

43 Ibid 22.

44 Nowadays, US antitrust laws have been enacted as statutory laws at federal and state levels. Although some states have their competition laws applying within their jurisdictions, the three federal antitrust laws – the Sherman Act of 1890, the Clayton Act of 1914, and the Federal Trade Commission Act of 1914 – play a significant role in the governance and promotion of competition in the market.

45 *Pacific Steel Group v Commercial Metals Company*, 2022 WL 1225030 (ND Cal, 2022) 10.

46 See eg *Lafortune v Ebie*, 102 Cal Rptr 588, 590, 26 Cal App3d 72 (Cal App 1972) 75; *Continental T V, Inc v GTE Sylvania Inc*, 97 S Ct 2549, 2562, 433 US 36 (US Cal, 1977) 58; *Shulton, Inc v Optel Corp*, 1986 WL 15617 (DNJ, 1986) 22; *Monmouth Chrysler-Plymouth, Inc v Chrysler Corp*, 509 A.2d 161, 166, 102 NJ 485 (NJ, 1986) 495; *St Martin v KFC Corp*, 935 F Supp 898 (WD Ky, 1996) 905; *Abbott Laboratories v Adelpia Supply USA*, 2017 WL 5992355 (EDNY, 2017) 3; *Wyoming Beverages, Inc v Core-Mark International, Inc*, 2018 WL 8221068 (D Wyo, 2018) 4.

This rule is used to determine an unreasonable restraint of trade under section 1 of the Sherman Act.⁴⁷ The rule of reason requires a court to determine whether the restraint promotes or suppress, or even destroy, competition. In other words, the court needs to determine whether the restraint has an anti-competitive effect on a given market.⁴⁸

In the franchising context, an exclusivity clause creating territorial restrictions also has to pass the test under the rule of reason to be enforceable under section 1 of the Sherman Act. In practice, the clause is likely intact in light of the national antitrust rule. In other words, an exclusivity clause in a franchise contract is ordinarily justified by the rule of reason because of its legitimate aims. For instance, some commentators provide that the territorial restrictions usually are justified if the franchisor utilizes the restrictions to promote intra-brand or inter-brand competition.⁴⁹ Consequently, the franchisor's duty not to encroach would validly be established under an exclusivity clause of a franchise agreement.⁵⁰

4.2.3.4 Regulation by the implied terms of a franchise contract

In some non-regulating states, courts may step in to protect a franchisee against the franchisor's encroachment by implying protective terms into a franchise contract. In particular, judges may imply the covenant of good faith and fair dealing in the agreement. A combination of Florida's court decisions in *Scheck v Burger King* (*Scheck I* and *Scheck II*) may provide an interesting example in this regard.⁵¹ These court decisions are seemingly the earliest examples in

47 *United States v Harwin*, 2021 WL 719614 (MD Fla, 2021) 2.

48 *Texaco Inc v Dagher*, 126 S Ct 1276, 1279, 547 US 1 (US, 2006) 5; *Allied Orthopedic Appliances Inc v Tyco Health Care Group LP*, 592 F3d 991 (CA 9 (Cal), 2010) 996; *In re Delta Dental Antitrust Litigation*, 484 F Supp 3d 627 (ND Ill, 2020) 633.

49 Kay Lynn Brumbaugh and Michael K Lindsey, 'Chapter 6: Antitrust Law' in Rupert M Barkoff and others (eds), *Fundamentals of Franchising* (4th edn, American Bar Association 2016) 259.

50 Courts in some relationship states expressly affirm the valid incorporation of an exclusive territory clause into a franchise contract. For example, the Indiana court in *Sheldon v Munford* affirmed that the incorporation of an exclusivity provision into a franchise agreement was permissible. The court based its decision on the fact that Indiana has a franchise relationship statute prohibiting the franchisor's practice of unfairly competing with the franchisee within an exclusive territory. See *Sheldon v Munford, Inc*, 660 F Supp 130 (ND Ind, 1987) 135. This court decision is then cited to demonstrate that the Indiana Deceptive Franchise Practices Act allows the franchisor to agree not to compete with its franchisees in the granted exclusive territories. Thus, the exclusivity and noncompetition clauses will not violate the antitrust law. See Paul J Galanti, 'Chapter 54. Franchise and Franchising'. Indiana Practices Series. Business Organizations. Westlaw. (October 2021 Update) at § 54.8; Larissa J Erkman, 'Monopolies and Combinations in Restraint of Trade' Indiana Law Encyclopedia. Westlaw. (March 2022 Update) at § 4.

51 *Scheck v Burger King Corp*, 756 F Supp (SD Fla, 1991) [Scheck I], and *Scheck v Burger King Corp*, 798 F Supp (SD Fla, 1992) [Scheck II].

relation to this issue. In these two cases, the factual background upon which the franchisee's lawsuit was based is that the franchisor licensed the new franchise store to open two miles from the plaintiff franchisee's location. According to this fact, the franchisee claimed that the franchisor breached the implied duty of good faith and fair dealing.⁵²

In *Scheck I*, the defendant franchisor filed the motion for summary judgment to dismiss the case. In moving to dismiss, the franchisor argued that it was not in bad faith because the franchise agreement did not grant any territorial rights to the franchisee. In other words, the agreement authorized the franchisor to expand new franchised outlets.⁵³ Nevertheless, the district court did not buy into the franchisor's proposition. The court posited that the explicit denial of the exclusive territory did not imply that the franchisor held the unlimited right to open other proximate franchise restaurants regardless of the effect on the franchisee's operations. In other words, the franchisee remained entitled to expect that the franchisor would not harm the right to enjoy the fruits of the agreement despite no exclusive territorial rights. Thus, the court concluded that the franchisor allegedly breached the covenant of good faith and then denied granting a summary judgment in favor of the franchisor.⁵⁴

In disagreement with the order denying summary judgment, the franchisor filed the motion to reconsider, which was then considered in the case *Scheck II*. However, the district court denied the reconsideration motion. In this case, the court remained persuasive that the franchisor did not retain the unfettered right to open franchise restaurants at any territory, although the franchise agreement did not confer on the franchisee an exclusive territory. Furthermore, the court contended that it did not imply the covenant of good faith and fair dealing in derogation of the express terms of the contract since the agreement did not explicitly address the franchisor's right to expand a franchised business at will. Conversely, the outcome would have been different had the franchisor expressly reserved the right to open franchise restaurants at any location desired. Therefore, the judge in *Scheck II* affirmed the denial of summary judgment released in *Scheck I*.⁵⁵

The judge in *Scheck I* and *Scheck II* circumvented the express terms of the franchise agreement to imply the covenant of good faith and fair dealing, preventing the franchisor from establishing the new franchised store that would

52 *Scheck I*, *ibid* 549.

53 The contractual clause on which the franchisor relied stated that the franchise agreement grants no exclusive area, or market or territorial rights to the franchisee. According to this statement, the court accepted that the franchisee was not entitled to the exclusive right over the territory under consideration. *See Scheck I*, *ibid*.

54 *Scheck I* (n 51) 549. It should be noted that this conclusion was drawn on the fact that the franchisor developed its policies and procedures to address the cannibalization that might ruin franchised restaurants and weaken the franchise network.

55 *Scheck II* (n 51) 696 – 97.

harm an existing franchisee's legitimate interests. Implying the covenant of good faith to bar franchisor encroachment was then adopted in some subsequent cases, such as the case *In re Vylene Enterprises*.⁵⁶ Nevertheless, the decisions in *Scheck I* and *Scheck II* must be read with caution as other courts have expressly denied following the reasoning made in these cases.

For example, the court in *Burger King v Weaver* found the reasoning of *Scheck I* and *Scheck II* unconvincing logically. According to the court, if the franchise contract conferred no exclusive territory on the franchisee, the franchisor would have no duty to refrain from enfranchising other new franchisees' franchised stores in the conflicting area.⁵⁷ In addition, some practitioners expostulate with the *Scheck I* and *Scheck II* decisions. For instance, Garner says that the decisions seem to go beyond the limits of judicial invocation of the duty of good faith in connection with express terms.⁵⁸ Furthermore, Harman questions how to describe the area within which other franchise outlets cannot open if no exclusive territory is granted to the existing franchisee.⁵⁹

4.2.3.5 Conclusions

The approach to regulating the franchisor's duty not to encroach is essentially twofold. The first approach is statutory. Five states' franchise relationship law specifically regulates the franchisor's practice of encroachment through anti-encroachment rules and anti-unfair competition rules. The rules typically prevent a franchisor from geographically encroaching upon the franchisee's marketing location. The second model is contractual. In this model, the terms of a franchise contract will address the encroachment issues. A franchise agreement may contain an express provision – an exclusivity clause – that requires the franchisor to refrain from encroaching upon the exclusive territory granted to the franchisee. In practice, the franchisor may reserve the right to compete with the franchisee's business through non-traditional channels of distribution, such as online sales. Exceptionally, certain courts may imply the covenant of good faith and fair dealing to establish the franchisor's duty not to cannibalize the franchisee's legitimate interests, including the duty not to encroach. Nevertheless, it would seem that US courts have not uniformly adopted this legal approach.

56 *In re Vylene Enterprises Inc* 90 F 3d 1472 (9th Cir 1996) 1477.

57 *Burger King Corp v Weaver*, 169 F3d (CA11 (Fla), 1999) 1317.

58 W Michael Garner, 'The Implied Covenant of Good Faith in Franchising: A Model for Discretion' (1995) 20(2) Oklahoma City University Law Review 305, 320-21.

59 Kathryn Lea Harman, 'The Good Faith Gamble in Franchising Agreements: Does Your Implied Covenant Trump My Express Term?' (1997-1998) 28 Cumberland Law Review 473, 505.

4.2.4 Australia

4.2.4.1 Introduction

Australia does not explicitly regulate the franchisor's duty not to encroach by statutes. Despite the lack of express regulation, certain rules of the Franchising Code of Conduct (the Code) could be employed to prevent a franchisor from encroaching upon a franchisee's business. The terms – be it express or implied – of a franchise agreement may establish or have an effect establishing the franchisor's obligation not to cannibalize the franchisee's operation of a franchised business. This section will examine how and the extent to which the Code regulates franchisor encroachment in subsection 4.2.4.2. Next, subsections 4.2.4.3 and 4.2.4.4 will explore the regulation of franchisor encroaching conduct by the express and implied terms of a franchise contract. Subsection 4.2.4.5 will summarize the problem-solving approaches under the Australian legal system.

4.2.4.2 Regulation by the rule of the Franchising Code of Conduct

As mentioned in the introduction, the Code does not directly regulate franchisor encroachment. Nevertheless, the Code regulates the parties' conduct through the rule imposing the obligation to act in good faith.⁶⁰ In this respect, some commentators claim that the franchisor encroaching practices may be constrained by the principle of good faith and fair dealing.⁶¹ Regarding this claim, a question arises: when is the franchisor's encroaching conduct treated as contrary to the requirement of good faith and fair dealing? In general, the scope of an obligation to act in good faith under the Code seems to be narrow. In *ACCC v Geowash Pty Ltd (No 3)*, Colvin J summarized unwritten law concerning the meaning of good faith under the Code. One of the summaries was that good faith would prevent the parties' conduct that was dishonest, capricious, arbitrary or motivated by a purpose which was hostile to the evident object of any provision of the franchise agreement or the Code or the parties' conduct motivated by bad faith. In other cases, good faith would not require the parties to subordinate their legitimate interests to the other party. Instead, it merely required due regard to the other party's legitimate interests in the performance of a franchise contract.⁶²

⁶⁰ The Code, cl. 6(1).

⁶¹ Tim Golder and Andrew Fuller, 'The risks of 'e-tailoring' a franchise system' (2006) 9(4) Internet Law Bulletin 41, 42-43.

⁶² *Australian Competition and Consumer Commission v Geowash Pty Ltd (No 3)*, [2019] FCA 72 [746]. Colvin J's summary of good faith has recently been cited by the Supreme Court of Victoria in *Lanhai Pty Ltd v 7-Eleven Stores Pty Ltd*, [2022] VSC 132 [149].

Concerning the meaning of good faith summed up by Colvin J, the franchisor would be considered acting in good faith if it has encroached upon the existing franchisee's business to pursue its legitimate business interests. In *Far Horizons v McDonald's Australia*, the franchise agreement under consideration did not grant the franchisee an exclusive territory or protected area. Despite the absence of exclusivity, Byrne J, implied the duty of good faith and fair dealing on the franchisor. In this regard, the franchisor was obliged to exercise its powers in good faith; that is to say, the franchisor must act reasonably and not capriciously or for some extraneous purpose.⁶³ In the context of placing a new franchised outlet, the judge provided that the franchisor may operate its store near the franchisee's outlet insofar as the franchisor has the incentive to promote its commercial interests. In other words, it would be contrary to good faith if the franchisor opens the new store as a means of pressuring the franchisee into surrendering the license.⁶⁴

The Australian Competition and Consumer Commission (ACCC) correspondingly adopts the pursuit of legitimate business goals test. On the ACCC's website, the franchisor encroachment is selected as an example of performing the duty of good faith. The example illustrates that the franchisor is regarded as acting in good faith in light of the Franchising Code of Conduct if it decides to open a new store in the vicinity of the franchisee's outlet because of the perceived commercial benefits of expanding its system. Nevertheless, it could be implied from the ACCC's illustration that the franchisor cannot argue for its legitimate business aims under some circumstances. For example, the franchisor may not be able to place a new franchise store in the location of the franchisee for the legitimate aims if the franchisee has an exclusive territory or the franchise agreement bars the franchisor from doing so.⁶⁵

4.2.4.3 Regulation by the express terms of a franchise contract

– Incorporation of an exclusivity clause

Australia accepts the contractual freedom that the parties are free to conclude a contract for specific terms.⁶⁶ In this respect, a franchise agreement may deal with the matter of franchisor encroachment explicitly. A franchise agreement may incorporate the terms granting an exclusive franchise territory to a franchisee. For example, in *Haviv Holdings v Howards Storage World*, clause 1C

63 *Far Horizons Pty Ltd v McDonald's Australia Ltd*, [2000] VSC 310 [120]. By the time, the duty of good faith was not statutorily established and imposed on the franchisor. However, because the court employed the duty of good faith to examine the franchisor's conduct, this decision would serve as a good illustration of the function of the good faith obligation under the Code.

64 *Far Horizons*, *ibid* [122] and [130].

65 ACCC, 'Acting in good faith' can be accessed at <<https://bit.ly/3hrWH3p>>.

66 J W Carter, *Contract Law in Australia* (7th edn, LexisNexis 2018) 8.

of the franchise agreement at issue provided that the franchisees were granted an exclusive franchise territory. Although the franchisor's duty not to encroach was not elaborated in the contract, the court construed that the franchisor could not grant a franchise to a third party within the franchisees' territory as this exclusivity was a valuable right of the franchisees.⁶⁷ Nevertheless, it would be wise to avoid conflicting interpretations by explicitly establishing the franchisor's duty not to encroach under the exclusivity provision.

– *Implications of Australian competition law for an exclusivity clause*

An exclusivity clause in a franchise agreement may have to be tested for validity in light of Australian competition law – the Competition and Consumer Act 2010 (CCA). Under the CCA, section 47 expressly prohibits the practice of exclusive dealing that has the purpose, or has or is likely to have the effect, of substantially lessening competition.⁶⁸ In that case, the exclusive arrangement prohibited by the CCA's provision will be unenforceable.⁶⁹ In the franchising context, some restrictions may be regarded as the practice of exclusive dealing. For example, the franchisor may be considered engaging in the exclusive dealing practice if, under a franchise agreement, the franchisor supplies or offers to supply goods or services on the condition that the franchisee will not re-supply the goods or services in particular places.⁷⁰

It is questionable if the clause of a franchise contract that prevents the franchisor from placing a new franchise store in the franchisee's exclusive territory is regarded as exclusive dealing in light of the CCA's rule. According to Buchan, allocating exclusive territories in franchising can be considered exclusive dealing.⁷¹ Despite this, the arrangement that shields the franchisee from intra-brand competition seems to survive the prohibition on exclusive dealing under the CCA as it has no anti-competitive purpose or effect.⁷²

4.2.4.4 Regulation by the implied terms of a franchise contract

In contract law, the franchisor's duty not to encroach could be implied. According to Buchan, a franchise contract can be an incomplete contract; hence, terms

67 *Haviv Holdings Pty Limited v Howards Storage World Pty Ltd*, [2009] FCA 242, [13], [32], and [45].

68 The CCA, s. 47(1) and (10).

69 *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410; *John S Hayes & Associates Pty Ltd v Kimberly-Clark Australia Pty Ltd* [1994] FCA 550; 52 FCR 201.

70 The CCA, s. 47(2)(f)(ii).

71 Jenny Buchan, 'How Competition Law May Affect Franchised SMEs in APEC Economies' in Michael T Schaper and Cassey Lee (eds), *Competition Law, Regulation & SMEs in the Asia-Pacific: Understanding the Small Business Perspective* (ISEAS-Yusof Ishak Institute 2016) 166.

72 John Pratt and Marco Hero, 'Chapter 7: Competition Laws and Data Privacy' in Will K Woods (ed), *Fundamentals of International Franchising* (2nd edn, American Bar Association 2013) 284.

may be implied into a franchise contract under some circumstances.⁷³ Under Australia's contract law, several doctrines can support the implication of the franchisor's obligation. For example, Terry and Lernia propose that Australian courts may utilize the doctrine of non-derogation from grant to address encroachment in franchising.⁷⁴ In doing so, the commentators suggest that the courts follow the precedent laid down by Finkelstein J in *JLCS v Squires Loft City Steakhouse* that applied the doctrine of non-derogation from grant in the case of licensing a trademark.⁷⁵

According to Finkelstein J, the principle of non-derogation from grant can be employed to require the licensor to avoid unduly interfering with the licensees' use of the trademark and goodwill derived from the use of the mark. The judge further elaborated that the licensor's interference would be undue if it weakened the value of the mark to the licensees. Thus, the licensor has a duty not to use or permit the use of the mark in a way that would have a significant adverse effect on the goodwill of the licensees' business. In this respect, not only can the licensor not open a new restaurant next to the licensees', but the licensor also cannot open the new restaurant so proximate to the licensees' that would significantly affect the licensee's goodwill. In Finkelstein J's opinion, a distance of fewer than 500 meters is considered too close and unreasonable.⁷⁶ Therefore, if applying this precedent in the franchising context, the franchisor could be required not to open a new franchised outlet in close proximity to the existing franchisee's operation that would diminish the value of the latter's business.

Buberis also suggests that a franchise agreement may contain implied terms. An example of these terms is that the franchisor may be barred from establishing other franchised outlets near the existing franchisee even though there is no territorial exclusivity. Buberis argues that the franchisee may convince Australian courts to follow the decision of the Canadian court in *Provigo Distribution v Supermarche Inc*, which implied the franchisor's duty to support and assist. According to him, this assistance duty would prevent the franchisor from encroaching upon the franchisee's business. Nevertheless, Buberis seems to accept that no case law has so far followed his suggestion.⁷⁷

73 Jenny Buchan, *Franchisees as Consumers: Benchmarks, Perspectives and Consequences* (Springer 2013) 77-78.

74 Andrew Terry and Cary Di Lernia, 'Franchising and the Quest for the Holy Grail: Good Faith or Good Intentions' (2009) 33(2) Melbourne University Law Review 542, 554.

75 The judge summarized the maxim that 'a grantor must not derogate from his grant, that is to say, he must not seek to take away with one hand what he has given with the other.' See *JLCS Pty Ltd v Squires Loft City Steakhouse Pty Ltd* [2008] FCA 867 [30].

76 Ibid [34] – [35].

77 Peter Buberis, *Australian Franchising Code of Conduct: A Critical Analysis with Current Case law* (Emerald Publishing 2020) 34-35.

4.2.4.5 Conclusions

The approach to regulating franchisor encroachment under the Australian legal system is twofold. First, the Franchising Code of Conduct requires a franchisor to act towards a franchisee in accordance with good faith. This good faith duty would require the franchisor not to encroach upon the existing franchisee's business for a purpose that is hostile to the evident object of provisions of a franchise agreement or the Code or a purpose motivated in bad faith. Second, the terms of a franchise agreement may protect a franchisee against franchisor encroachment. In some cases, a franchise contract may incorporate an exclusivity clause that grants the franchisee the exclusive marketing area. In this case, the franchisor may not be able to place new franchised units within that territory. In other cases, the franchisor's duty not to encroach may be implied by courts. Nevertheless, the implication of this obligation would not be allowed if a franchise contract expressly provides otherwise.

4.2.5 Comparative analysis

4.2.5.1 Introduction

From the descriptive examination, the regulation of franchisor encroachment under the franchise legal framework of the DCFR, the USA, and Australia can be contractual and legislative. A franchise contract may contain express and implied terms governing the franchisor's encroaching conduct. Furthermore, encroachment by a franchisor may be regulated by franchise relationship law rules. This section will conduct a comparative examination of these two legal approaches in subsection 4.2.5.2. Then, subsection 4.2.5.3 will summarize the comparison and enumerate key recommendations concerning the regulation of the franchisor's duty not to encroach under comprehensive franchise law.

4.2.5.2 Comparison and analysis

– Regulation of franchisor encroachment by contractual terms

(1) Similarity

The DCFR, the USA, and Australia are similar in that the three legal systems allow the establishment of a franchise contract's terms governing franchisor encroachment.⁷⁸ In the selected legal systems, a franchisor and a franchisee may agree on an exclusivity provision that, among other things, establishes the franchisee's exclusive marketing area and the franchisor's obligation not to encroach on that territory. According to the principle of freedom of contract,

⁷⁸ See subsections 4.2.2.2, 4.2.3.3, and 4.2.4.3.

the contracting parties are free to determine the contents and scope of their agreement unless mandatory rules provide otherwise. Thus, it is commonplace that several franchise agreements incorporate exclusivity clauses establishing franchisees' exclusive territory and preventing franchisors from cannibalizing those areas of the franchisees.

In addition, contract law rules of the DCFR, the USA, and Australia similarly permit a court to fill a gap in a franchise contract by implying contractually binding terms.⁷⁹ Where expressly agreed terms are absent, a court may, in some exceptional circumstances, imply the terms preventing a franchisor from arbitrarily encroaching upon a franchisee's business.⁸⁰ In this respect, a franchisor may be required to refrain from encroaching on a franchisee's business, such as placing a new franchised store within the vicinity of the franchisee's area, without legitimate grounds. In this case, an objective standard for the implication is basically similar. Under the DCFR and the US legal system, a court may consider the requirement of good faith and fair dealing when implying terms regarding franchisor encroachment. Likewise, in Australia, a judge may supply anti-encroachment terms into a franchise agreement utilizing the doctrine of non-derogation from grant of which good faith is the genesis.⁸¹

(2) *Difference*

The difference between the franchise legal framework of the DCFR, the USA, and Australia seems to be subtle. As can be seen, if a franchise contract contains an exclusivity clause, the validity of this exclusive provision will be assessed by the rules of competition law since this clause has anti-competitive effects on a franchise network. The exclusivity clause will survive applicable competition or antitrust law rules under the selected legal systems.⁸² However, the reason why this clause is valid varies among the chosen legal systems. In the context of the DCFR, an exclusive territory clause may be enforceable in light of the European competition law because of three reasons. For example, an exclusive territorial clause may be presumed to be lawful under the Block Exemption Regulation (BER). In the USA, an exclusivity clause is likely justified under the rule of reason, which prevents it from violating the Sherman Act. In Australia, an exclusive territorial clause may not be prohibited by the CCA as it does not have the purpose or effect of substantially lessening competition.

⁷⁹ See subsections 4.2.2.3, 4.2.3.4, and 4.2.4.4.

⁸⁰ It should be noted that, in the USA, some courts insist that the principle of good faith cannot be used to imply an obligation that would be inconsistent with, or contemplated by, the contractual terms or the contractual relationship. See *eg Dalton v Educational Testing Service*, No 263, 87 NY2d 384, 389, 663 NE 2d 289, 292, 639 N.Y.S.2d 977, 980, 1995 WL 717083 (NY, Dec 07, 1995); *Ophthalmic Surgeons, Ltd v Paychex, Inc*, 632 F 3d 31, 41 (CA 1 (RI), 2011) 41; *Primarque Products Co Inc v Williams West & Witts Products Company*, 303 F Supp 3d 188 (D Mass, 2018) 205.

⁸¹ Terry and Lerner (n 74) 554.

⁸² See subsections 4.2.2.2, 4.2.3.3, and 4.2.4.3.

Despite varying reasons, it is likely that the incorporation of an exclusivity clause preventing a franchisor from encroaching upon a franchisee's franchised business is not restricted by the competition law of the selected legal systems.

(3) *Discussion*

From the comparison, the use of expressly agreed terms in a franchise agreement to govern the franchisor's duty not to encroach seems to be typical in franchising practice. From my point of view, this kind of regulation is beneficial in that a franchise contract can provide crystal clarity with regard to rights and duties associated with franchisor encroachment. In light of the principle of contractual freedom, recognized by many legal systems, a franchisor and a franchisee would be able to elaborate the terms regarding the franchisee's right to exclusivity against traditional and non-traditional encroachment by a franchisor. This subsection will first exemplify the benefits of regulating traditional and non-traditional encroachment by the expressly agreed terms in the following headings (3.1) and (3.2). The subsequent headings (3.3) and (3.4) will discuss a major constraint of this approach from a franchisee's perspective and the protective role of judicial intervention in this regard.

(3.1) *Traditional encroachment*

In some cases, an exclusive territory clause in a franchise contract requires a franchisor to refrain from engaging in traditional or geographical encroachment. For example, the clause may require the franchisor not to place a company-own franchise store or authorize other newcomer franchisees to open a franchised outlet within an exclusive area granted to the existing franchisee. The exclusivity clause may clarify some practical issues concerning the geographical scope of bricks and mortar and mobile franchises. In other words, the term can precisely allocate and define the size of an exclusive location granted to a franchisee. A high degree of certainty regarding the geographical scope of an exclusive territory would facilitate the enforcement of the franchisor's performance of the obligation.

(3.1.1) *Bricks and mortar franchise unit*

In some franchise businesses, the franchisee's operation is carried out at fixed premises, such as retail shops. In defining the terrestrial scope of a bricks and mortar franchised unit, a franchisor and franchisee can choose various parameters to designate the franchisee's exclusive territory. For example, the parties may specify the franchisee's location through the use of population, distance such as a specified radius of the building, zip codes, and administrative jurisdictions such as municipalities, districts, provinces, and regions. For example, in the USA, the franchisor in the case *Newspaper* granted the franchisee an exclusive territory covering the region, including Minnesota, Iowa, North Dakota, South Dakota, and twelve counties of Wisconsin bordering Minnesota

and Iowa.⁸³ If the methods identified earlier are not suitable, the parties may demarcate the boundary of the protected area by hand drawing.⁸⁴

Some criteria, such as population and governmental units, may be susceptible to modifications. For instance, a government may initiate the creation or division of new administrative territory, affecting the delineation of the franchisee's location under an exclusivity clause. In this case, it would be advisable that a franchisor and a franchisee anticipate and conclude contract terms, addressing solutions or the rights and duties of the parties in the case of changes. For instance, a franchise agreement may contain the terms conferring the franchisee the right to terminate or the right to relocate on the condition that the geographical scope of the protected territory is substantially affected by the territorial division by the government.

(3.1.2) *Mobile franchise unit*

Franchise units can be movable. In contrast to fixed-site franchising, mobile franchises distribute goods or services using moving vehicles such as vans and mini-trucks.⁸⁵ Imagine one franchised food truck stops by *Scheveningen* beach and offers '*Hollandse Nieuwe*' or raw herrings to sea-goers on Saturday and goes to sell the special herrings at *Katwijk* beach on Sunday. At *Katwijk* beach, another franchised truck may be selling the food just across the street. As can be seen from the hypothetical situation, the mobility of service units increases the chance of intra-brand competition; members of a franchise network might race each other to the areas where potential customers are domiciled. Without a well-defined territory, franchise food trucks of the same franchise system might saturate the market, which would cause financial losses to the truck service operators.⁸⁶

In the context of mobile franchising, a franchisor and a franchisee could fix such potential chaos by defining an exclusive area for marketing goods or services by a mobile unit. In this case, the parties may consider the most appropriate parameter, which may vary from case to case, to locate the protected area of the franchisee's mobile truck. In some cases, the franchisee's exclusive territory may be specified by reference to administrative territories. For example, the first ice-cream truck franchisee may be assigned to operate

⁸³ *Newpaper, LLC v Party City Corp.*, 2013 WL 5406722 (D Minn, 2013) 1.

⁸⁴ Lauer and Weinberg (n 42) 17.

⁸⁵ John F Preble and Richard C Hoffman, 'Competitive Advantage through Specialty Franchising' (1994) 8(2) *Journal of Services Marketing* 5, 6; Lilly Chow and Lorelle Frazer, 'Servicing customers directly: Mobile franchising arrangements in Australia' (2003) 37(3/4) *European Journal of Marketing*, 594, 595.

⁸⁶ Despite the designation of an exclusive territory, it should be noted that many franchisors include carving-out exceptions in a franchise contract. In the contract, the franchisor may reserve the right to market goods or services in captive markets, such as malls, universities, and petrol stations, in the franchisee's territory or the right to distribute the products in special events, such as the FIFA World Cup and the Olympic games.

the business in The Hague, while the second franchisee is authorized to sell products in Leiden. This delineation is not uncommon in practice. In Australia, some franchisors may define the scope of the mobile franchisee's area using postcodes.⁸⁷ In my opinion, this way of designation would result in a sizeable marketing location that would enable each mobile franchised unit to entice a reasonable number of customers to increase the volume of products sales. This wide protected area would also decrease potential competition in a franchise network as it shields one mobile franchisee from competing with the other.

(3.2) *Non-traditional encroachment*

Due to the variety in marketing techniques, a franchisor may compete with its franchisees within an exclusive territory in non-traditional ways. For example, the franchisor may engage in internet encroachment by selling goods or providing services to customers in the territory of the franchisee through the franchisor's transactional website. Because of the advancement of the internet, many businesses have increasingly been active in electronic commerce. It is not surprising that franchise businesses also engage in that activity. According to the empirical study conducted by Dixon and Quinn, some franchisors utilize their websites to facilitate online ordering and payment.⁸⁸

A franchisor's internet sales within the franchisee's exclusive location would trigger a conflict between the parties. Some disputes end up in courts because the parties could not anticipate the conflict at the time of the conclusion of a franchise contract. In this case, some scholars suggest that a franchise contract can be employed to regulate online practices.⁸⁹ In doing so, a franchisor and a franchisee may conclude an express exclusivity agreement to align the interests of the parties over online marketing in an exclusive area. For instance, the franchisor may agree to solely operate a transactional website, receiving and processing orders from customers in its franchisees' marketing area. When it comes to finalizing the delivery of the orders, the franchisor may ask the customers to pick up their packages at the nearest franchise unit.⁹⁰

Concerning the abovementioned approach, I believe that an exclusivity agreement would benefit a franchisee if the terms of the agreement are self-evident in that the franchisor only acts as an intermediary between online customers and the franchisee. In other words, the franchisee's interests will be protected if the franchisor operates a website receiving orders from online

⁸⁷ Chow and Frazer (n 85) 605-06.

⁸⁸ Helen Dixon and Barry Quinn, 'Franchising and the Internet: an exploratory study of franchisor Web sites' (2004) 14(4) *Internet Research* 311, 317.

⁸⁹ Gwen Fontenot, Anne Keaty, and Rajesh Srivastava, 'Selling on the Internet into the Franchisee's Territory' (2006) 13(3) *Journal of Marketing Channels* 79, 82.

⁹⁰ Rozenn Perrigot, Guy Basset and Gérard Cliquet, 'E-commerce opportunities and challenges for franchise chains' in Frank Hoy, Rozenn Perrigot, and Andrew Terry (eds), *Handbook of Research on Franchising* (Edward Elgar Publishing 2017) 280.

customers on behalf of the franchisee, who operates a franchised store in the location of the customers' residences. In this case, franchisees will sell and deliver the products from their stock, thereby gaining profits from sales generated through the franchisor's website. It should be noted that the franchisee may be required to pay operating costs to the franchisor in exchange for the franchisor's service.

(3.3) *Major constraint on a franchisee*

Theoretically, a franchisee may receive favorable terms in a franchise contract. A franchisee may bargain for the terms that favor the franchisee's interest if the franchisor has compelling reasons to give the franchisee those favorable terms. For example, the franchisor may accept the terms if the franchisor needs to sell its franchise license to collect a substantial amount of franchise fees or to place the franchisee's business in a particular location for the first time. In these cases, the franchisee may induce the incorporation of exclusivity clauses in a franchise contract. In the context of encroachment, the franchisee may negotiate for a 'no shop' provision, granting the franchisee a protected territory and preventing the franchisor from opening its own outlet or licensing other franchisees to open a franchised store within the protected area. Furthermore, a franchisee may negotiate the terms conferring the franchisee the right to refuse the placement of new franchised units. In this case, the franchisor may establish a new franchised store on the condition that the franchisee does not exercise the right within a specified period. Alternatively, a franchisee may bargain for the terms that entitle the franchisee to receive a share of revenue generated from the franchisor's sales in the franchisee's exclusive location.⁹¹

However, regulating franchisor encroachment by a franchise agreement is not pragmatically feasible. In reality, the bargaining power between a franchisor and a franchisee is ordinarily asymmetric. A franchisor is usually superior to a franchisee in terms of economic power, making the franchisee's bargaining power very weak in making a franchise contract. The Franchise Council of Australia claims that many small franchisees are disadvantaged by the practices of sophisticated franchisors in drafting agreements.⁹² A superior franchisor typically proposes a franchise contract with standardized terms to a prospective franchisee to make it easier for the franchisor to administer the entire franchise system. In this case, an inferior franchisee will conclude a franchise contract on the basis of take-it-or-leave-it, with little chance

91 This arrangement can be observed in *Newpaper, LLC v Party City Corp.* See *Newpaper* (n 83) 2.

92 Franchise Council of Australia, *Submission by the Franchise Council of Australia to the Treasury Department in relation to the possible extension of unfair contract term protections to small business* (2014) at 3-4, <<https://bit.ly/30juDVq>> accessed 17 February 2023.

for the franchisee to modify the terms.⁹³ In many cases, the standardized terms are not favorable to a franchisee. For example, a franchise contract typically includes no exclusivity, meaning a franchisor does not grant a franchisee an exclusive area, protecting the franchisee against the franchisor's encroachment. In the USA, for example, it is claimed that the number of franchise contracts designating an exclusive territory has declined.⁹⁴ Without exclusivity assigned to the franchisee, it is contractually possible for the franchisor to engage in either traditional or non-traditional encroaching conduct to the franchisee's detriment.

It should be mentioned that a franchisor may include an exclusivity clause in a franchise contract because of economic incentives. Some practitioners claim that the incorporation of an exclusive territory clause into a franchise contract would help startups or small franchisors increase the volume of sales of their franchise business.⁹⁵ The sales of a franchise license could be generated if potential franchisees feel confident about a grant of a protected area.⁹⁶ In this case, some franchisors may use a franchise agreement with an exclusivity provision to attract potential franchisees to join a franchise system. However, I think that this situation is unlikely to arise as many franchisors have established their franchise brand in the market. In this respect, it is the franchisor's brand, not the exclusivity, that entices prospective franchisees to purchase a franchise license. Furthermore, some franchisors do not provide their franchisees with territorial exclusivity because the franchisee's exclusivity is not so imperative in distributing products or services in some industries, such as the hospitality industry. Thus, there is always the possibility that a franchisee concludes a franchise agreement without any territorial protection clause.

(3.4) *Judicial intervention*

In theory, judicial intervention would protect weaker franchisees against the franchisor's opportunistic conduct. In some legal systems, the requirement of good faith is established as a normative standard of conduct. In this respect, courts may employ the principle of good faith to imply terms into a franchise agreement controlling a franchisor's exploitative behaviors. A practical example

93 John Sotos, 'Recent Trends in Franchise Relationship Laws' (2012) 10(1) *International Journal of Franchising Law* 3, 4. Despite this, a franchisee may exchange some considerations to acquire the franchisor's agreement to the protective terms. For instance, the franchisee may agree to pay exclusivity fees to keep the exclusivity clauses alive for the entire life of a franchise contract. The fees may be included in the up-front fees that the franchisee must pay for a franchise license or included in the royalties that must be paid periodically during the term of the agreement.

94 Emerson (n 36) 234.

95 Lauer and Weinberg (n 42) 18-19.

96 Charles Modell, 'Drafting Exclusive Territory Provisions in Franchise Agreements' (1996) 16(2) *Franchise Law Journal* 74, 74.

can be seen in the US cases *Scheck I* and *Scheck II*, where courts implied the covenant of good faith and fair dealing to prevent the franchisor from establishing the new franchised store that would harm the existing franchisee's legitimate interests.⁹⁷

Nevertheless, a franchisee may encounter some constraints when utilizing this approach. In some jurisdictions, the cost of litigation is notoriously expensive. Furthermore, legal proceedings are time-consuming. These features of civil justice would discourage an aggrieved franchisee from suing a franchisor in court. Besides, a franchisor typically rules out the possibility of intervention by courts. A franchisor may explicitly reserve the right to expand its marketing to a franchisor's location. If a franchise contract expressly provides so, courts in some jurisdictions may be reluctant to intervene in a franchise relationship. For example, in the USA, the Illinois court in *Patel v Dunkin' Donuts of America* held that the franchisee could not bar the franchisor from opening the new store within one mile of the franchisee's outlet because the franchise contract explicitly reserved the franchisor's right to do so.⁹⁸ In addition, a franchisor may prohibit a franchisee from engaging in class actions against the franchisor. In this case, franchisees in a particular franchise system cannot collectively sue the franchisor if the franchisor's encroachment has been done system-wide.

– *Regulation of franchisor encroachment by franchise relationship legislation*

(1) *Similarity*

A general similarity among the DCFR, the USA, and Australia is that franchise relationship law rules do not explicitly regulate franchisor encroachment. Under the DCFR, no default rule of franchise law in Part E of Book IV supplies the franchisor's obligation not to encroach upon the franchisee's marketing area. Likewise, no federal franchise legislation has been enacted in the USA to regulate the encroachment matter. The same conclusion goes for a majority of the US states, except for the five relationship states, Hawaii, Indiana, Iowa, Minnesota, and Washington, which regulate franchisor encroachment through their franchise relationship law. In Australia, it could be said without hesitation that the Franchising Code of Conduct does not directly control the encroachment by a franchisor, although the rule on the obligation to act in good faith could be employed to address franchisor encroachment to some extent.

(2) *Difference*

A marked difference can be detected. As mentioned in the preceding paragraph, five American states, namely, Hawaii, Indiana, Iowa, Minnesota, and Washington, have franchise relationship law rules specifically regulating the

⁹⁷ See subsection 4.2.3.4.

⁹⁸ *Patel v Dunkin' Donuts of America, Inc*, 496 NE 2d 1159, 1160, 100 Ill Dec 94, 95, 146 Ill App3d (Ill App 1 Dist, 1986) 236.

franchisor's encroaching conduct.⁹⁹ In this case, a question is: what is the idea underlying this regulatory approach? In answering this question, Iowa will be taken as an illustration because it was the first state that regulates franchisor encroachment through franchise relationship law, which is often taken to show how anti-encroachment rules are legislated.¹⁰⁰ From a historical viewpoint, by the start of the 1990s, the Franchise Regulation Study Committee was set up to examine the need for the regulation of franchise businesses in the state and propose action items. In examining the need to regulate franchise businesses, the Committee testified some individuals, including franchisees, who thought the franchisor's encroachment was a great concern. Therefore, in the Final Report, the Committee recommended that Iowa enacted the legislation to limit the franchisor's ability to compete with an established franchisee offering the same goods or services.¹⁰¹ Due to this particular recommendation, the state legislature first enacted the 1992 Act, which contained the anti-encroachment rule preventing franchisors from encroaching upon their franchisees' territory.

(3) *Discussion*

From the comparison, franchise relationship law rarely addresses the issue of franchisor encroachment. The absence of a franchise regulation leaves a weaker franchisee unprotected from a franchisor's encroaching conduct. Thus, I suggest that the statutory law regulates the encroachment issue to some extent. This suggestion is based on the premise that rules of franchise-specific law, particularly franchise relationship law, can provide extra-contractual protection to a weaker franchisee. According to Sotos, franchise relationship law will provide minimum standards for franchise relationships and control certain contractual terms in a franchise agreement. Most importantly, the law may insert the duty of good faith with a particular intention to address franchisors' bad faith behaviors.¹⁰² In this sense, the regulation by franchise relationship law would be a key actor in a race to protect the franchisee against franchisor encroaching conduct, which may unfairly jeopardize the franchisee's interest in a particular marketing location. Because of the perceived benefits of statutory regulation, I propose that comprehensive franchise law lays down the following rule to regulate franchisor encroachment in a franchise relationship.

'The franchisor may (a) operate or authorize other franchisees to operate a franchised business within a reasonable area of the existing franchisee's business, or (b) engage in any conduct that triggers or is likely to trigger competition between the

99 See subsection 4.2.3.2.

100 Emerson (n 36) 234 and 258.

101 The digital copy of the Report can be accessed at <<https://bit.ly/2Jm9iFG>>.

102 Sotos (n 93) 4-5.

franchisor and the franchisee within a reasonable area of the existing franchisee's business provided that the franchisor has offered the existing franchisee the right to operate the new outlet within a reasonable area of the franchisee's business or the franchisor has offered reasonable compensation or other forms of consideration to offset, in whole or in part, lost profits to be caused by the conduct in (a) or (b).'

(3.1) *Aims of the proposed anti-encroachment rule*

The underlying idea behind the proposition of this anti-encroachment rule is that a franchisee's marketing territory should be protected against all kinds of intra-brand competition, including geographical and online encroachment, that could lead to the franchisee's business disaster. According to Benoliel, a new competing unit might attract customers and experienced personnel from the incumbent store. This situation would result in a considerable diminution in profits and eventually lead to the business failure of the existing outlet.¹⁰³ As discussed earlier, many franchisees can hardly bargain for territorial exclusivity because the franchisees are usually in an inferior position during the negotiating process. Thus, this legal protection would enable a weaker franchisee to recoup its investment in the franchised business operation by shielding the franchisee from the franchisor's practices of undue competition.

As can be seen, this proposed rule constitutes the franchisor's obligation regarding encroachment upon the franchisee's franchised business. The franchisor must remedy the franchisee in certain forms before engaging in encroaching practices. This requirement is obligatory as the franchisor's failure to perform the obligation can be enforced in civil lawsuits. In other words, an aggrieved franchisee can go to court to seek monetary compensation or different kinds of private law relief for the franchisor's contravention of the rule.

Furthermore, this model rule is intended to be mandatory. This mandatory character means the parties to a franchise contract cannot agree to exclude the application of the rule governing franchisor encroachment or mitigate the effect of the rule. In my view, this mandatory aspect would redress the disparity in bargaining power between a franchisor and a franchisee. Under the compulsory rule, a franchisor, particularly a sophisticated franchisor, will not be able to decide all the matters in a franchise relationship to the detriment of a weaker franchisee. For example, some practitioners may advise a franchisor not to grant a franchisee an exclusive territory or reserve the right to engage in certain encroaching conduct to avoid the franchisee's encroachment claim.¹⁰⁴ In this context, the franchisee needs not to negotiate for the protection of a marketing area in a franchise contract since the rule will mandate the franchisor to remedy the franchisee before engaging in encroaching practices.

¹⁰³ Benoliel (n 23) 215-20.

¹⁰⁴ Emily I Bridges, 'Keep Off My (Virtual) Lawn: Encroachment in the Age of the Internet' (2017) 36 Franchise Law Journal 415, 425-27.

(3.2) Regulation of the franchisor's encroaching conduct

(3.2.1) Forms of the franchisor's encroaching conduct

This proposed rule regulates the franchisor's engaging in both traditional and non-traditional practices of encroachment that are likely to compete with the existing franchisee's business. First, the model rule intends to regulate the franchisor's geographic encroachment, such as establishing a new bricks and mortar franchise outlet or a new mobile franchise store that causes intra-brand competition. Besides, this provision aims to regulate the placement of a new franchise unit, irrespective of whether the franchisor or the other new franchisee operates that unit. Second, this model rule also intends to regulate the franchisor's non-geographical encroachment. As can be seen, the expression 'engaging in any conduct' is an umbrella term that captures the franchisor's conduct that, from a marketing standpoint, triggers or would trigger internal competition between the franchisor and the franchisee, including distributing goods or services through alternative distribution channels.

In particular, this term aims to cover the conduct of making direct and online sales that competes with the franchisee in the protected area. The reason is that the practice of non-traditional encroachment by internet sales could contribute to a decline in the profitability of an incumbent franchisee. In the contemporary business context, digital marketing is said to be the fastest-growing form of marketing. Due to the pervasiveness of the internet, businesses tend to use digital platforms, such as websites, emails, social media platforms, or mobile applications, to market their products or services. This online marketing practice is increasingly common at both national and international levels as it is claimed to be a low-cost, efficient, speedy alternative for approaching customers in the market.¹⁰⁵

Undoubtedly, the use of online sales can be utilized in the franchising context.¹⁰⁶ Some franchisors may launch their website or other online marketing platforms to engage customers and facilitate sales of franchise products.¹⁰⁷ These transactional sites or platforms may inevitably cause virtual encroachment.¹⁰⁸ This e-encroachment may trigger intra-brand competition between the franchisor and its franchisees since a group of consumers in the franchisees' marketing area can be solicited by the franchisor's online platforms. Theoretically speaking, this inner competition would cannibalize the franchisees' sales, thereby causing conflict between the franchisor and the franchisee. This theory can be affirmed by some evidence, showing that the conflict over internet sales

105 Gary Armstrong, Philip Kotler, and Marc Oliver Opresnik, *Marketing: An Introduction* (7th global edn, Pearson Education Limited 2023) 469.

106 Courtenay Atwell and Jenny Buchan, 'The Franchise Fulcrum: The Legal System's Contributions to Research about Power and Control in Business Format Franchising' (2014) 21 *Journal of Marketing Channels* 180, 189.

107 Armstrong, Kotler, and Opresnik (n 105) 475-76.

108 Perrigot, Basset and Cliquet (n 90) 279.

has been materialized, particularly in the case where a franchisor employs this online strategy with an exploitative purpose.¹⁰⁹ Thus, my view is that the comprehensive franchise law rule should not only address the franchisor's traditional encroachment. The law rule should also address the franchisor's non-traditional encroachment, such as online sales, because this practice would allow an opportunistic franchisor to penetrate its franchisees' marketing area, thereby causing financial damage to the franchisees.

(3.2.2) *The franchisee's protected area*

This proposed rule aims to regulate the franchisor's traditional and non-traditional encroachment to be conducted in a reasonable area of an existing franchisee. Incorporating the reasonableness element in the model rule is purposeful because it is not feasible for the language of a black-letter rule to specify the scope of the franchisee's protected territory.¹¹⁰ In some cases, an individual franchisee may need a larger protected territory than other fellow franchisees within the same franchise network. Additionally, some marketing strategies may cause the business area to change over time. For instance, a mobile franchise unit is a customer-based business; hence, the unit usually is not fixed to any location. Instead, the franchise truck unit will relocate from place to place to approach its potential customers. This mobile nature of a franchise business shows that demarcating the protected area may vary from case to case. Thus, when adjudicating a dispute, judges need to decide if the franchisor will encroach on the existing franchisee's reasonable location.

However, this proposed rule does not intend for courts to describe the scope of the franchisee's protected location in a franchise contract because the task of demarcating a protected marketing area would unduly spend public resources and be laborious for the judges. In many cases, the franchisee's marketing area is allocated; a franchisor may consider several factors, such

109 For instance, in the US case *Emporium Drug Mart v Drug Emporium*, the franchisees brought arbitration proceedings against the franchisor, claiming that the franchisor engaged in encroaching conduct. The factual circumstances on which the franchisees' claim was based is that the franchisor's subsidiary operated a drugstore website that made products available to customers within the exclusive territory of the franchisees. In this case, the arbitrators considered the unique circumstances of the case and determined that the use of the website was likely to confuse customers. Particularly, the arbitrators found that there was an attempt of the franchisor and its subsidiary to build market share using the site. In other words, it was obvious that the franchisor and its subsidiary aimed to increase the sales volume using the online drugstore at the expense of the franchisees. Although the franchise agreement under consideration did not address the use of e-commerce, the arbitration panel enjoined the franchisor from selling products via the website in the exclusive territory of the franchisees. See Summary reported at Bus. Franchise Guide (CCH) ¶11,966 (September 2, 2000).

110 This practice is not uncommon from a regulatory viewpoint. Taking Iowa's 2000 Act as an example, paragraph (a) of section 537A.10(6) does not provide any specific parameters for defining the existing franchisee's protected area. Instead, the law uses a vague criterion, namely, 'unreasonable proximity'.

as administrative territories, population, and foot traffic numbers, to designate the franchisee's exclusive area in a franchise agreement. For example, the franchisor may provide that the franchisee exclusively operates a franchised business in Molenwijk, which is in Katwijk aan Zee, near Leiden. However, this proposed rule is going to say that the franchisee's designated marketing area is not decisive. Theoretically, the designated location may not be reasonable and proper to protect the franchisee's interests in operating a franchised business. The franchisor may open a new franchised outlet in a particular area outside Molenwijk, but it is located just across the street in Molenwijk. Thus, the rule aims to provide judges with the power to review if this particular spot is the area where the franchisee should reasonably be protected. If so, the franchisor will be required to meet the preconditions explained below.

(3.3) *Preconditions for encroaching upon the franchisee's protected area*

It should be mentioned that this proposed rule does not intend to prohibit the franchisor's traditional and non-traditional encroachment in the first place. Instead, the franchisor's encroaching practices is allowed provided that the franchisor has satisfied either of the following two requirements.¹¹¹

Firstly, the franchisor must have provided the existing franchisee with the right of first offer; it must have offered the franchisee to operate a new franchised outlet in a reasonable area of the franchisee's business before trying to sell its franchise to other franchisees or open its own franchise store. This requirement would permit the franchisor to expand franchised stores geographically. In the example of Molenwijk, the franchisor must give the franchisee operating a franchised business in Molenwijk before opening a new franchised store in an intended area. It should be noted that the rule does not require the franchisee to accept the offer. Thus, the franchisor may open a new franchised store even though the franchisee refuses the franchisor's first offer.

Secondly, the franchisor must have offered the franchisee reasonable compensation in money or other forms of remedy to offset the franchisee's lost profit that could be caused by the franchisor's encroaching conduct. In my view, the franchisee's potential lost profit means the profit that the franchisee would have gained if the franchisor's encroaching had not been done. This requirement is introduced to suit the franchisor's engaging in non-traditional encroachment. Suppose the franchisor decides to launch a transactional website that enables customers to order the products to be delivered within the existing franchisee's protected location. In that case, the franchisor has to offer the franchisee reasonable compensation to redress the franchisee's potential loss caused by internet encroachment. Alternatively, the franchisor may offer to share the franchisee the benefits from online sales. For

111 In adopting this proposed provision, legal systems should ascertain that this anti-encroachment rule conforms to competition law rules applying to agreements in restraint of trade or commerce.

example, the franchisor and the franchisee may agree that the franchisor is required to share a portion of the benefits with the franchisee if the goods are sold and delivered to customers in the franchisee's protected business area.¹¹²

The reason behind the proposed requirements is twofold.

First, this rule intends to allow a franchisor to change its marketing strategies more flexibly. In practice, some business strategies may benefit all the franchisees in a franchise system. For example, raising the density of franchise units in a specific territory may increase the visibility and customer awareness of a particular brand.¹¹³ In this respect, the intensification of the brand's perceptibility by customers would benefit all franchisees in the long run. In this case, the franchisor may open a new franchised outlet in a reasonable area of the existing franchisee by satisfying the requirements imposed by the rule.

Second, this rule intends to minimize an existing franchisee's undue financial loss caused by the franchisor's encroaching conduct. In general, a franchisee usually expects to operate a franchised business without fear of inner competition that would reduce profitability. Thus, the rule should also permit the franchisee to protect itself from exposing to any loss or damage to the franchisee's benefits. For example, suppose a franchisor decides to open a new franchised store near an existing franchisee's business to meet customers' demand in that area. In this case, the franchisor has to offer the franchisee the right to operate the new unit before licensing a franchise to other franchisees. This offer would allow the existing franchisee to decide to protect its lucrative marketing area.

4.2.5.3 Conclusions

– Concluding remarks

The descriptive and comparative examination of the franchise legal frameworks of the DCFR, the USA, and Australia show that the regulation of franchisor encroachment can take the forms of contractual and statutory regulations. First, a franchise contract may incorporate an exclusivity provision that explicitly prevents a franchisor from encroaching upon a franchisee's business operation. In the absence of such a provision, courts may employ the principle of good faith and fair dealing to imply terms into a franchise agreement, protecting a franchisee against the franchisor's cannibalization. These legal mechanisms are theoretically feasible under all the selected legal systems. Second, some American states enact franchise relationship laws containing anti-encroachment or anti-unfair competition rules. These rules are mandatory and prohibit a

112 This example arrangement is derived from the US court decision in *Newspaper v Party City Corp.* See *Newspaper* (n 83) 4.

113 Blair and Lafontaine (n 23) 204.

franchisor from geographically encroaching upon a franchisee's marketing area.

– *Key recommendations*

(1) *Regulation of franchisor's traditional and non-traditional encroachment*

Comprehensive franchise law should contain a mandatory, anti-encroachment rule that regulates the franchisor's encroachment upon the franchisee's business. The introduction of the regulatory provision is based on the premise that the regulation of franchisor encroachment by the express and implied terms of a franchise contract is not efficient in protecting a weaker franchisee. Typically, a superior franchisor can draft a franchise contract to permit the franchisor to engage in traditional and non-traditional encroaching practices that would harm the weaker franchisee's legitimate interests in operating a franchised business.

(2) *Requirements for engaging in regulated conduct*

An anti-encroachment rule should regulate the franchisor's traditional and non-traditional encroachment in the way that these encroaching practices are allowed on the condition that the franchisor: (1) has offered the franchisee the right to operate a new franchise outlet in a reasonable area of the franchisee's business or (2) has offered reasonable compensation or other remedial forms to offset the franchisee's potential lost profits caused by the franchisor's encroachment.

4.3 DUTY TO ASSIST

4.3.1 Introduction

In many cases, a franchisee is an inexperienced business person who purchases a franchise, believing that a franchisor will provide the franchisee with assistance and support in opening and operating a first-in-lifetime franchised business. Frequently, franchisors offer franchisees several forms of support that are an interesting feature of franchise businesses.¹¹⁴ As pointed out in the introduction, some franchisors may not render franchisees with appropriate and necessary assistance. This section will examine how the franchise legal framework of the DCFR, the USA, and Australia requires a franchisor to assist a franchisee in an initial and ongoing phase of a franchise relationship in

114 Paul Rubin, 'The Theory of the Firm and the Structure of the Franchise Contract' (1978) 21(1) *Journal of Law and Economics* 223, 230; Stuart Price, 'Performance of Fast-food Franchises in Britain' (1993) 5(3) *International Journal of Contemporary Hospitality Management* 10, 11.

sections 4.3.2, 4.3.3, and 4.3.4, respectively. Section 4.3.5 will compare, contrast, and discuss the regulatory approaches of the chosen legal systems to develop guidelines for formulating the rules regulating the franchisor's duty to assist under comprehensive franchise law.

4.3.2 The Draft Common Frame of Reference (DCFR)

4.3.2.1 Introduction

A franchise contract will primarily regulate the franchisor's duty to assist. In some cases, a franchisor and a franchisee may agree on express terms requiring the franchisor to provide specific forms of assistance to the franchisee in the opening and operation of a franchised business. In the absence of express terms, the DCFR allows the franchisor's assistance obligation to be generated by legal rules. In Part E of Book IV, IV.E. – 4:203 constitutes the franchisor's duty to assist a franchisee if the parties do not agree otherwise. This section will examine the construction of the franchisor's assistance obligation by the express terms of a franchise contract and the default rules of the DCFR in subsections 4.3.2.2 and 4.3.2.3, respectively. Subsection 4.3.2.4. will conclude on the main characteristics of the franchisor's assistance duty under the DCFR.

4.3.2.2 Regulation by the express terms of a franchise contract

A franchise contract's terms will generally govern the franchisor's duty to assist. As said earlier in this chapter, the DCFR recognizes the contractual freedom where the parties are, subject to some applicable mandatory rules, free to determine the contents of a contract.¹¹⁵ Thus, a franchisor and a franchisee are free to establish the terms requiring the franchisor to provide some assistance to the franchisee in a franchised business operation. In practice, some European self-regulatory organizations play an essential role in encouraging the establishment of this obligation. For example, in the European Franchise Federation (EFF)'s Code of Ethics for franchising, clause 2.2(iv) states that the franchisor shall provide the individual franchisee with initial training and continuing commercial and/or technical assistance during the entire life of the agreement.¹¹⁶

In drafting a franchise contract, the ICC's Model International Franchising Contract (Model Contract) points out some of the franchisor's obligations of assistance. In the Model Contract, the franchisor's obligations to assist the franchisee include providing initial training to the franchisee.¹¹⁷ However,

¹¹⁵ The DCFR, II.-1:102(1).

¹¹⁶ The English text of the Code of Ethics can be accessed at <<https://bit.ly/2W2xeps>>.

¹¹⁷ The Model Contract, art.13.1.

the drafting group of the Model Contract leaves a question of whether training fees should be paid for the parties to decide.¹¹⁸ Besides, the Model Contract requires the franchisor to provide adequate assistance in the pre-opening stage.¹¹⁹ According to the explanation, the franchisor may offer support in connection with an initial advertising campaign, shop design, interior design, number of employees, and stock requirements.¹²⁰ It should be noted that the Model contract does not touch upon an ongoing assistance issue. In this case, the franchisor's ongoing duty may be generated by the rule described in the following subsection.

4.3.2.3 Regulation by the terms generated by the rule of the DCFR

In the absence of the express terms, IV.E. – 4:203 will establish the franchisor's obligation of assistance. The DCFR's provision deals explicitly with this particular obligation because the drafters of the DCFR contemplate that this franchisor's duty is vital for a franchisee in the sense that the franchisee should have clear guidance in operating a franchised business. In this respect, the drafters of the DCFR argue that the franchisor is in the best position to provide the franchisee with such guidance.¹²¹ Although the drafters do not give the reason behind the argument, it is obvious that the franchisor should guide its franchisees because the franchisor knows its franchise system well. Besides, the drafters of the DCFR provide that the franchisor can guarantee the uniform conduct of its franchisees by actively assisting them in operating the franchised businesses.¹²² Thus, from the drafters' viewpoint, the franchisor must be required to assist the franchisee in the operation of a franchised business.

According to IV.E. – 4:203, the franchisor's duty to assist can be divided into two cases. That is, the franchisor is required to provide the franchisee with general assistance and specific assistance. These aspects of the franchisor's duty to assist will be explored in the following two italicized headings.

– *General assistance*

IV.E. – 4:203(1) obligates a franchisor to provide a franchisee with assistance in the form of training courses, guidance, and advice. According to the commentaries to this provision, this general assistance can be categorized into initial and ongoing assistance. The franchisor may also be required to assist the franchisee in commencing the franchised business operation. The franchisor

118 International Chamber of Commerce, *ICC Model International Franchising Contract* (ICC Publications 2011) 29.

119 The Model Contract, art.14.1.

120 International Chamber of Commerce (n 118) 30.

121 Bar and Clive (n 6) 2401.

122 Ibid 2401.

may be required to solve some operational problems occurring in the franchise relationship.¹²³ In both cases, IV.E. – 4:203(1) provides that the franchisor's assistance must be rendered without additional costs. The drafters of the DCFR explain that the franchisor cannot ask for additional costs for the necessary assistance under IV.E. – 4:203(1) because the franchisor is deemed to include the costs in the upfront payment that the franchisee is obliged to make to the franchisor.¹²⁴ From a practical perspective, the franchisor may add the costs of providing support in the payment of franchise fees. However, the costs added may vary from case to case because franchisees may need different amounts of the franchisor's assistance.

– *Specific assistance*

Paragraph (2) of IV.E. – 4:203 obligates a franchisor to provide specific assistance; that is to say, the franchisor is required to be responsive to a franchisee's reasonable request for further assistance. As can be seen, this assistance obligation is conditional upon a specific, reasonable request by a franchisee.¹²⁵ In other words, the franchisor has to assist the franchisee insofar as the franchisee has made a reasonable demand for the franchisor's specific support.¹²⁶ Nevertheless, IV.E. – 4:203(2) does not exemplify forms of special support; hence, it is of a franchisee's choice. In any case, the franchisee has to cover extra costs of assisting insofar as the cost is reasonable.¹²⁷

4.3.2.4 Conclusions

Under the DCFR, the franchisor's duty to assist will be regulated by a franchise contract's terms. The terms governing the obligation can be generated by the parties' agreement and the franchise rule of the DCFR. In many cases, a franchisor and a franchisee may agree on the terms that the franchisor is required to provide the franchisee with some assistance in connection with a franchised business operation. As can be seen from the Model Contract's clauses, a franchisor may agree to give a franchisee initial training, and assistance in the pre-opening phase. Notably, the DCFR supplies a default provision establish-

¹²³ Ibid 2400.

¹²⁴ Ibid 2400-401.

¹²⁵ The drafters of the DCFR refer to the criteria set out by I.-1:104 when it comes to assessing if the franchisee's request for specific assistance is reasonable. In this case, the request must be ascertained objectively on a case-by-case basis. However, the drafters exemplify that the franchisee's request would seem reasonable if it aims to receive specific guidance to guarantee the adequate operation of the franchised business. See Bar and Clive (n 6) 2402.

¹²⁶ Unlike the case of general assistance, IV.E. – 4:203(2) provides that a franchisor can ask for the payment of additional costs made by a requesting franchisee for rendering individually tailored support. Though, this article permits the franchisee to ask for reasonable costs.

¹²⁷ Bar and Clive (n 6) 2402.

ing the franchisor's assistance obligation in the absence of the expressly agreed terms. In IV.E. – 4:203, a franchisor is obliged to provide a franchisee with general assistance in the form of training courses, guidance, and advice. Besides, a franchisor is required to be responsive to a franchisee's reasonable request for specific assistance.

4.3.3 The United States of America (USA)

4.3.3.1 Introduction

Federal and state franchise-specific statutes do not regulate the franchisor's duty to assist. In other words, a franchisor is not statutorily required to provide a franchisee with support in the opening and operation of a franchised business. However, the franchisor's obligation may be constructed under the realm of contract law. In many cases, a franchisor and a franchisee expressly agree on the terms under a franchise contract that creates the franchisor's duty to assist the franchisee. In this case, the franchisor's duty to assist is contractual in character. This section will examine the extent to which the franchisor's contractual duty of assistance is constructed by the terms of a franchise contract in subsection 4.3.3.2. Subsection 4.3.3.3 will summarize the characteristics of the franchisor's obligation to assist in the US legal system.

4.3.3.2 Regulation by the express terms of a franchise contract

It is common in practice that a franchise contract incorporates the terms requiring a franchisor to provide a franchisee with some assistance and support.¹²⁸ In the USA, some trade associations offer recommendations that more or less influence this commercial reality.¹²⁹ For example, the American Association of Franchisees and Dealers (AAFD) introduces the Franchisee Bill of Rights, which expressly recognizes the franchisee's right to initial and ongoing training and support.¹³⁰ In implementing the Bill of Rights, the AAFD introduces the Fair Franchising Standards, containing the standards that require a franchisee to perform the training duty and the duty to give instructions. Under the Fair Franchising Standards, standard 8.8 provides that the franchisor has to provide the franchisee with initial and ongoing training in all relevant aspects of the franchise business.¹³¹

128 See eg *7-Eleven, Inc v McEvoy*, 300 F Supp 2d 352 (D Md, 2004) 361; *Strategic Intent, LLC v Strangford Lough Brewing Co Ltd*, 2011 WL 1810474, (ED Wash, 2011) 5.

129 Gregory Klass, *Contract Law in the United States* (2nd edn, Kluwer Law International 2012) 132.

130 The Franchisee Bill of Rights can be accessed at <<https://bit.ly/3nVoLA6>>.

131 The AAFD's Fair Franchising Standards can be downloaded at <<https://bit.ly/3xUDHAA>>.

Drafting the provision establishing the franchisor's duty to assist may differ from business to business. In practice, some organizations may offer model provisions of a franchise agreement to facilitate this contract drafting. For example, the American Bar Association (ABA) publishes the Annotated Franchise Agreement as a guide to drafting a franchise agreement's provisions.¹³² In the ABA's publication, section VII of Chapter 3 elaborates on the provisions concerning training and operating assistance. According to this section, a franchise agreement may require a franchisor to provide a franchisee with three forms of assistance – initial training, ongoing training, and operating assistance. These three forms are enumerated by the sample clauses provided in sections VII.A, B, and C, respectively. Summaries to the franchisor's assistance required by the model provisions are as follows.

– *Initial training*

First of all, a franchisor may be required to arrange an initial training course for a franchisee. The sample clause in section VII.A provides that the franchisor shall provide the franchisee with a training course before opening the franchised business.¹³³ In offering the training, the franchisor is free to decide the program's scope, content, location, and format. Concerning the objectives, this training program aims primarily to help the franchisee learn to operate the business in a uniform fashion. The program also aims at ensuring that the franchise system's standards are maintained. Therefore, the provision of the initial training is regarded as essential that a franchise agreement must include these terms to ensure that a franchisee receives the training before launching a franchised outlet.¹³⁴

– *Ongoing training*

Secondly, a franchisor may be required to arrange an ongoing training program. The sample provision in section VII.B suggests that the franchisor may organize and require the franchisee to participate in the training program to maintain the franchise system and brand's standards.¹³⁵ This training course ordinarily focuses on training the franchisee about how to generally operate a franchised business or other subject matters that are designed to assist the franchisee. According to the authors of the ABA's book, organizing the ongoing training program may be done by a franchisor in various ways. For example,

132 Nina Greene, Dawn Newton, and Kerry Olson (eds), *The Annotated Franchise Agreement* (2nd edn, American Bar Association 2021).

133 Harris Chernow and Beata Krakus, 'Training, Site Selection, Construction, and Opening' in Nina Greene, Dawn Newton, and Kerry Olson (eds), *The Annotated Franchise Agreement* (2nd edn, American Bar Association 2021) 57.

134 *Ibid* 59.

135 *Ibid* 62.

the franchisor may hold an annual convention or a meeting of franchisees through a webinar. These assemblies would enable the franchisor to provide additional assistance and instant feedback to franchisees without a need to arrange a personal training program for individual franchisees.¹³⁶

– *Operating assistance*

Thirdly, a franchisor may be required to provide additional operating assistance during a franchise relationship. However, the sample clause in section VII.C suggests that the provision of this form of assistance may be discretionary. A franchise agreement may provide that the franchisor can, in its sole discretion, arrange additional training programs or offer continuing advisory assistance in the operation of the franchised business and advice and written materials concerning techniques of managing and operating the franchised business.¹³⁷ In this case, the franchisor's assistance would not be enforceable as it is not obligatory.

4.3.3.3 Conclusions

The USA takes a contractual approach to regulating the franchisor's duty to assist. The franchisor's obligation is regulated by the expressly agreed terms of a franchise contract. In other words, the franchise agreement will provide that the franchisor is required to assist or support the franchisee in the operation of a franchised business. Despite the fact that forms of the franchisor's assistance vary from agreement to agreement, the franchisor may agree to assist its franchisees in two aspects. As exemplified in this section, a franchisor may agree to provide a franchisee with initial training and ongoing training programs to help the franchisee operate a franchised business effectively. A franchisor may also, from time to time, offer operational assistance, which is at the franchisor's discretion.

4.3.4 Australia

4.3.4.1 Introduction

The franchisor's duty to assist a franchisee is not statutorily regulated in Australia. Neither the Franchising Code of Conduct nor the Competition and Consumer Act 2010 devote provisions to regulating the franchisor's assistance duty. In practice, a franchise agreement will play a governing role in this respect. Under a franchise agreement, the franchisor's obligation to assist a

¹³⁶ Ibid 63-65.

¹³⁷ Ibid 68.

franchisee can be constituted by expressly agreed terms.¹³⁸ This section devotes subsection 4.3.4.2 to examining the construction of the franchisor's duty to assist by the express terms of a franchise contract. Subsection 4.3.4.3 will conclude on the characteristics of the franchisor's duty to assist in the Australian legal system.

4.3.4.2 Regulation by the express terms of a franchise contract

As mentioned in the introduction, a franchise agreement may establish the franchisor's duty to assist a franchisee. In this regard, some trade organizations, such as the Franchise Council of Australia (FCA), may encourage franchisor members to provide franchisees with assistance and support. According to the FCA Member Standards, a franchisor is urged to have training and support processes as applicable to the franchise system to help franchisees improve their abilities to conduct their franchises.¹³⁹ Because of this required standard, some franchise businesses listed on the FCA's directory website are committing to providing franchisees with training and support. For example, Poolwerx, a service franchise business in Australia and New Zealand, advertises on its website that the company offers a variety of training programs, as well as ongoing support to help its franchisees succeed in day-to-day business operations.¹⁴⁰

In a franchise contract, the expressly agreed terms may regulate specific forms of franchisor's assistance rendered to a franchisee. For example, in *Masterclass Enterprises v Bedshed Franchisors (WA)*, the franchise contract terms illustrated that the franchisor agreed to provide the franchisee with a training program on the operation of a franchised store before the specific commencement date. Furthermore, the franchisor agreed to give the franchisee advice and assistance from time to time as the franchisor considers it is reasonably required. The franchisor committed to paying regular visits and offering advice concerning operational matters, such as the training of staff, sales methods and techniques, new products, and general operating procedures for the franchised store. The franchisor also agreed to provide written information upon the franchisee's reasonable request in connection with the franchised business.¹⁴¹

138 Sotos (n 93) 10.

139 The FCA Member Standards can be accessed at <<https://bit.ly/3ADUYiZ>>.

140 Poolwerx, 'TRAINING AND SUPPORT' <<https://bit.ly/2SgxQEd>> accessed 22 January 2022.

141 *Masterclass Enterprises Pty Ltd v Bedshed Franchisors (WA) Pty Ltd* [2008] WASC 67 BC200 803343 [11].

4.3.4.3 Conclusions

Australia takes a contractual approach to regulating the franchisor's duty to assist. Since no statutory law regulates the franchisor's obligation, a franchise agreement, as well as operational manuals, would be primary instruments that create the franchisor's duty to assist. Under the terms of a franchise contract, a franchisor may commit to supporting a franchisee in a franchised business operation in several manners. The practical example shows that a franchisor may agree to establish training programs for franchisees. A franchisee may also agree to provide operational advice and pay regular visits during a franchise relationship. The terms of a franchise contract governing the franchisor's assistance obligation may vary from business to business.

4.3.5 Comparative analysis

4.3.5.1 Introduction

From the descriptive examination, the regulation of the franchisor's assistance obligation under the franchise legal framework of the DCFR, the USA, and Australia is principally contractual. Under the selected legal systems, the terms of a franchise contract will designate if a franchisor is obliged to provide a franchisee with forms of assistance. This section will compare, contrast, and discuss the selected legal systems' approach in constituting the franchisor's contractual duty to assist in subsection 4.3.5.2. Subsection 4.3.5.3 will conclude on the comparison and put forward key recommendations concerning the establishment of the franchisor's duty to assist under comprehensive franchise law.

4.3.5.2 Comparison and analysis

– Similarity

As mentioned above, the DCFR, the USA, and Australia are similar in that a franchise agreement is a primary instrument that generates the franchisor's duty of assistance.¹⁴² Under the freedom of contract principle recognized under the selected legal systems, a franchisor and a franchisee are free to expressly agree and incorporate the terms establishing the franchisor's assistance obligation into a franchise contract. In this respect, the contents of the

¹⁴² See subsections 4.3.2.2, 4.3.3.2, and 4.3.4.2.

expressly agreed terms will vary from business to business.¹⁴³ Some organizations, such as the ICC and the ABA, may offer model clauses to ease the difficulty in drafting the contractual terms.

As can be seen from the model clauses offered by the ICC and the ABA, two standard features of the franchisor's assistance obligation can be observed. First, the franchisor may be required to provide the franchisee with initial assistance in the form of pre-opening training programs. The primary goal of organizing the training courses is to equip the franchisee with the basic knowledge necessary for operating a franchised business. Second, the franchisor may be obliged to render ongoing support to the franchisee during the franchised business operation. In this case, the franchisor typically agrees to provide the franchisee with operational advice and manuals.

– *Difference*

Sometimes, a franchisor and a franchisee may not explicitly agree on establishing the franchisor's assistance obligation. In this context, the DCFR markedly differs from the US and Australian legal systems because the DCFR supplies the default rule regulating the franchisor's duty to assist.¹⁴⁴ When the parties leave this issue untouched, IV.E. – 4:203 will fill the gap by imposing the franchisor's obligation to provide the franchisee with general assistance in the form of training, guidance, and advice. The franchisor will also be required to be responsive to the franchisee's request for special forms of assistance. Additionally, IV.E. – 4:203 designates a person who bears the cost of the assistance. Whereas the franchisor has to cover the cost of providing general support, the franchisee is responsible for a reasonable cost of rendering special support. The establishment of this mechanism would arguably result from the idea that civil codes usually contain default provisions applied to fill a gap in some specific contracts, such as sales contracts. In practice, this idea can be found to be embraced in the Dutch civil code, for example.¹⁴⁵

Conversely, the like-mechanism cannot be found in the USA and Australia. As said earlier, franchise-specific legislation in those countries contains no provision establishing the franchisor's mandatory assistance obligation. Furthermore, the franchisor's duty of assistance cannot be implied under common law rules. In the USA, some courts held that the implied covenant of good faith and fair dealing could not be used to establish an independent duty to assist,

¹⁴³ It should be mentioned that the terms of a franchise agreement may be identical among franchise systems in the same business. In practice, some franchisors may appoint the same legal firm to draft a single-unit franchise agreement for their own franchise system. In this case, the firm may prepare franchise agreements with similar terms for its clients.

¹⁴⁴ See subsection 4.3.2.3.

¹⁴⁵ Arthur S Hartkamp, *Contract Law in the Netherlands* (2nd edn, Kluwer Law International 2015) 103.

separating from an express agreement.¹⁴⁶ In Australia, no case law indicates that the statutory duty to act in good faith under the Franchising Code of Conduct is utilized to establish the franchisor's duty to assist. Thus, if a franchise contract does not address the existence of the duty explicitly, these two systems would assume that the franchisor undertakes no obligation to support the franchisee in the franchised business operation.

– Discussion

The first approach observed from the comparison is the regulation of the franchisor's duty to assist by express terms of a franchise contract. In terms of greater clarity, a franchise contract may be a proper instrument that provides more clarifications on the franchisor's duty of assistance. Under a franchise agreement, a franchisor and a franchisee can enumerate particular forms of the franchisor's assistance to the franchisee, taking into account the franchise business's uniqueness. For example, the franchise agreements in the US case *Burger King Corp v Hinton* made a list of supporting services to be given. These services include, for example, the provision of a manual or some research data and advice.¹⁴⁷ In some cases, a franchisor and a franchisee may not contemplate and agree on comprehensive forms of the franchisor's assistance. In this case, the franchisee may not receive necessary assistance and support in operating a franchised business. Thus, the use of private regulation in this respect may not be protective of a franchisee.

In the absence of an express agreement, the DCFR shows that it offers an alternative approach – the regulation of the franchisor's duty to assist by the default law rule. As can be seen, the DCFR contains the rule that fills the gap in a franchise contract by establishing the franchisor's assistance obligation if the parties are silent on this point. Nevertheless, the DCFR's rule is made by default. It means the application of the rule can be excluded or deviated from by agreement. A bigger franchisor may employ its superior power to circumvent the utilization of the default provision by drafting a franchise agreement excluding this provision entirely. Therefore, the regulation of the franchisor's assistance by default rules may not be effective in protecting a franchisee in this regard.

In reality, many franchisees are inexperienced business persons without prior knowledge of doing business. In this case, it is unsurprising that some scholars regard the franchisor's assistance as imperative for the success of the

146 See eg *TCBY Systems, Inc v RSP Co, Inc*, 33 F3d 925 (CA8 (Ark), 1994) 928; *Camp Creek Hospitality Inns, Inc v Sheraton Franchise Corp*, 139 F3d 1396 (CA 11 (Ga), 1998) 1403; *HLT Existing Franchise Holding LLC v Worcester Hospitality Group LLC*, 994 F Supp 2d 520 (SDNY, 2014) 536.

147 *Burger King Corporation v Hinton, Inc*, 203 F Supp 2d (SD Fla, 2002) 1360.

franchisee's business.¹⁴⁸ Thus, I suggest that comprehensive franchise law includes the following mandatory rule constituting the franchisor's assistance obligation. The establishment of the franchisor's duty to assist will be beneficial not only to a franchisee. It will also benefit a franchisor in selling a franchise license. One empirical study shows that some franchisees gain more confidence in deciding to buy a franchise if they can be aware of support mechanisms to be given.¹⁴⁹

'(1) The franchisor must provide the franchisee with (a) initial assistance that is necessary for the opening of the franchised business and (b) ongoing assistance that is necessary for the operation of the franchised business. In this case, the franchisor must bear the costs associated with the provision of the initial and ongoing assistance.

(2) The franchisor must be responsive to the franchisee's reasonable request for special assistance. In this case, the franchisee must bear the costs associated with the provision of the special assistance.'

(1) *Mandatory assistance by a franchisor*

This model rule provides that the franchisor's duty to assist is mandatory. This model rule requires a franchisor to offer a franchisee the following three forms of assistance.

(1.1) *Initial assistance*

The first requirement of the first paragraph is that the franchisor provides the franchisee with initial assistance. This type of assistance is of paramount importance to franchisees who are inexperienced in doing business.¹⁵⁰ As can be seen, it is accepted that a franchisor should assist its franchisees in an initial stage of a franchise relationship. For example, some organizations, such as the ICC, AAFD, and ABA, recommend the incorporation of a franchise contract's provisions that establish the franchisor's duty to offer initial support to franchisees. Besides, the DCFR's model rule requires the franchisor to assist a franchisee in commencing the operation of a franchised unit. Thus, these

148 Cecilia M Falbe and Thomas C Dandridge, 'Franchising as a Strategic Partnership: Issues of Co-operation and Conflict in a Global Market' (1992) 10(3) *International Small Business Journal*, 40, 41-42.

149 Anne Marie Doherty, Xiaomin Chen, Nicholas Alexander, 'The franchise relationship in China: agency and institutional theory perspectives' (2014) 48 *European Journal of Marketing* 1664, 1680.

150 The franchisor's initial assistance will also benefit the franchisor itself. Regardless of the franchisee's business experience, the franchisor's assistance and support in starting a franchised business will equip its franchisees with basic knowledge and know-how for operating the businesses in the franchisor's franchise system. In this respect, the franchisor can create uniformity in doing a franchise business and steer the franchise system to success in the industry.

examples affirm that the franchisor's initial assistance is vital for a franchisee to commence a franchised business.

It should be noted that this rule aims to set an underlying principle that the franchisor has to provide the franchisee with necessary assistance in an initial phase of a franchise relationship. In other words, the forms of the franchisor's support are left for legal systems or the parties to decide to elaborate on specific forms of initial assistance, which can vary. For instance, legal systems or the parties may provide that the initial assistance shall take the form of providing essential training; that is to say, a franchisor may arrange a training course that enables a franchisee to gain basic knowledge about the day-to-day operations of a franchised business, as well as some managerial know-how and skills.¹⁵¹

(1.2) *Ongoing assistance*

The second requirement of the first paragraph is that the franchisor shall provide the franchisee with ongoing assistance. This type of support is to be provided during the operation of a franchised business to ensure that the franchisee's business remains competitive in the market. Ongoing assistance is also required to ensure that a franchisee operates its franchised unit uniformly. The maintenance of uniformity in the operation of the franchises business would eventually benefit all franchisees in the networks as it would minimize the occurrence of free-riders that harm the franchise's brand. Thus, it would be imperative for a franchisor to provide ongoing assistance in the course of a franchise relationship.

The proposed provision aims to require a franchisor to assist a franchisee throughout an ongoing relationship. In this respect, the particular forms of ongoing support may differ from case to case. For instance, one franchise consultant says that a franchisor may provide ongoing support in the forms of site support visits, advertising and marketing support, and another industry-specific support.¹⁵² Additionally, a franchisor may provide a franchisee with logistical support, such as structures, equipment, signs, or processed food.¹⁵³ It should be mentioned that the franchisor is required to assist the franchisee insofar as it is necessary for the franchisee to operate an ongoing franchised business.

151 Phillip D Grub, 'Multinational Franchising: A New Trend in Global Expansion' (1972) 7(1) *Journal of International Law and Economics* 21, 28.

152 Mark Siebert, 'How Much Ongoing Support – and What Kinds – Should You Provide to Your Franchisees?' (*Entrepreneur*, 29 January 2016) accessed <<https://bit.ly/3lYulcT>> 22 January 2022.

153 Grub (n 151) 29.

(1.3) *Special assistance*

The second paragraph of the proposed rule deals with the provision of special assistance by a franchisor. In some cases, a franchisor can be required to provide a franchisee with assistance, which is tailor-made to fit the franchisee's needs. The idea behind this requirement is that individual franchisees may encounter some difficulties in operating franchised businesses. For example, the franchisee may face some technical or managerial problems to which the franchisor is the only person who can fix them. In this regard, the principle should be that an individual franchisee can demand the franchisor's special support.

Unlike the provision of initial and ongoing assistance, a franchisor is required to provide a franchisee with special assistance only upon the franchisee's reasonable request. However, it would be impracticable to provide specific instances of the franchisee's reasonable request for assistance in the text as there can be diverse operational issues in a franchise business. Thus, it would be wise that the proposed provision leaves the issue to be decided on a case-by-case basis, considering the circumstances of the case. In any event, the objective criteria of reasonableness offered by the DCFR's model rule could be followed as guidelines.¹⁵⁴ A court should consider the nature and purpose of a franchise agreement, the circumstances of the case, and the usages and practices of the trade or profession involved to determine whether the franchisee's request is reasonable.

(2) *Costs associated with the provision of assistance*

The proposed rule also designates a person who bears the costs of providing support to avoid any potential conflict between the franchisor and franchisee.

First, the proposed rule provides that the franchisor pays the costs of providing preopening and ongoing assistance. The rationale behind this requirement is that the initial and ongoing assistance not only benefits individual franchisees but it also benefits the franchisor by enhancing the franchisor's franchise business goodwill. It should be mentioned that the rule intends to designate the franchisor as a person who is primarily responsible for the payment.

In practice, a franchisor may shift the burden to a franchisee by including the costs, such as training costs, in the initial franchise fees that the franchisee has to pay for the grant of a franchise license.¹⁵⁵ Furthermore, the franchisor may include the costs for ongoing support in the royalty fees paid by the franchisee.¹⁵⁶ In this case, there is a question: should there be any limit on

¹⁵⁴ The DCFR, I-1:104.

¹⁵⁵ Shelley Nadler, 'Who pays for a franchisee's initial training?' (What Franchise) accessed <<http://bit.ly/3H5RPxS>> 15 January 2023.

¹⁵⁶ 'Understanding the Hidden Costs of Franchising' (Guidant) accessed <<http://bit.ly/3w6Euis>> 15 January 2023.

the costs levied against the franchisee? In my view, there should be no cap on the amount that the franchisor charges the franchisee for initial and ongoing assistance and support. In some cases, the franchisor may justifiably ask for the payment. For example, Rich argues that the franchisor can charge the franchisee for initial and ongoing training costs because the franchisor teaches the franchisee how to professionally operated the franchised business.¹⁵⁷

However, when it comes to levying the costs against the franchisee, I suggest that the franchisor considers two factors: transparency and reciprocity. First, charging the costs should be transparent. How much the franchisee has to pay for initial and ongoing assistance and support must be detailed in a franchise agreement. In this respect, the franchisee will have a chance to deliberate on the levy before entering into a franchise contract with the franchisor. Second, the costs charged against the franchisee must be reciprocal. In other words, the franchisor should levy the amount that reasonably suits quantity and quality of the franchisor's assistance provided to the franchisee. If the franchisor excessively charges the franchisee, the franchisee should be permitted to claim the residual amount on legal bases available in legal systems, such as unjustified enrichment.

Second, the proposed rule provides that the franchisee is required to cover any expenses arising from the provision of special assistance. The reason is that this type of franchisor support benefits the franchisee individually because special assistance is usually tailored to suit the need of an individual franchisee for assistance. Thus, it would be reasonable that the requesting franchisee bears the costs of providing special assistance. For example, the requesting franchisee may have to reimburse expenses incurred when the franchisor sends its technical staff to fix on-site issues. Those expenses may include travel and overnight accommodation expenses. In sum, the franchisee is required to reimburse for the expenses that the franchisor has actually paid in order to assist or support the franchisee.

4.3.5.3 Conclusions

– Concluding remarks

The comparative examination finds that the DCFR, the USA, and Australia are similar in that a franchise contract will be a primary source of the franchisor's duty to assist. Under the selected legal systems, the terms of a franchise contract will constitute the franchisor's obligation to assist and elaborate on the contents of the franchisor's duty. Under the terms, practical examples show that a franchisor is typically required to provide a franchisee with initial assistance and ongoing support. It should be noted that many franchise con-

¹⁵⁷ Sarah Stowe, 'Should franchisors charge franchisees for their training' (28 October 2015, Inside Franchise Business) accessed <<http://bit.ly/3wb8M3z>> 15 January 2023.

tracts may not explicitly establish the franchisor's assistance obligation.¹⁵⁸ In this case, the DCFR differs from the US and Australian legal systems in that the DCFR offers a franchise default provision imposing an assistance obligation on a franchisor.

– *Key recommendations*

(1) *Establishment of the franchisor's duty to assist*

Comprehensive franchise law should include the rule that constitutes the franchisor's duty to assist a franchisee. This obligation should be mandatory. In this case, the rule should obligate the franchisor to provide the franchisee with the following three forms of assistance: (1) initial or preopening assistance, (2) ongoing assistance, and (3) special assistance.

(2) *Initial assistance*

The requirement of initial assistance will ensure that the franchisee is adequately assisted in the opening of a franchised business. However, the provision does not specify particular forms of initial assistance. Thus, legal systems or the parties are free to enumerate a list of pre-opening assistance, which usually includes providing a training or educational program.

(3) *Ongoing assistance*

The requirement of continuing assistance will ensure that the franchisee is adequately provided with ongoing support periodically after opening a franchised business. Likewise, legal systems or the parties are free to elaborate on the specific forms of assistance to be rendered. In practice, the ongoing assistance may take the form of refresher training programs, annual seminars, and advertising programs.

(4) *Special assistance*

An individual franchisee may encounter some specific problems in running a franchised business. In this case, the franchisor should be required to respond to the franchisee's reasonable request for support. A question of whether the franchisee's demand is reasonable should be decided on a case-by-case basis, considering the nature and purpose of a franchise agreement, the circumstances of the case, and the usages and practices of the trade or profession involved.

(5) *Costs of providing required assistance*

Comprehensive franchise law should also designate a person who bears the costs of rendering the mandatory assistance. The franchisor should be required to bear the costs of providing the franchisee with initial and ongoing assistance.

¹⁵⁸ Some contracts give the franchisor discretion when it is reasonable to provide the franchisee with assistance.

The franchisee should be required to reimburse the expenses that the franchisor spends in providing special assistance.

4.4 PRIVATE LAW REMEDIES

4.4.1 Introduction

A research study on a substantive aspect of the franchisor's ongoing duties will be incomplete if the study does not explore the potential remedies in the case of the franchisor's failure to perform the duties. From a franchisee's perspective, a question may arise if an aggrieved franchisee can force the franchisor to stop encroaching upon the franchisee's business or assist the franchisee according to the terms. If the franchisor's breaching conduct inflicts a loss on the franchisee, the injured franchisee would be curious to know if the franchisee can claim monetary compensation. The franchisee would also want to search for exit ways if maintaining a franchise relationship is no longer desirable. This section will examine the remedial system of the DCFR, the USA, and Australia that permits an aggrieved franchisee to compel the franchisor's action or inaction, claim damages, and cancel a franchise contract in sections 4.4.2, 4.4.3, and 4.4.4, respectively. A comparative examination of the remedial regimes will be conducted in section 4.4.5 to formulate suggestions on establishing a remedial system under comprehensive franchise law.

4.4.2 The Draft Common Frame of Reference (DCFR)

4.4.2.1 Introduction

Under the DCFR, an aggrieved franchisee can resort to the remedial rules that entitle the franchisee to enforce the franchisor's performance in kind, recover damages, and terminate a franchise contract. These remedial rules are mainly prescribed by contract law provisions in Book III. This section will examine the rules that permit an aggrieved franchisee to seek those three remedies in subsections 4.4.2.2, 4.4.2.3, and 4.4.2.4, respectively. Subsection 4.4.2.5 will conclude on the nature of the remedial system of the DCFR.

4.4.2.2 Enforcement of performance

A franchisee may resort to III. – 3:302 for the right to enforce a franchisor to perform contractual obligations in the case of non-compliance with the obligations. According to III. – 3:302(1)(2), the creditor is entitled to enforcing specific performance of a non-monetary obligation if the debtor fails to comply with the terms regulating an obligation. In the context of this chapter, the franchisee

may enforce the franchisor's performance *in natura* if the franchisor failed to perform the duty not to encroach or the duty to assist. For example, a franchisee may enforce a franchisor to comply with an exclusivity clause by refraining from encroaching upon the franchisee's exclusive territory by operating a company-own outlet or placing a new franchised unit. A franchisee may compel a franchisor to arrange a pre-sale training program before opening a franchised business or provide specific assistance in accordance with the contract terms.

The right to enforce specific performance under the DCFR is not unqualified because III. – 3:302(3) and (4) impose limitations on enforcing the performance of an obligation. Under III. – 3:302(3) and (4), the franchisor may raise a defense relying upon two legal bases.

First, the franchisor may argue that the performance of the obligation would be (a) unlawful, (b) unreasonably burdensome or expensive, or (c) of such a personal character that it would be unreasonable to enforce it. For instance, the franchisor may claim that taking down the whole franchised unit established in breach of the exclusivity provision is unreasonably burdensome and expensive. The franchisor may argue that it is unreasonably burdensome for the franchisor, who resides at a great distance, to send its staff to assist the franchisee on a matter that could easily be solved by local personnel.¹⁵⁹ In these cases, the franchisor has to prove great distress, vexation, or inconvenience caused by the enforcement of the specific performance.¹⁶⁰ Upon the satisfaction of the exception, the franchisor cannot be forced to comply with the obligation. In any event, the franchisee may seek damages as a substituting remedy since III. – 3:303 provides the fact that the right to enforce specific performance does not preclude a claim for damages.

Second, the franchisor may claim that the right to enforce specific performance is lost because the franchisee does not request the performance within a reasonable time after the franchisee has become, or could reasonably be expected to have become, aware of the non-performance. Suppose the franchisee has become aware that the franchisor fails to arrange an annual conference, which is a form of ongoing support, promised under a franchise agreement. In this case, the franchisee may lose the right to enforce the franchisor's performance if the franchisee does not request the arrangement in a reasonable time; for example, three months.

¹⁵⁹ This example is adapted from Illustration 4 of the Comments to III. – 3:302. In this Illustration, the drafters of the DCFR provide that it would be unreasonably burdensome if the creditor could easily obtain performance from another source. See Bar and Clive (n 3) 831.

¹⁶⁰ Ibid.

4.4.2.3 Monetary compensation

A franchisee who suffers any loss or damage caused by the franchisor's failure to perform the duty not to encroach or the duty to assist may claim monetary compensation in the form of damages. In this case, the injured franchisee may seek an award of damages under III. – 3:701. The following two italicized headings will explain the requirements for the recovery of damages and principle governing a measure of damages under the rule.

– *Requirements for recovery of damages*

The requirement for claiming damages under III. – 3:701 is threefold.

First, an injured franchisee needs to prove the franchisor's non-performance of the obligation. According to III. – 3:101(1), the phrase 'non-performance' denotes a situation where the debtor does not perform an obligation. For example, a franchisor will be considered not in compliance with the obligation not to encroach if it appointed another franchisee to operate a franchised store within an exclusive location of the existing franchisee. III. – 3:101(1) also provides that the debtor's failure to perform an obligation must not be excused. According to III. – 3:104(1), the franchisor's non-performance is excused if an impediment beyond the franchisor's control occurs to prevent the franchisor from performing the obligation. For example, the franchisor may argue that it cannot arrange a pre-opening training course for the franchisee on the agreed date because the government has shut down the venue for training amidst the COVID-19 pandemic. In this case, the franchisor's non-performance of the duty to assist can be excused.

Second, an injured franchisee has to prove the loss or damage suffered as a result of the franchisor's non-performance of the obligation. According to III. – 3:701(3), the recoverable loss includes economic and non-economic loss. To elaborate, the franchisee may claim damages for economic loss, including loss of income or profit, burdens incurred and a reduction in the value of the property. The franchisee may recover compensation for non-economic loss, including pain and suffering and impairment of the quality of life. In addition to actual loss, III. – 3:701(2) permits the franchisee to recover damages for future loss that has not accrued yet at the time of assessing damages. Thus, the franchisee may claim damages for future incomes that the franchisee could reasonably have been expected to make if the franchisor had duly performed its obligations.¹⁶¹

Third, an injured franchisee must illustrate the chain of causation. That is, the franchisee must show that the loss incurred has been caused by the franchisor's failure to perform the duty not to encroach or the duty to assist. Nevertheless, the franchisor's liability for damages will be subject to the

161 Ibid 918.

foreseeability principle set out by III. – 3: 703. According to this provision, the franchisor will be responsible only for the loss which the franchisor foresaw or could reasonably be expected to have foreseen, at the time of incurring the obligation, as a likely result of the non-performance. However, this rule does not apply if the franchisor's non-performance of an obligation is intentional, reckless, or grossly negligent.

– *Principles governing a measure of damages*

A character of damages under III. – 3:701 is compensatory. According to III. – 3:702, the sum of damages must put the franchisee as nearly as possible into the position in which the franchisee would have been if the franchisor had duly performed an obligation. Furthermore, this provision also provides that damages cover the loss suffered and the gain deprived. In this respect, an aggrieved franchisee would recover damages for loss of expectation interests and expenditure incurred.¹⁶² For example, in the case of franchisor encroachment, an injured franchisee may seek an award of damages for the loss of revenues that the franchisee would have gained if the franchisor had not encroached upon the franchisee's exclusive territory. In the case of the franchisor's failure to assist, the franchisee may recover damages for the expenditure incurred if the franchisee has outsourced some promised technical support to other companies.

4.4.2.4 Cancellation of a franchise contract

The franchisor's non-performance of a contractual obligation would permit an aggrieved franchisee to cancel a franchise contract by way of termination. The franchisee may terminate a franchise contract following the contract terms or under the rules of the DCFR. The following three italicized headings will examine the contractual and legal rights to terminate a franchise contract, as well as the effects of termination of the contract.

– *Contractual right to terminate*

A franchise contract may allow a franchisee to terminate the contract in the event of the franchisor's non-compliance with contractual terms. Taking the ICC's Model Contract as an example, article 26.1 entitles the franchisee to terminate a franchise contract in the case of the franchisor's substantial breach of obligations arising out of the agreement.¹⁶³ Moreover, the Model Contract

¹⁶² Ibid 924.

¹⁶³ This clause is enforceable under the DCFR as it conforms to IV.E. – 2:304(1). This article prevents the parties from incorporating the terms of a contract that allows the termination of the contract for insubstantial non-performance.

defines the term 'substantial breach' to mean any failure by a party to carry out all or part of obligations under a franchise contract resulting in such detriment to the other party as to substantially deprive the other party of what it is entitled to expect under the contract.¹⁶⁴ Thus, the franchisee may terminate a franchise contract if the franchisor licensed other franchisees to operate a franchised business within the granted territory of the franchisee.¹⁶⁵ The franchisee may also terminate a franchise contract if the franchisor failed to provide the franchisee with adequate assistance in the pre-opening stage.¹⁶⁶

– *Legal right to terminate*

Besides the contractual right to terminate, Section 5 of Book III of the DCFR contains the provisions in Section 5 of Book III that allow an aggrieved franchisee to terminate a franchise contract on several grounds.¹⁶⁷ For example, a franchisee may terminate a franchise contract for fundamental non-performance of an obligation. According to paragraph (1) of III. – 3:502, an aggrieved franchisee may terminate a franchise relationship if the franchisor's non-performance of obligations is fundamental. In this case, the franchisee needs to plead that the franchisor's failure to perform an obligation substantially deprives the franchisee of what the franchisee was entitled to expect under the franchise contract.

For example, the franchisee may argue that the franchisor's breach of the duty not to encroach has significantly seized the franchisee's profits or incomes that the franchisee can expect from a franchised business operation in the exclusive area. Furthermore, the franchisee may claim that the franchisor's failure to provide ongoing assistance has lessened the franchisee's ability to run a franchised business profitably. In terminating a franchise contract for the franchisor's substantial non-performance, the franchisee must prove that the franchisor foresaw or could reasonably be expected to have foreseen that substantial deprivation at the time of conclusion of the agreement.¹⁶⁸

An aggrieved franchisee may terminate a franchise contract in case of delayed performance, which is not fundamental. According to III. – 3:503(1), the franchisee may terminate the franchise contract on the condition that the franchisee gives the franchisor notice fixing a reasonable period of time for the performance, and the franchisor does not perform within that fixed period.

164 International Chamber of Commerce (n 118) 40.

165 See subsection 4.2.2.2.

166 See subsection 4.3.2.2.

167 It should be mentioned that these are grounds for terminating a franchise contract with a definite period. In other words, a franchisee may terminate a franchise agreement for an indefinite period without any ground by giving a franchisor notice of termination. The detailed examination of the right to terminate a franchise agreement for an indefinite period is made in subsection 5.5.2.4 in chapter 5.

168 The DCFR, III. – 3:502(2)(a).

Assume the franchisor promises to arrange an ongoing training program for the franchisee on the 31st of August 2023. If the franchisor fails to do so, the franchisee can notify the franchisor to set up the training course within one month after the agreed date. In this case, the franchisee can terminate the franchise contract if the franchisor does not arrange the training course after the fixed period has passed.

Additionally, an aggrieved franchisee may terminate a franchise contract for anticipated non-performance. According to III. – 3:504, the franchisee may terminate the franchise contract if the franchisor has declared that, or it is otherwise obvious that, there will be non-performance of the obligations before the due date, and the anticipated non-performance is fundamental. As can be seen, the franchisee needs to satisfy two conditional elements. First, there is a threat of non-performance of an obligation before it is due. Suppose the franchisor promises not to encroach upon the franchisee's exclusive territory during the entire franchise relationship. In that case, the franchisee may demonstrate that the franchisor threatens to break the promise by negotiating with another prospective franchisee to open a new franchised store in the franchisee's exclusive location. Second, the franchisor's non-performance of an obligation must be fundamental. This element means that the obligation must be the main obligation of which the non-performance would allow the franchisee to terminate a franchise contract.¹⁶⁹

– *Effects of termination*¹⁷⁰

The successful termination of a franchise contract will end a franchise relationship with future effect.¹⁷¹ III. – 3:509(1) provides that termination will end the parties' outstanding obligations under a contract. According to the drafters of the DCFR, an outstanding obligation means an unperformed obligation. In other words, the obligation is outstanding if it is not performed in a way that conforms with the terms of the contract.¹⁷² However, III. – 3: 509(2) makes clear that termination will not affect any provision of a contract for the settlement of disputes or provisions that are to operate after the termination. For example, non-compete and confidentiality clauses will remain in force after the termination of the contract. An aggrieved franchisee may retain the right to damages even after the termination of a franchise contract. According to III. – 3:509(3), the franchisee is entitled to damages for the loss caused by the

¹⁶⁹ Bar and Clive (n 3) 868.

¹⁷⁰ Apart from the effects to be examined in this heading, termination of a franchise contract will entitle the franchisee to seek specific remedies regarding repurchase and goodwill under the DCFR. The franchisee's right to these specific remedies will severally and thoroughly be examined in subsection 5.5.2.5 in chapter 5.

¹⁷¹ Bar and Clive (n 3) 887.

¹⁷² Ibid 886.

franchisor's actual non-performance of an obligation under a franchise agreement.

Additionally, termination of a contract gives rise to restitutionary remedies in some cases. According to III. – 3: 510(1), a party is obliged to return any benefit received by the other's performance of obligations under the terminated contract.¹⁷³ Furthermore, III. – 3: 510(5) provides that the obligation to return a benefit extends to any natural and legal fruits received from the benefit. It should be noted that the parties are not required to return all benefits received under the terminated contract. According to the drafters of the DCFR, a contracting party is required to return the benefit that would unjustly enrich that party.¹⁷⁴ For instance, the franchisor will be required to return paid training fees to the franchisee if the franchisee terminates a franchise contract because the franchisor fails to arrange a training course for the franchisee.

4.4.2.5 Conclusions

The remedial regime under the DCFR is contractual. Since the franchisor's duty not to encroach and the duty to assist is contractually established, an aggrieved franchisee needs to resort to contract law remedies in Book III when it comes to failure to perform those obligations. In Book III, the franchisee may enforce the franchisor's performance of the obligations, claim damages, and cancel a franchise contract by way of termination. Granting these three remedies is not conditional upon a court's discretion. In other words, resorting to the three sanctions is a matter of right; the franchisee merely has to meet the requirements for utilizing each remedy. Nevertheless, the franchisor may manage to argue for exceptions to liability in some cases.

4.4.3 The United States of America (USA)

4.4.3.1 Introduction

As described in sections 4.2.3 and 4.3.3, the terms of a franchise contract primarily regulate the franchisor's duty not to encroach and the duty to assist. In this case, an aggrieved franchisee has to resort to contract law remedies to enforce the franchisor's performance, claim monetary compensation, and cancel a franchise contract.¹⁷⁵ As shown in subsection 4.2.3.2, five US states

¹⁷³ The ways in which the restitution is made are addressed by III. – 3: 510(2) – (4).

¹⁷⁴ Bar and Clive (n 3) 893.

¹⁷⁵ Except for Louisiana, contract law rules governing the three remedies are based on state common law principles. Since the common law rules may vary slightly from state to state, the rules to be examined in this section should be understood as being accepted among the majority of the states.

– Hawaii, Indiana, Iowa, Minnesota, and Washington – regulate franchisor encroachment through franchise relationship law rules. In this case, an aggrieved franchisee may seek statutory remedies that allow the franchisee to compel the franchisor’s action or inaction, recover compensation, and cancel a franchise agreement. This section will examine the contractual and statutory remedies of enforcement of performance, damages, and cancellation of a franchise contract in subsections 4.4.3.2, 4.4.3.3, and 4.4.3.4, respectively. Conclusions about the character of the US remedial system will be drawn in subsection 4.4.3.5.

4.4.3.2 *Enforcement of performance*

An aggrieved franchisee may compel the franchisor’s action and inaction by seeking specific performance and injunctive relief. In general, the franchisee may resort to common law rules for these remedies. In five relationship states, the franchisee may seek a remedy of injunctions under state franchise relationship law rules. The following two italicized headings will examine the enforcement of the franchisor’s performance under common law and franchise relationship laws.

– *Specific performance and injunctions in common law*

An aggrieved franchisee may seek common law remedies that permit the franchisee to enforce the franchisor’s action or inaction. First of all, an aggrieved franchisee may seek a decree of specific performance to compel the franchisor’s performance. Under common law, specific performance is a contract law remedy that allows a plaintiff to compel a defendant to perform contractual duties affirmatively in case of breach of contract.¹⁷⁶ According to the rule, the claimant franchisee has to illustrate the franchisor’s breach of contract by showing that the franchisor does not comply with the terms imposing obligations on the franchisor. In addition to specific performance, an aggrieved franchisee may seek an order of injunctions, which is a remedy that prevents a person from doing an act specified by a contract.¹⁷⁷ In theory, therefore, an aggrieved franchisee may seek a decree of specific performance

176 See eg *Berryhill v Hatt*, 428 NW 2d 647 (Iowa, 1988) 657; *Clemente v Pearle Vision Inc* 762 F Supp 1518 (D Me, 1991) 1519; *Reed v Triton Servs, Inc*, 15 NE 3d 936, 938, 2014 -Ohio- 3185, (Ohio App 12 Dist, 2014) 938-39; *Minnesota Vikings Football Stadium, LLC v Wells Fargo Bank, National Association*, 193 F Supp 3d 1002, (D Minn, 2016) 1014; *H B Fuller Co v Hamm*, 2018 WL 4047122 (D Minn, 2018) 4; *Homeland Energy Solutions, LLC v Retterath*, 938 NW 2d 664 (Iowa, 2020) 693.

177 See eg *Nemer Jeep-Eagle, Inc v Jeep-Eagle Sales Corp*, 992 F 2d 430 (CA2 (NY), 1993) 433; *DiPilato v 7-Eleven, Inc*, 662 F Supp 2d 333 (SDNY, 2009) 345; *Pure Wafer Incorporated v City of Prescott*, 275 F Supp 3d 1173 (D Ariz, 2017) 1176.

and injunctions to enforce the franchisor's performance of the duty not to encroach and the duty to assist.

In common law, specific performance and injunctive relief are equitable remedies. In this regard, granting these remedies is a matter of courts' discretion. As courts have discretion in ordering specific performance and injunctions, a grant of the remedies can be constrained by several limitations, including indefiniteness, insecurity, burdens of enforcement and supervision, inappropriateness for personal service contracts, unfairness, and public policy.¹⁷⁸ For instance, the courts in Florida concurrently held that a franchise contract is not subject to a claim for specific performance because of the nature of personal service contracts.¹⁷⁹ In *North American Financial Group*, the court denied granting specific performance requiring the franchisor to provide personal, specialized services for an unspecified time to train the franchisees to operate a franchise business. The court reasoned that this remedy would require the court to supervise the franchisor's performance of the obligations periodically.¹⁸⁰

More importantly, courts usually do not issue these exceptional remedies if the remedy at law is more suitable than equitable remedies. In common law, the general rule is that damages are considered the remedy at law; hence, courts will not grant equitable relief if the remedy of damages is adequate to protect an expectation of the injured party.¹⁸¹ Despite this, an aggrieved franchisee may demonstrate the inadequacy of damages to make equitable relief more appropriate. One factor that can be used to show the inadequacy of the remedy at law is the difficulty in determining damages to be awarded. Farnsworth exemplifies that equitable relief is often granted if it is not possible at the time of trial to quantify the amount of loss that will occur in the future.¹⁸² In this case, courts may decree a remedy of specific performance or injunctions as the difficulty in determining damages would cause irreparable harm to a plaintiff.

178 E Allan Farnsworth, *Contracts* (4th edn, Aspen Publishers 2004) 751-57.

179 See eg *Burger Chef Systems, Inc v Burger Chef of Fla, Inc*, 317 So2d 795 (Fla App 1975) 797; *Burger King Corp v Weaver*, 798 F Supp 684 (SD Fla, 1992) 692; *Burger King Corp v Agad*, 911 F Supp 1499 (SD Fla, 1995) 1506.

180 *North American Financial Group, Ltd v SMR Enterprises, Inc*, 583 F Supp 691 (DC Ill, 1984) 699.

181 See eg *C-B Kenworth Inc v General Motors Corp* 675 F Supp. 686 (D Me, 1987) 686-87; *Augusta News Co v News America Pub Inc* 750 F Supp 28 (D Me, 1990) 32; *Foreign Motors Inc v Audi of America Inc* 755 F Supp 30 (D Mass, 1991) 33; *Clemente* (n 176) 1519; *Nemer Jeep-Eagle* (n 177) 433; *Dunkin' Donuts Inc v Kashi Enterprises, Inc*, 119 F Supp 2d 1363 (ND Ga, 2000) 1364; *JTH Tax, Inc v Lee*, 514 F Supp 2d 818 ED Va, 2007) 825; *DiPilato* (n 177) 345; *AAMCO Transmissions, Inc v Dunlap*, 646 Fed Appx 182 (CA3 (Pa), 2016) 183; *Arabian Motors Group WLL v Ford Motor Company*, 228 F Supp 3d 797 (ED Mich, 2017) 800; *Martin v Weed Incorporated*, 2018 WL 9880066 (D Ariz, 2018) 2.

182 E Allan Farnsworth, *United States Contract Law* (rev edn, Juris Publishing 1999) 185.

In practice, some franchisees managed to prove the irreparability of harm. For example, in *Pepsi-Cola v Pepsico*, the plaintiff franchisee sought an injunction because the franchisor was encroaching upon the franchisee's exclusive area. In this case, the franchisee successfully established that the remedy of damages was not appropriate as there was the likelihood of irreparable injury. That is, the franchisee argued that it would suffer irreparable harm because of the difficulty and uncertainty in restoring goodwill among customers and regaining customers who were, and would be, solicited by the franchisor. Convinced by the franchisee's argument, the court granted an injunction enjoining the franchisor's encroachment was appropriate.¹⁸³

– *Specific performance and injunctions under state franchise relationship law*

In terms of the remedy to enforce performance, the franchise relationship law of Hawaii, Iowa, Minnesota, and Washington permit a legal action for injunctive relief in the event of the franchisor's violation of the relationship law rules regulating franchisor encroachment.¹⁸⁴ Accordingly, in principle, an aggrieved franchisee may enjoin a franchisor from encroaching upon the franchisee's exclusive territory. Nevertheless, a remedy of statutory injunctions is regarded as an equitable remedy. Thus, courts usually have discretion in issuing injunctive relief for justice's sake.¹⁸⁵ A claimant franchisee also has to satisfy some elements for a grant of the remedy. As far as case law is concerned, these components include (1) the likelihood of success on the merits, (2) the threat of irreparable harm to the claimant in the absence of the relief, (3) the balance between the harm caused to the claimant and the harm that the relief would cause to the other litigants, and (4) public interest.¹⁸⁶

4.4.3.3 Monetary compensation

An injured franchisee who has incurred the loss or damage caused by the franchisor's breach of contract may claim monetary compensation in the form of contract law damages. In addition, in the five relationship states, the franchisee may claim damages in the event of the franchisor's violation of franchise relationship law rules governing franchisor encroachment. The

183 *Pepsi-Cola Bottling Co of Pittsburg, Inc v Pepsico, Inc*, 175 F Supp 2d 1288, (D Kan, 2001) 1294-295.

184 Hawaii: HI ST, § 482E-6(2)(E), in conjunction with § 482E-9(a) and § 480-13(a)(1); Iowa: IA ST, § 523H. 6(1), in conjunction with § 523H.13, and IA ST, § 537A.10(6)(a), in conjunction with § 537A.10(13); Minnesota: MN ST, § 80C.14(Subd. 1), in conjunction with MN ADC, 2860.4400(C) and MN ST, § 80C.17(Subd.1); Washington: WA ST, 19.100.180(f), in conjunction with WA ST, 19.100.190 and WA ST, 19.86.090.

185 *Dataphase Systems, Inc v C L Systems, Inc*, 640 F 2d 109 (CA Mo, 1981) 113.

186 See eg *Upper Midwest Sales Co v Ecolab, Inc*, 577 NW 2d 236 (Minn App, 1998) 240; *McCabe v AIR-serv Group, LLC*, 2007 WL 4591932 (D Minn, 2007) 3.

following two italicized headings will examine the requirements for recovering common law and statutory law damages and the principles governing a measure of two types of damages.

– *Requirements for recovery of damages*

First of all, an injured franchisee may seek an award of damages for breach of contract. In many states, common law rules would require the plaintiff franchisee to prove three conditions of a claim for damages in contract as follows.¹⁸⁷ First, the franchisee needs to show the existence of a valid franchise contract and the plaintiff's performance of all the terms and conditions required under the contract. Second, the claimant franchisee needs to prove the defendant's breach of the contract without legal excuse. In this case, it would be imperative for the franchisee to show that the franchisor fails to comply with the exact terms of a franchise contract.¹⁸⁸ The franchisee must demonstrate its damage sustained. In the franchising context, the recoverable loss typically includes the loss of income, loss of profits, and loss of value of a franchised business.¹⁸⁹ Third, the franchisee must prove a causal connection between the franchisor's breach of contract and the loss or damage sustained. That is, the franchisee has to demonstrate that the loss or damage suffered is the natural and direct consequence of the franchisor's breach.¹⁹⁰

Secondly, an injured franchisee may seek an award of statutory damages for the franchisor's violation of anti-encroachment or ant-competitive provisions

187 See eg *McGinney v Jackson*, 575 So 2d 1070 (Ala, 1991) 1071; *Molo Oil Co v River City Ford Truck Sales, Inc*, 578 NW 2d 222 (Iowa, 1998) 224; *Dickinson v Cosmos Broadcasting Co, Inc*, 782 So 2d 260 (Ala, 2000) 265; *Cater v Barker* 617 SE2d 113, 116, 172 N C App 441 (n C App, 2005) 445; *Associated Underwriters of America Agency, Inc v McCarthy*, 826 NE 2d 1160, 1168, 292 Ill Dec 724, 732, 356 Ill App3d 1010 (Ill App 1 Dist, 2005) 1019; *Shaffer v Regions Financial Corp*, 29 So 3d 872 (Ala, 2009) 880; *Royal Indem Co v Factory Mut Ins Co*, 786 NW 2d 839 (Iowa, 2010) 846; *Oasis West Realty, LLC v Goldman*, 250 P3d 1115, 1121, 124 Cal Rptr 3d 256, 263, 51 Cal 4th 811 (Cal, 2011) 821; *Sherwood Brands, Inc v Great American Ins Co*, 13 A3d 1268, 1286, 418 Md 300 (Md, 2011) 329.

188 For example, in *Stillwell v RadioShack*, the court found that the franchisor did not breach the agreement by engaging in online sales via its website in the franchisee's exclusive area because the agreement prevented the franchisor from opening a franchise store or authorizing the establishment of a franchise store within a granted area of the franchisee. In other words, the franchisor was barred from engaging in traditional encroachment only.

189 See eg *Seegmiller v Western Men Inc* 437 P2d 892, 894–95, 20 Utah 2d 352 (Utah, 1968) 355; *Atlantic Richfield Co v Razumic* 390 A2d 736, 742, 480 Pa 366 (Pa, 1978) 381; *Westfield Centre Service Inc v Cities Service Oil Co* 432 A2d 48, 57, 86 NJ 453 (NJ, 1981) 469.

190 See eg *Postal Instant Press, Inc v Sealy*, 51 Cal Rptr 2d 365, 368, 43 Cal App 4th 1704 (Cal App 2 Dist, 1996) 1709; *Meineke Car Care Centers, Inc v RLB Holdings, LLC*, 423 Fed Appx 274, 282, 2011 WL 1422900, (CA4 (NC), 2011) 6.

under franchise relationship law.¹⁹¹ In claiming statutory damages, it is vital for the franchisee to sufficiently demonstrate the franchisor's violating conduct that caused damage to the franchisee. For example, in *Coyne's & Co. v Enesco*, the court held that the franchisee sufficiently asserted that the franchisor violated the Minnesota franchise relationship law's provision, making it unfair and inequitable practice for any person to compete with a franchisee in an exclusive territory. In this case, the franchisee claimed that it was an exclusive distributor of the franchisor. The franchisee alleged that, although the franchisor was aware of the franchisee's exclusive rights, the franchisor notified customers and the relevant market segment that the franchisor would be immediately marketing the products in the exclusive area of the franchisee.¹⁹² In addition to asserting the franchisor's contravening conduct, the franchisee must also establish a causal link between the violating conduct and the loss or injury suffered.¹⁹³

– *Principles governing a measure of damages*

In principle, contract law and statutory law damages similarly aim at compensating loss or damage suffered by a claimant. In common law, an award of damages for breach of contract aims to put an injured party into as good a pecuniary position as the party would have had if the contract had been performed or if the breach had not occurred.¹⁹⁴ Likewise, under franchise relationship laws, statutory damages aim to compensate an aggrieved

191 In other states, an aggrieved franchisee may have to resort to a remedy of damages under other statutory frameworks. For example, the franchisee may claim treble damages under section 4 of the Clayton Act (15 USCA § 15(a)). In claiming antitrust damages, the franchisee may have to prove that it has suffered loss or damage because of the franchisor's conduct, and the franchisee is better situated to bring a claim. See *Doctor's Hospital of Jefferson Inc v Southeast Medical Alliance Inc* 123 F3d 301 (CA5 (La), 1997) 305. Nevertheless, the loss or damage sustained must be an antitrust injury, which is an injury that the antitrust laws aim to prevent and results from the franchisor's anticompetitive acts. See *Brunswick Corp v Pueblo Bowl-O-Mat Inc* 97 S Ct 690, 697, 429 US 477 (USNJ, 1977) 489. In establishing the franchisor's unlawful conduct, the franchisee may demonstrate that the franchisor has engaged in the practice of unreasonable restraint of trade in light of section 1 of the Sherman Act. See *State Oil Co v Khan* 118 S Ct 275, 279, 522 US 3 (US Ill, 1997) 10. In this case, the franchisee must plead that the franchisor's concerted action has produced anticompetitive effects within the relevant products and geographic markets, and the franchisor's action is illegal. See *Queen City Pizza Inc v Domino's Pizza Inc* 124 F3d 430 (CA3 (Pa), 1997) 442.

192 *Coyne's & Co, Inc v Enesco, LLC*, 2010 WL 3269977 (D Minn, 2010) 19.

193 *Noble Roman's, Inc v Hattenhauer Distributing Company*, 307 F Supp 3d 907 (SD Ind, 2018) 926.

194 See eg *United Indus Syndicate, Inc v Western Auto Supply Co*, 686 F 2d 1312 (CA Mo, 1982) 1316; *Machine Maintenance & Equipment Co, Inc v Cooper Industries, Inc*, 634 F Supp 367 (ED Mo, 1986) 371; *Oscar Gruss & Son, Inc v Hollander*, 337 F3d 186 (CA2 (NY), 2003) 196; *Coventry Enterprises LLC v Sanomedics International Holdings, Inc*, 191 F Supp 3d 312 (SDNY, 2016) 321.

franchisee for actual loss.¹⁹⁵ It should be noted that punitive damages may be recovered in some relationship states. In Hawaii and Washington, the laws permit an award of damages in the form of treble damages that serves punitive purposes.¹⁹⁶ In this case, a court may award the amount not to exceed three times the actual damages suffered by a plaintiff franchisee.

When it comes to measuring damages, the general principle of common law and statutory law differ slightly. As mentioned in the preceding paragraph, contract law damages are awarded to put the plaintiff into as good a pecuniary position as it would have had if there had been no breach of contract. In this case, the plaintiff would recover damages for the loss of expectancy interests, such as the loss of profits or gains.¹⁹⁷ In contrast, the state franchise relationship laws do not explicitly establish a general measure of damages. Some relationship statutes, such as Arkansas's, merely provide that the franchisee may seek actual damages.¹⁹⁸ Thus, in calculating statutory damages, courts are permitted to find a proper standard for calculating damages.¹⁹⁹ In some cases, the principle would be that an injured party will be placed in a position that the party would have been in had there been no violation of the provision of the statutes. In this case, statutory damages will not cover the benefit of the bargain. In other cases, an amount of damages can be measured to cover the lost bargains if damages for reliance loss cannot return the *status quo ante* of the plaintiff.

4.4.3.4 Cancellation of a franchise contract

An aggrieved franchisee may put an end to a franchise contract. In theory, the franchisee may exercise the right to terminate conferred on by the terms of the franchise agreement. In the absence of the contractual right, the franchisee may resort to common law rules to rescind a franchise agreement. In some relationship states, franchise relationship legislation allows courts to rescind a franchise contract for a violation of the provision concerning prohibited practices. This subsection will examine the termination and rescission of a franchise contract and surveys the effects of termination and rescission of the contract in the following three italicized headings.

195 W Michael Garner, 2 Franchise and Distribution Law and Practice, Westlaw, November 2020 Update, § 10:37.

196 *Ace Quality Farm Products, LLC v Hanh*, 2015 WL 6955304, (Hawaii App, 2015) 4.

197 W Michael Garner, 2 Franchise and Distribution Law and Practice, Westlaw, November 2020 Update, § 8:62.

198 AR ST, § 4-72-208(b).

199 Ronald K Gardner Jr and Mary Kellerman DesCombaz, 'Chapter 11: Relationship and Termination Laws' in Alexander M Meiklejohn (ed), *Franchising: Cases, Materials, & Problems* (American Bar Association 2013) 567.

– *Contractual right to terminate*

The terms establishing the franchisee's right to terminate may vary from contract to contract. In some cases, a franchise contract may permit a franchisee to terminate a franchise contract without cause. For example, a franchise contract may allow the franchisee to terminate the agreement at will by giving the franchisor prior notice of termination.²⁰⁰ For example, in the case *Sensormatic Electronics*, the franchise agreement at issue provided that the franchisee had the right, at its option, to terminate the agreement at any time by giving written notice to the franchisor at least 60 days before the effective date of the termination.²⁰¹ In this case, the franchisee may exercise this right within a specified period to terminate a franchise agreement in response to the franchisor's failure to perform its obligations.

In practice, however, a franchisee rarely retains the right to terminate a franchise contract at its option. Typically, a franchisee is required to terminate a franchise contract for cause, particularly for the franchisor's breach of the agreement. The ABA's Annotated Franchise Agreement exemplifies that the franchisee may terminate a franchise agreement because of the franchisor's breach of a material provision of the contract. In terminating the contract, the franchisee shall provide the franchisor with a written notice that identifies grounds for the breach, and allow the franchisor to cure the breach within 30 days after the receipt of the notice.²⁰² In this respect, the franchisee may terminate a franchise contract provided that the franchisor owes the franchisee the duty not to encroach or the duty to assist under the contract. Otherwise, the franchisee would not be able to terminate the agreement for the franchisor's breach of contract.

– *Rescission of a contract under common law and statutory law*

If a franchisor fails to perform the contractual duty not to encroach or duty to assist, an aggrieved franchisee may cancel a franchise agreement by following common law rules on rescission of a contract.²⁰³ In common law, the

200 Bethany L. Appleby and Iris Figueroa Rosario, 'Termination and Default' in Nina Greene, Dawn Newton, and Kerry Olson (eds), *The Annotated Franchise Agreement* (2nd edn, American Bar Association 2021) 223.

201 *Sensormatic Sec Corp v Sensormatic Electronics Corp* 249 F Supp2d 703 (D Md, 2003) 713.

202 Appleby and Rosario (n 200) 222.

203 It should be noted that the common law rules on rescission to be reviewed in this subsection will be those peculiar to rescinding a franchise contract for a definite period. In other words, cancelling a franchise contract for an indefinite period will be extensively examined in subsection 5.4.3.3 in chapter 5.

franchisee may rescind a franchise contract based on the two following grounds.²⁰⁴

Firstly, an aggrieved franchisee may rescind a franchise contract for the franchisee's material breach of a franchise contract.²⁰⁵ The definition of 'material breach' may vary from state to state. For example, the Wisconsin court in *Citgo Petroleum v Ranger Enterprises* stated that a breach of a franchise contract was material if it defeated the object of the contract or concerned a matter of such importance that the contract would not have been made if default in that particular had been expected.²⁰⁶ US courts seem to adopt a similar principle, providing that breach of contract is considered material if it destroys the primary purposes of the contract or the root or essence of the contract.²⁰⁷ In the context of this chapter, the franchisee would not have concluded a franchise agreement with the franchisor if the franchisee could expect the franchisor's encroachment or the franchisor's failure to assist the franchisee. In this case, the franchisor's breach of the two duties would be considered substantial and permit the franchisee to rescind the franchise contract.

Secondly, an aggrieved franchisee may rescind a franchise contract for the franchisor's repudiation. The term 'repudiation' may be understood differently among the states. Repudiation exists when a party unjustifiably refuses to perform a contract as a whole or any substantial part of it. The party's repudiation would give the plaintiff an option to rescind a contract. In this case, the plaintiff must demonstrate that the defendant's refusal to perform is distinct, unequivocal, and absolute, and the refusal is acted upon as such by the plaintiff.²⁰⁸ In the context of this chapter, an existing franchisee may rescind a franchise contract based on this ground if a franchisor concludes a new franchise agreement that permits a new franchisee to operate a franchised business within the franchisee's exclusive territory. A franchisee may rescind a franchise agreement if a franchisor refuses to launch a preopening

204 It should be noted that common law rules governing rescission may vary from state to state. Thus, the rules stated in this subsection are examples of the common law theories employed by the majority of the US states.

205 In other jurisdictions, breach of contract may not be a single basis for an award of rescission. For instance, courts in Florida have regarded rescission in equity as an exceptional and unusual remedy. In addition to the party's default, courts may interfere with the freedom of contract and grant an award of rescission based on other legal grounds, such as fraud, mistake, or undue influence. See *Bank of New York Mellon v Reyes* 126 So 3d 304 (Fla App 3 Dist, 2013) 308, citing *International Realty Associates v McAdoo* 99 So 117, 119, 87 Fla 1 (Fla, 1924) 7.

206 *Citgo Petroleum Corp v Ranger Enterprises Inc* 632 F Supp2d 878 (WD Wis, 2009) 894.

207 See eg *Wilson v Wilson* 134 SE2d 240, 243, 261 NC 40 (NC, 1964) 43; *Manpower Inc v Mason*, 405 F Supp 2d 959 (ED Wis, 2005) 969; *BOB Acres, LLC v Schumacher Farms, LLC*, 797 NW 2d 723 (Minn App, 2011) 728; *Reuter v Jax Ltd, Inc*, 711 F 3d 918 (CA8 (Minn), 2013) 921.

208 See eg *King Features Syndicate v Valley Broadcasting Co*, 42 F Supp 107 (DC TEX 1941) 108; *Savage v Horne* 31 So 2d 477, 482, 159 Fla 301 (Fla, 1947) 310–11; *J K Welding Co v W J Halloran Steel Erection Co*, 178 F Supp 584 (DCRI 1959) 589.

training course prior to the agreed date. Under common law rules, the claimant franchisee must propose to rescind a contract within a reasonable time. Furthermore, the claimant franchisee must offer to restore what the franchisee has received from the agreement. In this respect, the situation of the parties shall remain unchanged so that the parties can be restored to the pre-contractual position.

In addition to common law, an aggrieved franchisee may resort to statutory law for rescission. In Minnesota, the franchisee may rescind a franchise contract if the franchisor violates the franchise relationship law. In particular, the franchisor's encroachment that violates the provision regarding unfair and inequitable practices will permit the franchisee to rescind a franchise contract.²⁰⁹ In this case, the franchisee must demonstrate that the franchise contract grants the franchisee an exclusive territory. The franchisee has to show that the franchisor competes with the franchisee in the exclusive territory or grants other franchisees to operate a franchised business in the territory.²¹⁰

It should be mentioned that the remedy of common and statutory rescission is not a matter of right.²¹¹ Courts will grant an order of rescission based on their discretion, considering the particulars of the case and the interest of justice.²¹² In this case, courts may deny awarding rescission of a franchise contract in several cases. For example, a franchisee may be prevented from seeking rescission because of the doctrine of unclean hands.²¹³ This maxim is said to protect the integrity of the court. Based on the court's discretion, some misbehaviors may result in the denial of equitable remedies. Those misbehaviors include fraudulent, unfair, and dishonest conduct regarding the remedial.²¹⁴ Nevertheless, the doctrine of unclean hands is an equitable defense that bars remedies in equity. The doctrine will not preclude the plain-

209 MN ST, § 80C.14(Subd.1), in conjunction with, MN ADC, 2860.4400(C).

210 *Newpaper, LLC v Party City Corp*, 2014 WL 2986653 (D Minn, 2014) 8.

211 See eg *Peck of Chehalis, Inc v C K of Western America, Inc*, 304 NW2d 91 (ND, 1981) 99; *Dr Performance of Minnesota, Inc v Dr Performance Management, LLC*, 2002 WL 31628440 (D Minn, 2002) 6, citing *Clapp v Peterson*, 327 NW2d 585 (Minn, 1982) 586.

212 See eg *Petrucelli v Palmer* 596 F Supp2d 347 (D Conn, 2009) 374; *Beaver v Inkmart LLC* 2012 WL 3822264 (SD Fla, 2012) 5; *Beck Chevrolet Co Inc v General Motors LLC* 787 F3d 663 (CA2 (NY), 2015) 680.

213 *Two Men and a Truck/International Inc v Two Men and a Truck/Kalamazoo Inc* 955 F Supp 784 (WD Mich, 1997) 785.

214 See eg *Walacavage v Walacavage* 77 A2d 723, 725, 168 Pa Super 334 (Pa Super, 1951) 338; *Mascenic v Anderson* 369 NE2d 172, 173, 11 Ill Dec 718, 719, 53 Ill App3d 971 (Ill App, 1977) 972; *Pellitteri v Pellitteri* 628 A2d 784, 788, 266 NJ Super 56 (NJ Super AD,1993) 65; *Two Men and a Truck/International* (n 213) 785; *Thompson v Orcutt* 777 A2d 670, 677, 257 Conn 301 (Conn, 2001) 310; *McKeever v Fiore* 829 A.2d 846, 852, 78 Conn App 783 (Conn App, 2003) 789.

tiff franchisee from recovering damages.²¹⁵ In other cases, courts may not award the franchisee the remedy of rescission because of the adequacy of damages. In some states, such as Michigan, courts may determine the adequacy of a remedy at law by ascertaining whether the legal remedy is complete and not doubtful and uncertain.²¹⁶

– *Effects of termination and rescission*²¹⁷

In general, termination and rescission will put an end to a franchise contract. However, the termination and rescission of a contract may differ in terms of temporal effects.

Termination of a contract will cancel a contract with a prospective effect.²¹⁸ In *DISH Network v WLAI-TV*, the court concluded that the termination would discharge all obligations that were still executory on both sides.²¹⁹ In *Anadarko Petroleum Corp*, the court elaborated that an obligation was executory on both sides if it was still unperformed by both parties or if it was something that remained to be done for both parties.²²⁰ In this case, the rights resulting from the breach or performance are still enforceable. Thus, the parties can sue the other party for enforcing any obligation accrued before the termination of the contract.²²¹ A franchise contract may play a supplementary role in determining the specific outcomes when a franchise relationship is terminated.²²² For example, the ABA's Annotated Franchise Agreement provides that the termination of a franchise agreement will not release or modify the franchisee's post-termination obligations imposed by the contract.²²³

215 See eg *Manshion Joho Center Co Ltd v Manshion Joho Center* No 114143/99, 7301, 7301A, 806 NYS2d 480, 482, 2005 NY Slip Op 09419, 2005 WL 3312624 (NYAD 1 Dept, Dec 08, 2005); *Delbuono v Clifford Development* 2007 WL 2363155 (Conn Super, 2007) 2; *Ivancicts v Griffith* 90 NE3d 641, 645, 418 Ill Dec 483, 487, 2017 IL App (4th) 170028, 642 (Ill App 4 Dist, 2017) 645.

216 See eg *Powers v Fisher* 272 NW 737, 739, 279 Mich 442 (Mich, 1937) 447; *Steggles v National Discount Corp* 39 NW2d 237, 239, 326 Mich 44 (Mi, 1949) 49.

217 Some franchise relationship states offer a franchisee the auxiliary remedies upon the cessation of a franchise relationship. These remedies will be explored in subsection 5.5.3.5 in chapter 5.

218 *CryoLife Inc v Medafor Inc* 2011 WL 13176332 (ND Ga, 2011) 5.

219 The court in *Anadarko Petroleum Corp* elaborated on this element that an obligation was executory on both sides if it was still unperformed by both parties, or was something remained to be done on both parties. See *Anadarko Petroleum Corp v Williams Alaska Petroleum Inc* 737 F3d 966 (CA5 (Tex), 2013) 971.

220 Ibid 971.

221 *CryoLife* (n 218).

222 *Napster LLC v Rounder Records Corp* 761 F Supp2d 200 (SDNY, 2011) 206.

223 Appleby and Rosario (n 200) 224. In contrast, if the franchisee rescinds a franchise contract under common law, all the post-termination agreements may cease to exist. In *Manpower v Mason*, the court provided that, if the plaintiff franchisors sought to put an end to the franchise agreements by way of rescission, the franchisors could not require the franchisees to comply with the post-termination provisions of the agreements because those clauses

Rescission of a contract will cancel the contract with a retrospective effect. In other words, the rescission will end the contract as if it does not exist in contemplation of law.²²⁴ In this case, the parties will be stored to the *status quo ante*.²²⁵ For instance, the parties have to make restitution to the other party.²²⁶ In this respect, the plaintiff franchisee may claim restitution of the money that it reasonably expended in preparing to open a franchised business under the contract so that the franchisee is placed to the *status quo ante*.²²⁷ However, an injured franchisee may be precluded from recovering damages for the franchisor's breach.²²⁸ According to the court in *Champion Windows of Chattanooga*, rescission is a remedy that no party can be held responsible for damages for breach of contract since the agreement is considered void.²²⁹

4.4.3.5 Conclusions

The remedial system in the USA is binary. The first and main source of private law remedies is common contract law. In other words, the remedies that would allow an aggrieved franchisee to enforce the franchisor's performance, claim damages, and cancel a franchise contract by way of termination and rescission are contractual remedies. When resorting to these contract law remedies, the franchisee typically needs to plead the franchisor's breach of a franchise contract. Besides the contract law relief, an aggrieved franchisee may resort to statutory remedies under franchise relationship law. These statutory remedies include injunctive relief, damages, and rescission. In claiming these remedies, an aggrieved franchisee has to demonstrate that a franchisor violates anti-encroachment or anti-competitive provisions under franchise relationship

were to be extinguished. See *Manpower Inc v Mason* 377 F Supp2d 672 (ED Wis, 2005) 679. Although the decision involves the franchisor's rescission of a franchise, I am of the opinion that the court's precedent may apply with equal force to the case of the franchisee's rescission of a franchise contract.

224 See eg *Chase Manhattan Bank, NA New York, N Y v Clusiau Sales & Rental, Inc*, 308 NW 2d (Minn, 1981) 494; *In re Graham* 430 BR 473 (Bkrtcy ED Tenn, 2010) 478; *Eden Isle Marina Inc v United States* 113 Fed Cl 372 (Fed Cl, 2013) 488–89; *Graves v Wayman* 859 NW2d 791 (Minn, 2015) 799.

225 See eg *Binkholder v Carpenter* 152 NW2d 593, 596, 260 Iowa 1297 (Iowa, 1967) 1302; *Martschinske v Olympic Styles Inc* 628 F Supp 231 (DSD, 1984) 238; *Federal Land Bank of Wichita v Krug* 856 P2d 111, 115, 253 Kan 307 (Kan, 1993) 313; *Cox v Zale Delaware Inc* 239 F3d 910 (CA7 (Ill), 2001) 914; *Petrucelli* (n 212) 375; *Bischoff v Cook* 185 P3d 902, 909, 118 Hawaii 154 (Hawaii App, 2008) 161; *Horwitz v Sonnenschein Nath and Rosenthal LLP* 926 NE2d 934, 942, 339 Ill Dec 459, 467, 399 Ill App3d 965 (Ill App 1 Dist, 2010) 973; *Damon v Groteboer* 937 F Supp2d 1048 (D Minn, 2013) 1087; *Devine v Buki* 767 SE2d 459, 465, 289 Va 162 (Va, 2015) 173.

226 See eg *Dr Performance of Minnesota* (n 211) 6; *Dunn v National Beverage Corp*, 745 NW 2d 549 (Minn, 2008) 554.

227 *Martin Investors, Inc v Vander Bie*, 269 NW 2d 868 (Minn, 1978) 876.

228 *Wong v Stoler* 188 Cal Rptr3d 674, 680, 237 Cal App4th 1375 (Cal App 1 Dist, 2015) 1385.

229 *Champion Windows of Chattanooga LLC v Edwards* 756 SE2d 314, 320, 326 Ga App 232 (Ga App, 2014) 239–40.

laws. In any case, only an award of damages is a matter of right in the US legal system. In other words, courts have discretion in decreeing specific performance and injunctions and rescinding a franchise contract.

4.4.4 Australia

4.4.4.1 Introduction

Contract law is a primary source of remedies in the event of the franchisor's failure to perform the contractual obligations.²³⁰ In this case, an aggrieved franchisee may seek the remedies of enforcement of performance, monetary compensation, and cancellation of a franchise contract under common law rules.²³¹ In some exceptional cases, which will be demonstrated later in this section, an aggrieved franchisee may seek equivalent remedies under specific legislation, including the Franchising Code of Conduct, and the Australian Consumer Law (ACL), which is incorporated in the Competition and Consumer Act 2010 (CCA).²³² This section will explore common law and statutory remedies of enforcement of performance, monetary compensation, and cancellation of a franchise contract in subsections 4.4.4.2, 4.4.4.3, and 4.4.4.4, respectively. Conclusions about the Australian remedial system will be drawn in subsection 4.4.4.5.

4.4.4.2 Enforcement of performance

In theory, an aggrieved franchisee may enforce the franchisor's performance under common law rules governing specific performance and injunctions. The franchisee may resort to remedial rules under the ACL to compel certain performance of the franchisor. The following two italicized headings will examine the enforcement of the franchisor's performance under these two legal regimes.

230 Tony D'Aloisio, 'Franchising in Australia' (1990) 58 *Antitrust Law Journal* 949, 972.

231 In Australia, the law of contract is primarily based on judge-made rules unless they are modified by statutes in some cases.

232 It should be noted that the ACL can apply to govern a franchise relationship even though a franchisee is regarded as a business consumer because the ACL does not exclusively regulate business-to-consumer relationships. As will be seen, some provisions may perfectly be applied to a franchise relationship, such as section 20 of the ACL. Furthermore, the Australian Competition and Consumer Commission asserts that a franchisor must not contravene the Australian Consumer Law's provisions. This assertion implies that the ACL will apply to a franchise agreement that would allow an aggrieved franchisee to seek private law remedies under the statute. See ACCC, 'Disclosure Obligations & COVID-19' accessed <<https://bit.ly/2Yaofn4>> 22 January 2022.

– *Specific performance and injunctions in common law*

Firstly, the franchisee may seek an order of specific performance and injunctions under common law rules. In common law, specific performance and injunctions are equitable remedies that aim at securing performance *in specie*. In general, an order of specific performance and injunctions requires proof of a breach of contract.²³³ Nevertheless, the nature of these equitable remedies differ slightly. A remedy of specific performance requires a party to perform a contract according to the terms.²³⁴ This remedy usually enforces the positive covenants of the contract.²³⁵ The remedy of injunctions not only enforces the performance of an obligation.²³⁶ But it also restrains violation of the provisions or terms of a contract.²³⁷ In this respect, the pre-existing basis for obtaining injunctive relief is not a breach of contract but interference with a legal or equitable right of the claimant.²³⁸

Granting remedies in equity is discretionary.²³⁹ In theory, an aggrieved franchisee would be constrained by several doctrines to seek a decree of specific performance or injunctions. Generally speaking, a decree of specific performance and injunctions is available only when the common law remedy of damages is inadequate.²⁴⁰ For example, in *W Hoy v WTH*, Barker J dismissed the franchisee's application for injunctive relief, reasoning that damages would provide an adequate remedy for the applicant franchisee.²⁴¹ In addition, courts may consider some discretionary factors in a denial of equitable remedies. As already mentioned in the approach in the USA, Chetwin pointed out that constant supervision of the court and a personal relationship are factors that would influence courts to deny ordering specific performance and injunctive relief.²⁴² Nevertheless, it is not always the case that courts will not grant equitable remedies in a contract of personal services. In *Imac Security Services*, Redlich J followed the authoritative decision in asserting that an injunction could be granted in a service contract where it was just in all the circumstances to do so.²⁴³

233 Carter (n 66) 923 and 933.

234 M W Bryan, V J Vann, and S Barkehall Thomas, *Equity and Trust in Australia* (2nd edn, Cambridge University Press 2017) 33; Carter, *ibid* 923.

235 *Imac Security Services Pty Ltd v Tyco Australia Pty Ltd*, [2002] VSC 592 [36].

236 Carter (n 66) 923 and 933.

237 *J C Williamson Limited v Lukey and Mulholland* [1931] 45 CLR 282, 297-298, per Dixon J.

238 *Imac Security Services* (n 235) [22].

239 Bryan, Vann, and Thomas (n 233) 38 and 47.

240 *Ibid* 43.

241 *W Hoy Pty Ltd v WTH Pty Ltd* [2018] FCA 310 [107].

242 Maree Chetwin, 'Relational and Discrete Contracts and Remedies Requiring Supervision: Same Principle?' (2014) 38(1) *University of Western Australia Law Review* 80, 89-90.

243 *Imac Security Services* (n 235) [37].

– Injunctions under the ACL

In some cases, an aggrieved franchisee may seek a statutory injunction to bar the franchisor from engaging in encroaching conduct under the ACL. As examined in chapter 3, certain conduct of a franchisor may fall within the ACL's reach.²⁴⁴ In the context of this chapter, a franchisee may seek an injunction under section 232(1) of the ACL because a franchisor engages in unconscionable conduct prohibited by section 20. Among other things, franchisor encroachment is an example of unconscionable conduct in light of section 20. In *RPR v Mar-max*, the court held that the franchisor's conduct in breach of an exclusive territory agreement would have contravened section 20 of the ACL upon the satisfaction of the following two conditions.²⁴⁵

First, an injured franchisee was at a special disadvantage in dealing with the alleged franchisor. Griffith J elaborated that a franchisee would be in the position of special disadvantage towards the franchisor if the franchisor was in a stronger bargaining position and had access to information that was not readily available to the franchisee. According to the judge, the position of special disadvantage could be implied by the *sui generis* nature of franchising relationships because these relationships were governed by the Franchising Code of Conduct.

The second condition was that the franchisor's conduct demonstrated a high level of moral obloquy. That is, the franchisor engaged in serious misconduct or conduct with a high level of moral obloquy in connection with the franchisor's breach of the duties. However, there had been no comprehensive definition of conduct with a high level of moral obloquy. Thus, an examination of the circumstances of the case was required.²⁴⁶

Despite the lack of uniform meaning, it would seem that the blatant disregard of the contractual obligations and the lack of good faith could indicate conduct with a high level of moral obloquy in the light of the ACL's provision. For example, in *ACCC v Simply No-Knead (Franchising)*, Sundberg J found that, despite the prohibition imposed by the exclusivity clause under the franchise contract, the franchisor, directly and indirectly, sold products to independent retail outlets which were located in the franchisees' territories in the manner that the franchisor must have known it would damage the franchisees. In this case, Sundberg J concluded that this practice was unconscionable as it was inconsistent with a proper relationship between the franchisor and the franchisee and showed a lack of good faith on the part of the franchisor.²⁴⁷

244 See subsection 3.4.4.2.

245 *RPR Maintenance Pty Ltd v Marmax Investments Pty Ltd*, [2014] FCA 409 [255] – [260].

246 *Ibid* [259].

247 *Australian Competition and Consumer Commission v Simply No-Knead (Franchising) Pty Ltd*, 104 FCR 253 [46].

The issuance of a statutory injunction is discretionary.²⁴⁸ Moreover, courts have discretion over the terms of the relief.²⁴⁹ In *ACCC v Chrisco Hampers Australia*, the court held that the terms of the injunctive relief could go beyond particular findings of violation and restrict the lawful conduct if the conduct was the only manner in which the public could be protected.²⁵⁰ In issuing injunctive relief, it is said that courts are not confined to traditional equity jurisdiction. In other words, courts are not restricted by equitable principles.²⁵¹ However, the court's discretion to issue a statutory injunction is by no means limitless. In many cases, courts usually consider if a grant of an injunction serves useful purposes, which other remedies cannot serve.²⁵² In particular, judges will issue an injunction if the public interest requires certain conduct to be prohibited.²⁵³ Thus, an aggrieved franchisee would struggle to convince a court to believe that the franchisor's encroaching conduct could harm the public interest.

4.4.4.3 Monetary compensation

An aggrieved franchisee may seek monetary compensation in common law and under the ACL. The following two italicized headings will examine the requirements for recovering common law and statutory damages and the principles governing the measure of damages.

– *Requirements for recovery of damages*

First of all, an injured franchisee may seek an award of damages for breach of contract. Under contract law, breach of contract includes anticipatory breach and failure to perform, which embraces non-performance, defective performance, and late performance.²⁵⁴ In the context of this chapter, a franchisee may demonstrate that a franchisor grants a franchise to another franchisee to operate a franchised business within the franchisee's exclusive territory or permit another franchisee to do some works associated with a franchise in

248 *Australian Competition and Consumer Commission v Dataline.Net.Au Pty Ltd*, [2007] FCAFC 146 [115].

249 The ACL, s. 232(4) – (7).

250 *Australian Competition and Consumer Commission v Chrisco Hampers Australia Ltd (No 2)*, [2016] FCA 144 [21].

251 *Andale Repetition Engineering Pty Ltd v Hoshizaki Lancer Pty Ltd*, [2011] VSC 496 [11].

252 See eg *Dataline.Net.Au Pty Ltd* (n 248) [114]; *Chrisco Hampers Australia* (n 250) [19].

253 *Australian Competition and Consumer Commission v Willesee Healthcare Pty Ltd* [2011] FCA 301; BC201102045 [39], citing *ICI Australia Operations Pty Ltd v Trade Practices Commission* (1992) 38 FCR 248, 255 per Lockhart J. According to the court in *Willesee Healthcare*, conduct may harm the public interest if many people can be affected by sustaining considerable loss or damage.

254 Carter (n 66) 655-57.

that territory.²⁵⁵ Moreover, a franchisee may plead that the franchisor fails to provide the franchisee with support during an ongoing business operation.

Most importantly, an injured franchisee has to show the loss or damage sustained.²⁵⁶ For instance, the franchisee may demonstrate that it suffers the loss of net profits caused by the franchisor's breach of the covenant not to compete within the exclusive territory.²⁵⁷ Additionally, the franchise must establish a causal link. That is, the aggrieved franchisee must establish that the loss or damage was caused by the franchisor's breach of the obligations. For example, the franchisee must show that the loss of net profits results from the franchisor's breaching conduct that allows another franchisee to open a franchised store within the vicinity of the franchisee's exclusive area.²⁵⁸

Secondly, an injured franchisee may seek an award of damages in the event of the franchisor's violation of section 20 of the ACL. As described in subsection 4.4.4.2(B), a franchisor may be claimed to engage in unconscionable conduct prohibited by section 20 by encroaching upon the franchisee's exclusive territory. In this case, an injured franchisee may claim statutory damages under section 236 of the ACL. In obtaining an award of damages, a claimant franchisee needs to establish a proper cause of action. Inferred from the High Court of Australia's decision in *Wardley Australia v Western Australia*, a cause of action for statutory damages consists of two elements – the contravening conduct and the loss or damage sustained.²⁵⁹

There must be a proximate cause between the contravening conduct and the loss suffered. Under section 236(1), a causal requirement is observed since the provision requires that the claimant has to suffer the loss or damage because of the conduct in contravention of the ACL.²⁶⁰ Nevertheless, it would seem that there has been no uniform theory regarding a causal nexus between the contravening conduct and the loss or damage sustained. In *Henville v Walker*, the court discussed the causation element under section 82(1) of the Trade Practices Act 1974 (Cth), which is a predecessor of section 236(1). According to the court, the common law notions of causation should not rigidly be applied without regard to the terms or objects of the Act because there could be many different kinds of contravening cases. In this respect, courts should adopt the common-sense approach, meaning one test should not be applied across the spectrum of factual situations, arising from case to case.²⁶¹

255 *Haviv Holdings* (n 67) [32].

256 *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR at 295, per Dixon J.

257 *Haviv Holdings* (n 67) [39].

258 *Ibid* [40] – [45].

259 *Wardley Australia Ltd v Western Australia*, [1992] HCA 55.

260 See eg *Marks (in a representative capacity) and Others v GIO Australia Holdings Ltd and Others* (1998) 158 ALR 333 [95], per Gummow J.

261 In this case, the court applied a material contribution test. That is, the court considered if the defendant's breach had materially contributed to the loss or damage sustained by the plaintiff. See *Henville v Walker*, [2001] 206 CLR 459 [92] – [109]. Courts in other cases

– *Principles governing a measure of damages*

In principle, common law and statutory damages are compensatory as they aim to compensate for loss or damage sustained by an injured person. In this respect, a court cannot award exemplary or punitive damages in the case of breach of contract.²⁶² Similarly, an injured party cannot recover punitive damages under the ACL. This conclusion may be implied from the court decision in *Musca v Astle Corp*. In this case, the court held that, since exemplary damages were not awarded to compensate for losses, they could not be recovered under the Trade Practices Act 1974.²⁶³ Since the Act 1974 is a predecessor of the CCA, this precedent could be followed when it comes to recovering damages under the ACL, which is part of the CCA.

A general principle of a measure of contract law and statutory damages differs slightly. In contract law, the general rule is settled; that is to say, a sum will be awarded to put the injured party in the same position as he or she would have been in had the contract been performed.²⁶⁴ Under the assessment rule, an injured party would recover damages for economic interests, including expectation and reliance loss.²⁶⁵ This principle applies to cases concerning breach of a franchise contract as well.²⁶⁶ Thus, in general, an injured franchisee would recover damages for expectation and reliance loss in the event of the franchisor's breach of the duty not to encroach and the duty to assist.²⁶⁷

In contrast, section 236 of the ACL does not indicate a general principle regarding a measure of statutory damage. Some court decisions only point out that damages under the statute are to be awarded for actual loss or damage, including economic loss and other forms of damage.²⁶⁸ Nevertheless, the High Court in *Gates v City Mutual Life Assurance Society Ltd* provided that courts might determine the proper measure of damages.²⁶⁹ Nowadays, it is said that courts should employ a unique or *sui generis* approach in assessing

may apply the 'but for' test. See *Merck Sharp & Dohme (Australia) Pty Ltd v Peterson* [2011] FCAFC 128.

262 Carter (n 66) 797.

263 *Musca v Astle Corp Pty Ltd* (1988) FCA 114 [66].

264 See eg *Wenham v Ella*, [1972] HCA 43, per Gibbs J; *Commonwealth v Amann Aviation Pty Ltd* [1991], 174 CLR 64, 98; *Darmody v National Centre Automotive* [2003] FMCA 358 [a]; *Roluke Pty Ltd v Lamaro Consultants Pty Ltd* [2008] NSWCA 323 [78].

265 Carter (n 66) 800.

266 *Haviv Holdings* (n 67) [27].

267 *Marks v GIO Australia Holdings Ltd* [1998] 196 CLR 494 [1] – [26] per Gaudron J, and [27] – [42] per McHugh, Hayne, and Callinan JJ.

268 *Wardley Australia* (n 259); *Murphy v Overton Investments Pty Ltd*, [2001] 216 CLR 388 [45] and [52].

269 *Gates v City Mutual Life Assurance Society Ltd*, [1986] HCA 3 per Mason, Wilson, and Dawson JJ.

damages.²⁷⁰ This idea was discussed by Gaudron J in *Marks v GIO Australia Holdings Ltd*. According to Gaudron J, the basis for considering the remedy of damages under section 82 of the TPA, a predecessor of section 236 of the ACL, was not confined by analogy to either actions in contract or tort. Instead, the relief was for an applicant who established what he/she had lost. Once a causal nexus between the loss or damage and the contravening conduct was established, the damages for the amount of the loss should be recoverable and not be limited to the concepts of the law of contract, tort, or other equitable remedies.²⁷¹

4.4.4.4 Cancellation of a franchise contract

Cancelling a franchise agreement can be done in several ways. An aggrieved franchisee may utilize the rights under a franchise contract and contract law to terminate a franchise contract. In the absence of these rights, the franchisee may resort to the rules of the Code to terminate a franchise agreement and the rule of the ACL to rescind a franchise agreement. This subsection will deal with these mechanisms and review the effects of the termination and rescission of a franchise contract in the following four italicized headings.

– Contractual right to terminate

A franchise agreement may provide an aggrieved franchisee with the right to terminate. In some exceptional cases, the terms of a franchise agreement for a definite term may permit a franchisee to terminate a franchise relationship under certain circumstances. For example, a franchise agreement in *Swim Loops* shows that a franchisee may terminate the contract on the condition that the franchisee substantially complies with the contract and the franchisor breaches a material and fundamental term of the contract. However, under the contract, the franchisee must allow the franchisor to cure the breach within one month after written notice of the breach is lodged.²⁷² A franchisee may conveniently terminate a franchise contract for an indefinite period by giving a franchisor notice of termination. For instance, in *Freier v Australian Postal Corporation (No 2)*, a franchisor or a franchisee may terminate a franchise agreement without cause by giving the other party ninety-day prior written notice.²⁷³

270 David D Knoll, 'Assessing commercial losses in private trade practices litigation' (2002) 10 Competition & Consumer Law Journal 1, 2.

271 *Marks* (n 267) [1] – [26] per Gaudron J. Some courts provided that damages under the ACL may coincide with those recoverable in tort actions. See *Kenny & Good Pty Ltd v MGICA (1992) Ltd*, 199 CLR 413 [125] – [131]. This court decision demonstrated that damages would cover only reliance loss.

272 *H20 Learning Pty Ltd v Swim Loops Pty Ltd (t/as Jump Swim Schools)*, [2019] NSWDC 165 [44].

273 *Freier v Australian Postal Corporation (No 2)* [2012] NSWSC 61 [4].

In this case, the franchisee may exercise the right to terminate the agreement following the terminating requirement.

– *Common law right to terminate*

Despite the absence of the contractual right to terminate, an aggrieved franchisee may cancel a franchise contract by way of termination under common contract law rules. In this case, the franchisee's common law right to terminate depends upon the term of a franchise agreement. If a franchise contract is concluded for an indefinite term, it could be said that the contract can be terminable upon reasonable notice. In this case, the franchisee does not need a ground for terminating a franchise contract. Nevertheless, the franchisee may terminate a perpetual franchise contract only after a reasonable period has ended.²⁷⁴ Conversely, the franchisee may terminate a fixed-term franchise agreement insofar as it has grounds for termination. Under Australia's contract law, a promisee is entitled to terminating a contract for the following three grounds: (1) a repudiation and an anticipatory breach of contract, (2) a breach of conditions, and (3) a sufficiently serious breach of intermediate terms.²⁷⁵

Firstly, an aggrieved franchisee may terminate a franchise agreement for the franchisor's anticipatory breach of contract. In this respect, the terminating franchisee has to show the franchisor's repudiation of a contract that precedes the time of performance.²⁷⁶ In doing so, the franchisee may demonstrate the franchisor's serious lack of readiness and willingness to perform its contractual obligations. In this case, the franchisee may refer to words or conduct that amounts to the franchisor's refusal to perform or a sufficiently serious prospective breach. Alternatively, the franchisee may show the franchisor's repudiation by referring to its actual inability to perform, although it does not necessarily amount to anticipatory breaching conduct.²⁷⁷

Secondly, an aggrieved franchisee may terminate a franchise contract for the franchisor's breach of a condition or an essential term.²⁷⁸ In practice, an essential term can be established in several ways. For example, the contract term is regarded as a condition if it is vital to the promisee in the sense that the promisee would not have entered into the contract unless the promisee

274 *Crawford Fitting Co v Sydney Valve & Fittings Pty Ltd* [1988] 14 NSWLR 438.

275 *Carter* (n 66) 655.

276 *Ibid* 686-87.

277 *Ibid* 688.

278 The franchisee may terminate the agreement for breach of a condition without having to show that the breach is sufficiently serious. This statement is inferred from the decision in the case *VIP Home Services*. According to the court in this case, if the clause of a franchise contract is considered a condition, any breach of the provision will give rise to the franchisee's right to terminate the contract, regardless of whether there is any loss caused to the franchisee. See *VIP Home Services (NSW) Pty Ltd v Swan*, [2011] 110 SASR 157 [45].

had been assured of strict compliance of the term, and this fact should have been apparent to the promisor as well.²⁷⁹ In this regard, the franchisee may satisfy the essentiality test by showing that the franchisee would not have entered into a franchise contract if the franchisee is not assured of the provision of the franchisor's assistance in a franchised business operation. The contract term is regarded as a condition if the promisor's failure to perform will bring about serious consequences to the promisee.²⁸⁰ In this respect, the franchisee may terminate a franchise agreement by arguing that the franchisor's encroaching practices in the franchisee's exclusive territory would cause a substantial reduction in profits.

Thirdly, an aggrieved franchisee may terminate a franchise contract for the franchisor's breach of an intermediate term.²⁸¹ In terminating a contract for a breach of an intermediate term, the franchisee may have to demonstrate the seriousness of the breach. That is, the franchisee must show that it was deprived of substantially the whole benefit which it was intended that the franchisee should obtain from the contract.²⁸² A question of whether the breach is sufficiently serious is a matter of fact. In the context of this chapter, the franchisee has the onus of proving that the franchisor's breach of the duties is serious. For example, the franchisee may demonstrate that the franchisor has committed a prolonged breach of the assistance obligation by failing to provide ongoing support, which would make the franchisor's performance substantially different from what was intended under the contract.²⁸³ The franchisee may argue that the franchisor's encroachment upon the exclusive area has substantially deprived the franchisee of incomes that were expected at the time of concluding a franchise agreement.

– *Statutory termination and rescission*

Firstly, an aggrieved franchisee may terminate a franchise agreement in a cooling-off period. Under the Code, clause 26(1) permits the franchisee to terminate a franchise agreement within 14 days after entering into the agreement. Exercising the franchisee's cooling-off right of termination seems to be desirable for a franchisee since the franchisee can exercise the right for any or no reason. That is, there is no need for the franchisee to insist that the franchisor violates the rules of the Code or breaches a franchise contract.

279 *Luna Park (NSW)* (n 256) per Jordan CJ.

280 *Carter* (n 66) 679-80.

281 The contract term is an intermediate term if it remains essential to the contract as a whole even though the term is not considered a condition. For example, in the case *VIP Home Services*, the court construed that the clause regarding the franchisor's obligation to allocate customers was an intermediate term. See *VIP Home Services (NSW)* (n 278) [48] – [49].

282 *Ibid.*

283 This example is made by way of analogy to the reasoning of the court in the case *VIP Home Services*. See *VIP Home Services (NSW)* (n 278) [52].

However, the franchisee has to ensure that it terminates a franchisee agreement within a 14-day period. For example, suppose a franchise contract requires a franchisor to provide a franchisee with a training session on the seventh day after concluding the contract, and the franchisor fails to do so. In this case, the franchisee would have seven days to exercise the right to terminate in a cooling-off period if the franchisee wants to exit the relationship with the franchisor.

If a cooling-off period mentioned above has lapsed, an aggrieved franchisee may terminate a franchise agreement through the process of proposing to terminate. Under the Code, clause 26B(1) permits a franchisee to give a franchisor at any time a written proposal for termination of a franchise agreement on the terms specified in the proposal, despite the agreement. If the franchisor is given the written proposal for termination, clause 26B(2) requires the franchisor to give the franchisee a written response to the proposal within 28 days. In this written response, the franchisor may, albeit improbably, agree to the terms specified in the franchisee's proposal and have the agreement terminated.

Secondly, an aggrieved franchisee may acquire an order of rescission if the franchisor violates the ACL's provisions. As examined earlier in this section, the franchisor may engage in unconscionable conduct in violation of section 20 of the ACL by encroaching upon the franchisee's exclusive territory. In this case, the franchisee may ask a court to make an order that rescinds a franchise contract under section 238(1), in conjunction with section 243(1)(a). In obtaining an order of rescission, the franchisee has to plead that it has suffered, or is likely to suffer, loss or damage because of the franchisor's unconscionable conduct. For instance, the franchisee may have to show that it has suffered or is likely to suffer the financial loss of profits because the franchisor unconscionably encroaches upon the franchisee's exclusive territory.

Despite satisfying the requirements mentioned above, a court will have a wide discretionary power in making a remedial order.²⁸⁴ According to section 238(1), in conjunction with section 243(1)(a)(i), a court may declare a franchise contract to be void if the court thinks it appropriate against the franchisor who engages in the contravening conduct. In making an order of rescission, the court will have to consider that the order can compensate the injured franchisee in whole or in part for the loss or damage or prevent or reduce the loss or damage.²⁸⁵ Thus, the franchisee needs to convince the court that an order of rescission is an appropriate remedy for redressing the franchisee's loss or damage caused by the franchisor's unconscionable conduct.

284 *Kizbeau Pty Ltd v WG & B Pty Ltd*, [1995] HCA 4 [35].

285 The ACL, s. 238(2).

– *Effects of termination and rescission*²⁸⁶

The effects of termination in common contract law and statutory termination and rescission may differ in some cases. In contract law, termination of a contract will discharge the parties from the contract *in futuro*. According to Dixon J in *McDonald v Dennys Lascelles Limited*, when a party elects to terminate a contract for a breach, the termination will take effect from the time of election or the exercise of the right to terminate. Thus, the franchisee's termination of a franchise contract in contract will end a franchise relationship from the time of termination. In this respect, the rights and obligations which arise from the partial execution of the contract and the right to damages which has accrued from the breach continue unaffected.²⁸⁷

Conversely, the franchisee's termination of a franchise agreement in a cooling-off period under the Code will require the franchisor to repay all the payments made by the franchisee to the franchisor connected to the agreement.²⁸⁸ This requirement suggests that the termination has a retrospective effect. Rescinding a franchise contract under the ACL may also have a retrospective effect. According to para (a)(ii) of section 243 of the ACL, a court has the power to declare a contract, in whole or in part, to be void *ab initio*.²⁸⁹ As a result, the rescission will require *restitutio in integrum*; that is to say, each party must be restored in the position which the party occupied before the contract was concluded. In this case, the court also has the power to decide what is just in the case of restoration.²⁹⁰

4.4.4.5 Conclusions

Australia has a dual system of private law remedies. Primarily, common contract law supplies remedial rules that permit an aggrieved franchisee to seek specific performance and injunctive relief, damages, and termination of a franchise contract. In seeking these contract law remedies, the franchisee usually has to demonstrate that the franchisor breaches a franchise contract by failing to perform the duty not to encroach or the duty to assist promised under the contract. Additionally, some statutory statutes may offer an aggrieved franchisee a set of private law remedies. As can be seen, the franchisor's failure to perform its obligations, particularly the duty not to encroach, may amount to unconscionable conduct prohibited by the ACL. In this case,

286 The termination of a franchise agreement may render the franchisee the right to specific remedies under the agreement. These special remedies will be discussed later in subsection 5.5.4.5 in chapter 5.

287 *McDonald v Dennys Lascelles Limited* [1933] HCA 25; 48 CLR 457, 476-77.

288 The Code, cl. 26(3).

289 Alternatively, a court may declare the whole or part of the contract to be void at all times on and after the specified date before the date on which the order of rescission is made.

290 *AH McDonald & Co Pty Ltd v Wells*, [1931] HCA 24, per Rich, Starke, and Dixon JJ.

if the franchisee successfully establishes the franchisor's unconscionable conduct, the franchisee may seek an order of injunctions, damages, and rescission of a franchise contract under the ACL. However, in seeking an order of damages and rescission, the franchisee also has to show its actual or potential loss caused by the franchisor's contravening conduct.

4.4.5 Comparative analysis

4.4.5.1 Introduction

In the case of the franchisor's non-performance of the duty not to encroach and the duty to assist, the descriptive examinations show that the DCFR, the USA, and Australia provide legal mechanisms that allow an aggrieved franchisee to compel the franchisor's action or inaction, claim damages, and cancel a franchise contract. Nevertheless, the remedial rules governing these three remedies may converge and diverge. Subsection 4.4.5.2 will examine the remedial rules under the franchise legal framework of the selected legal systems to draw similarities and differences to put forward the proposals for constructing comprehensive franchise law's remedial system. Concluding remarks on the characteristics of the remedies and key recommendations will be provided in subsection 4.4.5.3.

4.4.5.2 Comparison and analysis

– Enforcement of performance

(1) Similarity

The DCFR, the USA, and Australia are similar in that their general contract law rules permit an aggrieved franchisee to seek a remedy of enforcement.²⁹¹ Under the chosen legal systems, the franchisee may, in theory, seek a remedy of enforcement to compel the franchisor to perform the duty not to encroach and the duty to assist.²⁹² In compelling the franchisor's performance, the selected legal systems generally require the franchisee to plead that the franchisor does not comply with the franchise contract's term that requires the franchisor not to cannibalize the franchisee's franchised business or to train and assist the franchisee in operating a franchised business. In short, the

²⁹¹ The phrase 'remedy of enforcement' will be used as a generic term to cover various types of private law mechanisms that aim at enforcing the performance *in specie* of the debtor or the promisor under the selected legal systems. Strictly speaking, the remedy of enforcement intends to include the right to enforce performance under the DCFR and an equitable remedy of specific performance and injunctions available in America and Australia.

²⁹² See subsections 4.4.2.2, 4.4.3.2, and 4.4.4.2.

franchisor's failure to perform the obligations is a common requirement of the remedy of enforcement under the DCFR, the US, and Australian legal systems.

(2) *Difference*

Despite the convergence mentioned above, the USA and Australia differs from the DCFR in the following two cases.

First, it is unlikely that an aggrieved franchisee succeeds in obtaining the remedy of enforcement in the USA and Australia. This prognosis is based on the fact that specific performance and injunctions in these two common law countries are considered equitable and discretionary remedies. In general, courts usually consider some equitable considerations, such as a burden of courts to supervise the performance and a character of personal service contracts, before deciding whether to order the equitable relief. In practice, these legal considerations typically bar the courts from issuing equitable remedies, thereby awarding damages instead. Conversely, granting specific performance under the DCFR is a matter of right. Thus, the general consideration of the issuance of specific performance is contradictory. Upon the franchisee's satisfaction of certain requirements, a court will have no choice but to order the franchisor to perform the contractual duties unless the franchisor can prove for exceptions from liability.²⁹³

Second, in the USA and Australia, franchisor encroachment may permit an aggrieved franchisee to resort to a statutory remedy that enforces the franchisor's action or inaction.²⁹⁴ In America, franchisor encroachment is regulated by the franchise relationship law of Hawaii, Indiana, Iowa, Minnesota, and Washington. Under the franchise statute of four jurisdictions, the franchisee may bring a legal action for injunctive relief, claiming that the franchisor violates the rules prohibiting the franchisor's encroaching conduct. In Australia, although the Franchising Code of Conduct does not regulate franchisor encroachment particularly, the franchisee may seek a decree of injunctions under the Australian Consumer Law (ACL) by claiming that the franchisor's encroaching practices is unconscionable or misleading conduct prohibited by the ACL. Despite the availability of the statutory remedy under the two countries, the franchisee would be constrained to seek an injunction under the statutes since the issuance of a statutory injunction is discretionary. Therefore, courts will ordinarily have discretion whether to order an injunction in the case at hand.

²⁹³ However, this advantage does not infer that the franchisee will always pursue the remedy of enforcement as a first resort. Several factors may prevent the franchisee from seeking this remedy. For example, the franchisee may not want to enforce the franchisor's performance as it lost faith in the franchisor because of the franchisor's failure to perform obligations.

²⁹⁴ See subsections 4.4.3.2 and 4.4.4.2.

(3) *Discussion*

As can be seen from the comparison, contract law will primarily provide mechanisms for an aggrieved franchisee to enforce the franchisor's performance of the duty not to encroach and the duty to assist. However, from my perspective, the franchisee would suffer some shortcomings when having recourse to contract law rules under the chosen legal systems. In particular, the drafters of the DCFR and the US and Australian courts, would agree that the remedy of enforcement is not an appropriate remedy in the case of the franchisor's non-performance of the duty not to encroach because of certain legal constraints.

To illustrate, Company A, a franchisor, concludes a franchise contract with Robin, a franchisee. Under the contract, Company A agrees that Robin is granted an exclusive right to operate a restaurant franchise in the city of Leiden. Company A also agrees that it will not open a company-own restaurant or license other franchisees to open franchise outlets within an exclusive territory of Robin. Nevertheless, several years later, Robin finds out that Company A has opened a franchise restaurant on Willem de Zwijgerlaan and licensed Emma to open a franchise restaurant on Breestraat; both new outlets are located in Leiden.

According to the illustrative case, it is unlikely that Robin warrants an order of specific performance under the contract law rules of the DCFR, the USA, and Australia. Under the DCFR, Company A may argue for an exception to an order of specific performance. That is, Company A could argue that it would be burdensome and expensive to shut down a franchise business or break a franchise agreement with Emma in order that Emma ceases the operation of a franchised store. Likewise, the US and Australian courts would not order specific performance or injunctions against Company A because the courts would consider that a remedy of damages is an adequate remedy under the circumstances. The courts would be unwilling to constantly supervise whether Company A acts in accordance with the courts' decree. In the end, Robin could not enforce Company A to comply with what the company has promised under a franchise agreement under the selected legal systems.

It should be noted that the aggrieved franchisee remains entitled to recover damages despite the unlikelihood of securing a remedy of enforcement. Under the selected legal systems, the franchisee would conveniently seek an award of damages in the case of the franchisor's non-performance of the duty not to encroach because it is a matter of the franchisee's right in that case. In my opinion, the remedy of damages would suitably protect the franchisee's interests associated with the exclusive right. From a commercial perspective, granting a franchisee the exclusive right and territorial protection usually aims at enabling a franchisee to maximize greater profitability. In light of the exclusivity, the franchisee would expect its investment to be recouped more rapidly by boosting profits from operating a franchised business. In this case, the franchisor's non-compliance of the exclusivity provision, as is in the hypo-

thetical situation, typically inflicts measurable, pecuniary losses to the franchisee, such as the lost profits. In this sense, monetary compensation in the form of damages would effectively redress the franchisee's damage, compared to enforcement of performance.

From a franchisee's viewpoint, however, an award of damages may not always produce a satisfactory outcome. In some cases, enforcement of performance *in specie* would do more justice for an aggrieved franchisee than damages. For example, the remedy of enforcement may be argued to enable an aggrieved franchisee to obtain the franchisor's initial and ongoing assistance necessary for the operation of a franchised business. Assume that, under a franchise contract, a franchisor promises to help a franchisee select a location of a franchised business operation and provide a franchisee with training programs and operational manuals at specified dates. In this case, it would be unfair for the franchisee if the franchisor could avoid its commitment despite the fact that the promise can practically be fulfilled. Thus, the franchisor should be compelled to render the franchisee with the promised forms of support.

Based on the reason mentioned above, I suggest that comprehensive franchise law contains the remedial system that offers an enforcement mechanism for an aggrieved franchisee to acquire the franchisor's performance of obligations where it is doable. This enforcement mechanism should be a matter of the right of the franchisee. For example, as proposed in subsection 4.3.5.2, comprehensive franchise law should contain the rule that requires the franchisor to provide the franchisee with (1) initial or preopening assistance, (2) ongoing assistance, and (3) special assistance.²⁹⁵ In this case, if the franchisor fails to provide the franchisee with the assistance required by the rule, the franchisee should be able to compel the franchisor's performance regardless of courts' discretion.

Comprehensive franchise law may introduce exceptions in that the franchisor cannot be forced to perform obligations. Inspired by the DCFR, the franchisor may be exempted from carrying out duties if it would be unlawful or unreasonably burdensome for the franchisor to do so. For instance, the franchisor may argue that it would be unreasonably burdensome to take down the whole franchised unit established in violation of the anti-encroachment provision. Besides, the franchisor may be exempted from performing obligations that the franchisor has to perform personally. For example, the franchisor may not be compelled to render the franchisee with forms of support that are not assignable by nature. In any event, if the remedial regime embraces these exceptions, it should ensure that the franchisee is not precluded from resorting to other remedies, particularly money damages.²⁹⁶

²⁹⁵ See subsection 4.3.5.3.

²⁹⁶ See subsection 4.4.2.2.

– *Monetary compensation*

(1) *Similarity*

Under the DCFR, the US, and Australian legal systems, an aggrieved franchisee may claim monetary compensation in the form of contract law damages. The requirements for recovering damages under contract law of the selected legal systems are relatively similar.²⁹⁷ Principally, the injured franchisee has to plead that a franchisor fails to perform obligations under a franchise agreement that causes the loss or damage to the franchisee. For example, the franchisee may show that the franchisee suffers damage because the franchisor encroaches upon the franchisee's exclusive territory or fails to provide the franchisee with a training program necessary for the operation of a franchised business. Besides, the franchisee needs to demonstrate a causal connection between the franchisor's breaching conduct and the loss or damage sustained.

The contract law principles governing a measure of damages are also comparable.²⁹⁸ Under the chosen legal systems, an award of damages aims to compensate for any loss or damage sustained by an injured party. Accordingly, an injured franchisee will not be able to claim punitive damages that intend to punish the franchisor's non-compliance with contract terms. In addition, a general principle of assessing damages of the DCFR, the USA, and Australia similarly permits an aggrieved franchisee to recover damages for the loss of expectation interests, such as the lost incomes or profits.

(2) *Difference*

The USA and Australia differ from the DCFR in that an injured franchisee may resort to statutory damages for actual loss in the case of franchisor encroachment. In America, the franchise relationship law of Hawaii, Indiana, Iowa, Minnesota, and Washington specifically regulate franchisor encroachment.²⁹⁹ In the event of the franchisor's contravention of the regulation, the injured franchisee may claim damages caused by the franchisor's contravening conduct. For example, the franchisee may claim damages if the franchisor sells its products in the vicinity of the franchisee's exclusive territory. Likewise, in Australia, the franchisor's encroaching conduct will allow the franchisee to seek an award of damages under the ACL. Nevertheless, Australia relatively differs from the USA in that the franchisee needs to convince a court to believe that the franchisor's encroachment amounts to unconscionable conduct prohibited by the ACL. This requirement results from the fact that the Franchising Code of Conduct does not explicitly bar the franchisor from cannibalizing upon the franchisee's franchised business.

²⁹⁷ See subsections 4.4.2.3, 4.4.3.3, and 4.4.4.3.

²⁹⁸ See subsections 4.4.2.3, 4.4.3.3, and 4.4.4.3.

²⁹⁹ See subsection 4.4.3.3.

In terms of recoverable damages, the USA shows a noticeable contrast to Australia in that punitive damages can be recovered. In two relationship states – Hawaii and Washington – courts have the power to award the amount not to exceed three times the actual damages suffered by a plaintiff franchisee. In short, courts may award punitive damages in the form of treble damages. This rule would allow the judges to consider awarding damages to suit the quantum of the franchisor's guilt in each individual case. Unlike the USA, in Australia, the ACL does not permit the recovery of the like-damages. Thus, in Australia, the franchisee will only recover compensable damages for the actual loss suffered. In other words, the franchisor will never be punished with the considerable amount of exemplary damages.

(3) *Discussion*

In some cases, an aggrieved franchisee may find a remedy of damages desirable in the event of the franchisor's non-performance of the obligations. For example, an aggrieved franchisee may suffer financial loss since the franchisor's encroaching conduct leads to a reduction in revenues from operating a franchised business in an exclusive area. The franchisee may incur unnecessary expenses as it has to seek assistance from third persons to fix technical problems. However, this assistance was supposed to be provided by the franchisor under a franchise agreement. In these illustrative situations, monetary compensation would do justice and redress the franchisee's disadvantaged conditions. Therefore, it is recommended at the outset that a remedy of damages should be made available for an injured franchisee in the case of the franchisor's breach of a franchise contract by failing to perform the duty not to encroach and the duty to assist.

From the comparison, a remedy of damages can be sought under contract law; an injured franchisee may recover damages on the basis of non-performance of an obligation under the DCFR or breach of contract under the US and Australian laws. From a theoretical perspective, resorting to contract law for damages would benefit the franchisee in that damages are considered a primary remedy in contract law. In either civilian jurisdictions or common law countries, a remedy of damages is the right of an injured party; hence, seeking damages will typically not be subject to various constraints, as is seen in the US and Australian legal systems. Besides, the franchisee will benefit from making use of contract law rules in that the franchisee will be permitted to recover damages for not only expenditure incurred but also expectancy losses. In particular, in the event of franchisor encroachment, the franchisee will be able to claim damages for lost profits that the franchisee could legitimately expect at the time of concluding a franchise contract.

Despite the advantages, claiming contract law damages would be unfeasible in several situations. The first and simplest case is that an injured franchisee cannot claim damages if a franchisor is not bound by contract terms not to cannibalize upon the franchisee's marketing territory or to assist and support

the franchisee in operating a franchised business.³⁰⁰ The occurrence of these circumstances may result from an intrinsic feature of a franchise relationship that a franchisee usually lacks sufficient bargaining power to induce a franchisor to incorporate a franchise contract's provisions establishing the franchisor's duty not to encroach and the duty to assist.³⁰¹ In my view, if the franchisee has no power to bargain for the incorporation of the protective terms, the franchisee should leave the negotiation in the first place. This suggestion would be highly practical if comprehensive franchise law also contains pre-disclosure rules that enable the franchisee to conduct pre-contractual due diligence that could minimize the risk of potential losses in running a franchised business.³⁰²

An injured franchisee may also not fail to demonstrate the damage suffered. In some cases, an aggrieved franchisee may be unable to materialize the loss or damage in money terms. For example, the franchisee may find it difficult to show that the franchisor's failure to assist causes the franchisee to lose the ability to operate a franchised unit profitably. In other cases, the franchisee may not show a connection between the franchisor's breaching conduct and the loss sustained. For instance, the franchisee may not recover damages for the lost chance to generate income because the franchisee may not connect the loss with the franchisor's placement of another franchised unit in the franchisee's exclusive location. The franchisee may also struggle to prove that sunk investment costs are losses recoverable under the law. In these cases, the franchisee would eventually lose a claim for damages or only receive a tiny sum that cannot even redress the smallest amount of loss.³⁰³

300 In other cases, the franchisee may simply not find proof of the franchisor's promise to do so, as the franchisee does not keep good records of the franchisor's promises.

301 This phenomenon undergirds the proposals for legislative intervention to create the franchisor's duties under comprehensive franchise law. See subsections 4.2.5.3 and 4.3.5.3.

302 The pre-contractual information rules are proposed in chapter 3. Under the rules, a prospective franchisee can explore what obligations the franchisor commits under a proposed franchise agreement and assess the franchisor's ability to perform its obligations. Furthermore, a prospective franchisee can consult or talk to current or former franchisees to ask for some information about the franchisor's compliance with a franchise agreement. These opportunities are said to be the key steps in purchasing a franchise. See Australian Competition & Consumer Commission, 'ACCC finds food franchisors not disclosing critical information' (Media release, 27 August 2019) <<https://bit.ly/2Lk7pYL>> accessed 22 January 2022.

303 For example, in the USA, it is accepted that a court has the power to award nominal damages in the case a plaintiff cannot prove actual damages from a breach of a contract or demonstrate proximate causation between the breach and the loss suffered. See eg *Nathan v Tremont Storage Warehouse*, 102 NE 2d 421, 423, 328 Mass 168 (Mass 1951) 171; *Kronos v AVX Corp*, No 49, 81 NY 2d 90, 95, 612 NE 2d 289, 292, 595 NYS 2d 931, 934, 1993 WL 93478 (NY, Apr 01, 1993); *Stromberger v 3M Co*, 990 F 2d 974 (CA7 (Ill), 1993) 976; *Boston Property Exchange Transfer Co v Iantosca*, 720 F 3d 1 (CA1 (Mass), 2013) 11. In many cases, a plaintiff will be awarded nominal damages of only \$1. See eg *Simpkins v Ryder Freight System, Inc*, 855 SW2d 416 (Mo App WD 1993) 423; *Coca-Cola Bottling Co of Elizabethtown*,

Additionally, franchise-specific legislation may regulate the franchisor's conduct and offer the franchisee an opportunity to seek an award of statutory damages. This approach can be seen in the five US relationship states. In those states, the franchise relationship laws regulate the franchisor's encroachment and provide an injured franchisee with the right to bring an action for damages in the event of the franchisor's contravention of the rules. From my viewpoint, resorting to statutory damages would benefit the franchisee in that the franchisee does not have to plead that the franchisor owes the franchisee any obligation that will be a basis for recovering contract law damages. Thus, I suggest that comprehensive franchise law not only regulates the franchisor's duties, but the law also provides an injured franchisee with the right to claim damages caused by the franchisor's non-performance of the obligations.

I also recommend that comprehensive franchise law further elaborates on a general principle concerning a measure of damages. As can be seen, the US and Australian statutory regimes do not clarify any measure of damages, leaving for courts to find a proper assessment in individual cases. This obscure standard would create uncertainty that would frustrate the franchisee's effort to structure a claim for damages. Nevertheless, the remedial system may utilize several approaches to define what type of loss or damage is recoverable under the law and exhibit a standard for measuring damages for such loss or damage. In this respect, the DCFR would be an excellent example in that it clarifies both the standard for assessing damages and the recoverable loss under the DCFR.³⁰⁴ Formulating these principles would make a remedy of damages under comprehensive franchise law a franchisee-friendly remedy. In any case, calculating damages will be quantified on a case-by-case basis.

– *Cancellation of a franchise contract*

(1) *Similarity*

The DCFR, the USA, and Australia similarly provide mechanisms that permit an aggrieved franchisee to end a franchise relationship if it is necessary for the franchisee to do so. Under the selected legal systems, the first and foremost source of power to cancel a franchise relationship is a franchise agreement.³⁰⁵ Ordinarily, a franchise contract contains a provision that allows the franchisee to terminate the contract. Under the chosen legal systems, the franchisee usually is permitted to exercise the right to terminate in the case of the franchisor's material breach of a franchise contract. In addition, an aggrieved franchisee may resort to contract law rules to terminate or rescind a franchise contract, particularly a franchise contract with a fixed period. In this case, the

Inc v Coca-Cola Co, 988 F2d 386 (CA3 (Del), 1993) 391; *Norman v Elkin*, 849 F Supp 2d 418 (D Del, 2012) 420.

³⁰⁴ See subsection 4.4.2.3.

³⁰⁵ See subsections 4.4.2.4, 4.4.3.4, and 4.4.4.4.

grounds for terminating or rescinding the agreement are relatively similar. Under the DCFR, the franchisee may terminate a franchise contract in the case of the franchisor's substantial non-performance of an obligation and anticipated non-performance of an obligation. In the USA and Australia, the franchisee may rescind or terminate a franchise contract for the franchisor's anticipatory and material breach of a franchise contract.

(2) *Difference*

Unlike the DCFR, the USA and Australia provide a statutory basis for an aggrieved franchisee to rescind or terminate a franchise contract. In the case of franchisor encroachment, the US state of Minnesota's franchise relationship law permits a franchisee to bring a claim for rescinding a franchise agreement in the case of the franchisor's contravention of the rule regulating franchisor encroachment. In Australia, the franchisee may choose to terminate a franchise agreement for any or no reason in a cool-off period prescribed by the Australian Franchising Code of Conduct. Although the period has expired, the franchisee may propose to terminate a franchise contract, and the contract will be terminated provided that the franchisor concurs. An aggrieved franchisee may obtain an order of rescission by a court under the ACL, which is not franchise-specific law. In this case, however, the franchisee needs to establish the franchisor's unconscionable or misleading conduct.

(3) *Discussion*

A remedy that permits the cancellation of a franchise contract, either by termination or rescission, would be vital for an aggrieved franchisee in several ways. First, the remedy of cancellation of a franchise contract permits the franchisee to leave a broken relationship. In some cases, the franchisor may commit a breach of trust by deliberately encroaching upon the franchisee's exclusive territory in a manner prohibited by a franchise contract or failing to render a series of assistance throughout a franchise relationship. In these situations, the franchisee's trust would irreparably be destroyed, and breaking away from a franchise relationship would be a panacea. The remedy of cancellation of a franchise contract would prevent the franchisor's unjust enrichment. That is, the franchisee's cancellation will cut ties with the franchisor and discharge the franchisee from performing outstanding obligations that would unjustly benefit the franchisor. For example, the franchisee will be released from paying future fees or royalties due to the cancellation.

From the comparison, a remedy of cancellation by termination or rescission is contractual. The franchisee ordinarily has to resort to either the franchise contract terms or general contract law rules for terminating or rescinding a franchise agreement. In both cases, not only is typically the franchisee required to prove the franchisor's non-performance of an obligation or breach of contract. The franchisee also has to demonstrate that the franchisor's non-performance or breach is serious enough in the sense that locking the parties into a

franchise contract is no longer desirable. From the descriptive sections, the DCFR requires that the franchisor's non-performance of an obligation is fundamental. Likewise, the US and Australian contract laws require that the franchisor's breach of a franchise contract is material. From a procedural standpoint, the franchisee would be restrained from cancelling a franchise agreement.

Nevertheless, a remedy of cancellation of a franchise contract can be statutory; an aggrieved franchisee may statutorily terminate a franchise agreement in a cooling-off period under the Australian Franchising Code of Conduct. Moreover, the franchisee may seek a court order of rescission under specific statutes, such as Minnesota's franchise relationship law and the Australian Consumer Law (ACL). Under the laws, the franchisee commonly needs to plead that the franchisor violates legal provisions regulating the franchisor's conduct, such as encroaching or unconscionable conduct. In my view, from a procedural viewpoint, seeking an order of statutory rescission would be helpful for an aggrieved franchisee in that the franchisee generally does not have to prove that the franchisor's violation is fundamental material. In other words, the franchisee needs not demonstrate that the franchisor's violation substantially destroys the foundation of a franchise contract.

As mentioned earlier in this discussion, a remedy of cancellation will allow the franchisee to leave the franchise relationship when the loss of trust is not curable. From an economic perspective, this allowance would help the franchisee achieve economic efficiency because the franchisee will have an opportunity to start a new franchise relationship with other franchisors. In other words, the franchisee can find the right partner that will cooperate with the franchisee in generating revenue from a franchised business operation. Thus, I suggest that comprehensive franchise law provides a mechanism that allows an aggrieved franchisee to cancel a franchise contract, particularly in the case of violation of the rules regulating the franchisor's obligations. Furthermore, the law should elaborate on the requirements for cancelling a franchise contract so that the franchisee can be aware of preconditions for seeking the remedy.³⁰⁶

4.4.5.3 Conclusions

– Concluding remarks

The comparative examination of the franchise legal framework of the DCFR, the USA, and Australia shows that an aggrieved franchisee can seek three contract law remedies – enforcement of performance, damages, and cancellation of a contract. In doing so, the franchisee typically has to establish the franchisor's non-performance of the duty not to encroach and the duty to assist.

³⁰⁶ The franchisee's rights to terminate a franchise agreement will extensively be discussed in chapter 5.

Nevertheless, the franchisee may be constrained to seek the remedies in contract if a franchise contract does not obligate the franchisor to perform these obligations. The comparative examination also reveals that the five US states and Australia offer the remedies under specific statutes that permit an aggrieved franchisee to seek remedies of enforcement, damages, cancellation of a contract. The franchisee may have to plead that the franchisor's conduct contravenes the statutory rules that provide a basis for seeking the three statutory remedies.

– *Key recommendations*

(1) *Remedial system*

Comprehensive franchise law should establish the remedial system constituting legal mechanisms for an aggrieved franchisee to utilize in the event of the franchisor's contravention of the rules regulating the franchisor's duty not to encroach and the duty to assist. Under the remedial regime, an aggrieved franchisee should be allowed to seek the enforcement of performance, recovery of damages, and cancellation of a franchise contract.

(2) *Enforcement of performance*

The remedial regime should allow the enforcement of the franchisor's action or inaction by an aggrieved franchisee. This enforcement remedy should confer on the franchisee the right to compel the franchisor to do or not to do something that the rules of comprehensive franchise law require. The law may establish exceptions that the franchisor can prove to escape this liability.

(3) *Monetary compensation*

The remedial system should permit an injured franchisee to seek damages for the loss or damage caused by the franchisor's contravening conduct. In this case, the remedial rule should be precise about the principles governing an award of statutory damages. In particular, the rule should define recoverable loss under comprehensive franchise law and establish a general standard for measuring damages.

(4) *Cancellation of a contract*

The remedial regime should provide a legal mechanism that enables the franchisee to cancel a franchise contract to leave an undesirable franchise relationship. In this case, the remedial system may have to be clear about the requirements for the cancellation mechanism under comprehensive franchise law.

4.5 CONCLUSIONS

Chapter four has examined the franchise legal framework of the DCFR, the USA, and Australia regulating the franchisor's duty not to encroach and the duty to assist and found that a franchise contract plays a primary role in regulating the franchisor's ongoing obligations. As examined in this chapter, the terms of a franchise agreement may grant a franchisee the exclusive right to conduct a franchised business in a specific location and require a franchisor to refrain from engaging in traditional and non-traditional encroachment in the vicinity of the franchisee's exclusive area. Additionally, the terms of a franchise agreement may ensure that a franchisee will acquire several forms of franchisor's assistance in opening and operating a franchised business. Nevertheless, the fourth chapter has discovered that the franchisor's ongoing obligations may be regulated by franchise relationship law rules, particularly the franchisor's duty not to encroach.

Chapter four has also explored that the DCFR, the USA, and Australia allow an aggrieved franchisee to seek contract law remedies that permit the franchisee to compel the franchisor's performance, claim monetary compensation, and cancel a franchise contract by way of termination or rescission. In seeking these three remedies, the franchisee usually has to demonstrate that the franchisor fails to perform the obligations in the manner specified by the contract's terms. Additionally, this fourth chapter has found that the franchisee may resort to statutory rules under the US and Australian legal systems for the remedies of enforcement of performance, damages, and cancellation of a franchise contract. In this respect, the franchisee has to demonstrate that the franchisor's conduct violates the statutory rules on which the three remedies are based.

5 Regulation of transfer, non-renewal, and termination of a franchise contract

5.1 INTRODUCTION

In practice, a franchisor commonly holds power to steer a franchisee's exits from a franchise relationship. In other words, a franchisor ordinarily includes in a franchise contract the terms that allow the franchisor to control the dissolution of a franchise relationship. Under a franchise contract, a franchisor typically retains the right to withhold consent to a transfer proposed by a franchisee and the right to decide whether to renew or terminate a franchise contract.¹ The franchisor may exercise its rights opportunistically, which would lead to catastrophic consequences for the franchisee. For example, the franchisor's early termination of a franchise contract would cause financial losses since the franchisee will be unable to recover several costs associated with a franchise operation.² This example underlies the need for regulating the franchisor's opportunistic conduct to protect a vulnerable franchisee.

The essential questions that arise from the view mentioned above are: how is the franchisor's conduct regarding the three exit issues regulated? what are private law remedies available to an aggrieved franchisee in the event of the franchisor's violation of the regulations? Chapter five will first examine the extent to which the franchise legal framework of the Draft Common Frame of Reference (DCFR), the United States of America (USA), and Australia regulates the franchisor's conduct regarding transfer, non-renewal, and termination of a franchise contract. The examination of the franchise legal frameworks will be conducted in sections 5.2, 5.3, and 5.4, respectively. After that, this fifth chapter will explore potential private law remedies in the case of the franchisor's contravention of the rules of the franchise legal frameworks in section 5.5. In the end, section 5.6 will conclude on the findings of this chapter.

1 In this fifth chapter, the issues concerning a transfer, non-renewal, and termination of a franchise contract will collectively be called 'three exit issues'.

2 Robert W Emerson, 'Franchising Constructive Termination: Quirk, Quagmire or a French Solution' (2015) 18 University of Pennsylvania Journal of Business Law 163, 167 – 73.

5.2 TRANSFER OF A FRANCHISE CONTRACT

5.2.1 Introduction

A franchise transfer is one of the exit strategies, which is exceedingly valuable for franchisees.³ In some cases, a franchisee may desire to transfer a franchise agreement to recoup the value of its local goodwill. Typically, a transfer of a franchise by a franchisee needs to be effectuated by the franchisor's approval. Sometimes, a franchisor refuses to consent to a proposed transfer. The franchisor's withholding consent could inflict financial loss or damage to the transferring franchisee. Section 5.2 is devoted to examining the extent to which the franchise legal framework of the DCFR, the USA, and Australia plays a protective role for franchisees when it comes to transferring a franchise agreement. This section will describe the rules of law and the terms of a franchise contract of the selected legal systems in sections 5.2.2, 5.2.3, and 5.2.4, respectively. After the descriptive examination, a comparative examination of the franchise legal framework of the DCFR, the USA, and Australia will be conducted in section 5.2.5.

5.2.2 The Draft Common Frame of Reference (DCFR)

5.2.2.1 Introduction

The DCFR does not contain specific rules regulating a transfer of a franchise contract by a franchisee. In this case, a transfer of a franchise contract will fall within the ambit of general contract law rules of the DCFR. In this section, the rules of contract law will be examined in subsection 5.2.2.2. A franchise contract may include the terms regulating a transfer of a franchise contract by a franchisee. This section will also explore the extent to which the terms of a franchise contract regulate the transfer in subsection 5.2.2.3. In the end, conclusions about the regulation of a franchise transfer under the DCFR's franchise legal framework will be provided in subsection 5.2.2.4.

5.2.2.2 Regulation of transfer by the rules of the DCFR

In Book III of the DCFR, III. – 5:302 formulates the rule governing a transfer of contractual position. According to the drafters of the DCFR, this rule aims to provide a practical solution for transferring contracts with a long duration,

3 In this chapter, a transfer of a franchise contract should be understood as a complete assignment of a franchise agreement, resulting in the transfer of the existing franchisee's rights and duties under the current franchise agreement to the third person or the new franchisee.

as well as takeovers and amalgamations of businesses.⁴ Since a franchise contract is typically a relational, long-term contract, III. – 5:302 would sufficiently apply to a transfer of a franchise contract by a franchisee. Thus, a transferring franchisee will have to follow the requirement imposed by III. – 5:302 when intending to transfer an entire franchise contract to the third party.

In transferring a franchise contract, a franchisee needs a franchisor's consent. According to III. – 5:302(1), the consent of the other party is a conditional element of a transfer of a contractual relationship. Without the franchisor's consent, the transfer will be ineffective.⁵ Nevertheless, III. – 5:302 merely requires the franchisor's consent to the franchisor's transfer. In other words, this article does not lay down a rule regulating the franchisor's exercise of its discretion. In any case, it should not imply that the DCFR provides the franchisor with absolute discretion in consenting to a proposed transfer. In some circumstances, the franchisor's withholding consent may be confined by certain rules of the DCFR. For example, the franchisor's consenting may be subject to the rule concerning an obligation to co-operate in Part E of Book IV. According to IV.E. – 2:201, the franchisor and the franchisee will be required to collaborate actively and loyally to achieve the objectives of the franchise contract. The drafters of the DCFR provide that this article implies a duty for a franchisor to treat its franchisees equally and not make any unjustified distinction between the franchisees.⁶

In my view, the duty to co-operate may be implied in the context of a transfer of a franchise contract. For example, the franchisor may be required to treat all proposals to transfer on an equal basis; that is to say, the franchisor may have to treat like cases alike. Suppose the franchisor has approved one proposed transfer upon the franchisee's satisfaction of the franchisor's conditions, such as a financial status and business skills. In this case, the franchisor may not refuse to consent to other transfers that satisfy the same conditions unless the franchisor has justifiable reasons to do so. Otherwise, the franchisor may be deemed failing to perform the obligation of co-operation under IV.E. – 2:201.

In some cases, a franchisor may not refuse to consent to a proposed transfer without justifiable reasons. It could be argued that the franchisor's exercise of the right to withhold consent is subject to the requirement of good faith and fair dealing. Under the DCFR, III. – 1: 103(1) sets forth the basic standard of conduct for performing an obligation, in exercising a right to performance,

4 Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.2, Oxford University Press 2010) 1102.

5 Ibid 1103.

6 Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.3, Oxford University Press 2010) 2291.

in pursuing or defending a remedy for non-performance, or in exercising a right to terminate an obligation or contractual relationship.⁷ In those practices, a party is required to act in accordance with good faith and fair dealing. The expression 'good faith and fair dealing' is defined to mean honesty, openness, and consideration of the interests of the other party to the relationship.⁸ Therefore, when exercising the right to disapprove a transfer, the franchisor may be required to provide some legitimate reasons so that its decision is considered in line with the standard of good faith and fair dealing.⁹

5.2.2.3 Regulation of transfer by the terms of a franchise contract

The terms of a franchise contract may govern a franchise transfer by a franchisee.¹⁰ In other words, a franchise contract may include the terms regulating the procedures and requirements for a transfer of a franchise contract. Taking the ICC's Model Contract as an example, article 30 lays down the following conditions for a transfer of a franchise by the franchisee. First, subclause 30.1 imposes a general requirement that a franchisee has a right to transfer a franchise upon the prior written consent of a franchisor.¹¹ Second, subclause 30.2 establishes procedures for obtaining the franchisor's consent. In a nutshell, the franchisee shall give the franchisor notice of a transfer, including the full address of the prospective transferee, the terms of the acquisition, and other information specifically requested by the franchisor. In this respect, the franchisor is required to respond in one month after receipt of the notice. Furthermore, subclause 30.2 makes clear that silence from the franchisor is considered a rejection of the franchisee's proposal.¹² As can be seen, article 30 of the ICC's Model Contract seems to favor the franchisor in the sense that it does not directly regulate the franchisor's right to withhold consent to a transfer.

7 According to III. – 1:103(2), the duty of good faith cannot be excluded or limited by contract or other juridical acts.

8 The DCFR, I. – 1:103.

9 According to the Comments to III. – 1:103, the principle of good faith and fair dealing is said to cover situations in which a party stands on ceremony without any good reason. See Christian von Bar and Eric Clive, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.1, Oxford University Press 2010) 678.

10 Some franchise associations in Europe encourage the incorporation of transfer provisions in a franchise contract. For example, the Italian franchise association or AIF suggests that a franchise contract must expressly indicate the terms and conditions for a possible transfer of the agreement. The agreement must also contain specific provisions relating to the obligations of the parties after the transfer. See article 10 of the Extensions to the European Code of Ethics for Franchising <<https://bit.ly/3D0IicE>> accessed 17 February 2023.

11 This requirement corresponds to III. – 5:302(1) that requires the franchisor's consent to a transfer.

12 International Chamber of Commerce, *ICC Model International Franchising Contract* (ICC Publications 2011) 42.

The franchisor's conduct under the ICC's Model Contract may be confined by the requirement of good faith and fair dealing imposed by the applicable law. Article 31.A of the ICC's Model Contract provides that the agreement shall be governed by, among other things, the UNIDROIT Principles of International Commercial Contracts (UNIDROIT Principles 2016).¹³ Under the UNIDROIT Principles 2016, article 1.7(1) requires each party to act in accordance with good faith and fair dealing in international trade. The example of good faith and fair dealing conduct is provided by the commentary to that article. Under Illustration 3, unjustified refusal to approve is said to be against good faith.¹⁴ According to this illustration, the franchisor's unjustified disapproval of a transfer may be regarded as a contravention of article 1.7(1) of the UNIDROIT Principles 2016, which is the law applicable to the ICC's Model Contract.

5.2.2.4 Conclusions

The DCFR and the ICC's Model Contract do not explicitly regulate the franchisor's consent to a transfer of a franchise contract by a franchisee. In particular, those instruments do not control how the franchisor exercises its discretion or right to consent to the transfer. Nevertheless, it does not imply that the franchisor's discretion or right is complete. The franchisor's withholding consent to a transfer may be restrained under certain circumstances. Under the DCFR, a franchisor may have to approve its franchisees' transfer equally. A franchisor may be required by good faith and fair dealing to have a legitimate reason for withholding consent to a transfer. Likewise, in the ICC's Model Contract, a franchisor may be prevented from unjustifiably refusing to approve a transfer by a franchisee because of the applicable law rule. Thus, it would seem that the requirement of good faith and fair dealing plays a vital role in regulating the franchisor's consent to a transfer of a franchise contract.

13 The current edition of the UNIDROIT Principles of International Commercial Contracts is the 2016 edition. The official text of the UNIDROIT Principles 2016 can be retrieved at <<https://bit.ly/3fT71xD>>.

14 International Institute for the Unification of Private Law, *UNIDROIT Principles of International Commercial Contracts 2016* (International Institute for the Unification of Private Law 2016) 19.

5.2.3 The United States of America (USA)

5.2.3.1 Introduction

A franchisee's transfer of a franchise contract is regulated by the franchise relationship law of eight American states (transfer states).¹⁵ Under the statutes, the franchisor's ability to control a franchisee's transfer of a franchise will be restricted. In this section, the transfer rules of the franchise relationship statutes will be examined in subsection 5.2.3.2. In other jurisdictions, a franchise contract's terms may govern a transfer of a franchise contract by a franchisee. Subsection 5.2.3.3 will also examine the transfer clauses of a franchise contract. Subsection 5.2.3.4 will conclude on the regulation of a franchise transfer in the USA.

5.2.3.2 Regulation of transfer by the rules of franchise relationship law

Transfer states may regulate a franchise transfer differently. Despite the variation, the regulation of a franchise transfer is typically twofold. That is to say, the rules of the franchise relationship law will govern a procedure of a transfer and grounds for withholding consent to a transfer.

– *Procedural requirements for a transfer*

State franchise relationship law may set forth procedural requirements for a transfer. Except for Michigan and Minnesota, the eight transfer states' franchise statute establishes a notice requirement for a transfer of a franchise. This requirement concerns an exchange of notice between a franchisor and a franchisee. In transferring a franchise, a franchisee is required to notify a franchisor of an intention to transfer in writing. In Arkansas, California, Nebraska, and New Jersey, the franchise statute explicitly requires that some information must be included in the notice. For example, the law of Arkansas provides that the notice must contain information concerning the prospective transferee, namely, name, address, statement of financial qualification, and business experience during the past five years.

Under the transfer rules, the franchisor is required to notify the franchisee of approval or disapproval of the proposed transfer in writing within a specified period. In Arkansas, California, Iowa, Nebraska, and New Jersey, the franchisor must notify the franchisee in writing within 60 days. In Hawaii, the franchisor has 30 days to inform the franchisee of approval or disapproval of the proposed transfer. More interestingly, the transfer rules regulating the

15 Arkansas: AR ST, § 4-72-205; California: CA BUS & PROF, § 20029; Hawaii: HI ST, § 482E-6; Iowa: IA ST, § 523H.5 and IA ST, § 537A.10(5); Michigan: MI ST, 445.1527; Minnesota: MN ST, § 80C.14(Subd.5); Nebraska: NE ST, § 87-405; and New Jersey: NJ ST, 56:10-6.

procedure for a transfer may protect a transferring franchisee. In Hawaii, Iowa, and Nebraska, the transfer rules of franchise relationship law explicitly provide that the franchisor's consent to the transfer is deemed to have been granted if the franchisor failed to give the franchisee notice within a specified period.

– *Grounds for withholding consent to a transfer*

State franchise relationship law may constrain the franchisor's ability to withhold consent to a transfer. In all the transfer states, the transfer rules of franchise relationship law require a franchisor to have legitimate grounds for withholding consent to a transfer. Those legitimate grounds can roughly be categorized into two standards: unacceptability or unqualification of the proposed transferee and good cause.

(1) *Unacceptability or unqualification of the proposed transferee*

In Arkansas, Nebraska, and New Jersey, a franchisor may refuse to consent to a transfer, provided that the proposed transferee is unacceptable.¹⁶ The unacceptability of the proposed transferee may be illustrated by the character, financial ability, or business experience of the transferee. In this case, the franchisor may have to satisfy some objective tests in deciding that the proposed transferee is not acceptable. In this respect, New Jersey's court decisions may be used as illustrations. In New Jersey, some courts have construed that the franchisor's disapproval of a proposed transferee must survive the standard of reasonableness. This requirement is objective; it requires the franchisor to support its decision with credible evidence, demonstrating that the proposed transferee is materially deficient.¹⁷

The franchise relationship law of California, Iowa, and Minnesota adopts a similar test. Under the relationship statutes, a franchisor may withhold consent to a transfer of a franchise, given the proposed transferee's unqualification. In California, a franchisor is allowed to set standards for approval of new or renewing franchisees. In this respect, the franchisor can withhold its consent if the transferee does not meet the franchisor's then-existing standards.¹⁸ Similarly, in Iowa, the relationship statutes permit a franchisor to refuse to consent to a transfer if the transferee does not meet a reasonable current qualification for a new franchisee. The reasonable current qualification is defined to mean a qualification based upon a legitimate business reason.¹⁹ For instance, in *Taylor Equipment v John Deere*, the court interpreted that the

16 Arkansas: AR ST, § 4-72-205(b)(1); Nebraska: NE ST, § 87-405; and New Jersey: NJ ST, 56:10-6.

17 See eg, *Simmons v General Motors Corp Oldsmobile Division* 435 A 2d 1167, 1177, 180 NJ Super 522 (NJ Super AD, 1981) 540; *VW Credit Inc v Coast Automotive Group Ltd* 787 A2d 951, 958, 346 NJ Super 326 (NJ Super AD, 2002) 337-38.

18 CA BUS & PROF, § 20028(a).

19 IA ST, § 523H.5(1) and IA ST, § 537A.10(5)(a).

legitimate business reasons included the transferee's inadequate equity capital, as well as a long-term plan to consolidate dealerships in the hands of key dealers.²⁰ Likewise, the law of Minnesota allows a franchisor to withhold consent to an assignment or transfer if the present qualifications and standards required by the franchisor are not satisfied by the transferring franchisee.²¹

(2) *Good cause*

Hawaii and Michigan adopt a standard of good cause to restrict the franchisor's ability to withhold consent to a transfer.²² In terms of definition, the franchise relationship statute of the two states establishes a set of events that would constitute good cause for withholding consent to a transfer by a franchisor. For example, a franchisor may refuse to consent to the transfer if the proposed transferee is a competitor of the franchisor. A franchisor may withhold consent for good cause because of the failure of the franchisee or proposed transferee to pay any outstanding sums to the franchisor or to cure any default in the franchise contract existing at the time of the proposed transfer. As can be seen, the scope of the application of this standard seems to be broader than the test of unacceptability or unqualification of the proposed transferee.

It should be mentioned that the law of Hawaii and Michigan merely offers a set of circumstances under which a franchisor may establish good cause for refusal to consent to a transfer. In terms of character, the list of events constituting good cause is non-exhaustive. In this case, a franchisor may be allowed to demonstrate other situations that would constitute good cause for withholding consent to a transfer. Nevertheless, the franchisor may have to satisfy certain tests. For example, in Michigan, the court in *America's Favorite Chicken* concluded that good cause must be based on the commercial reasonability.²³ The court held that it was commercially reasonable for a franchisor to require a franchisee to provide a release of any and all claims before the franchisor approved the proposed transfer of a franchise.

5.2.3.3 *Regulation of transfer by the terms of a franchise contract*

A franchise contract may regulate a transfer of a franchise by a franchisee.²⁴ In practice, particularly in non-transfer states, it is relatively common that a franchise contract governs the matter of a franchise transfer through transfer

20 *Taylor Equipment Inc v John Deere Co* 98 F3d 1028 (CA8 (SD), 1996) 1034.

21 MN ST, § 80C.14(Subd.5).

22 Hawaii: HI ST, § 482E-6(2)(i) and Michigan: MI ST, 445.1527(g).

23 *Franchise Management Unlimited Inc v America's Favorite Chicken* 561 NW2d 123, 127, 221 Mich App 239 (Mich App, 1997) 247.

24 *Popeyes Inc v Tokita* 1993 WL 386260 (ED La, 1993) 11.

provisions.²⁵ For example, Royal Mountain Chocolate Factory, Inc, a Colorado-based corporation, has its franchise agreement that contains clause 16 governing transfer by a franchisee.²⁶ A franchise agreement of Baskin-Robbins Franchising LLC, a Delaware-based company, contains section 13 addressing transfer of a franchise.²⁷ Section 11 of a franchise agreement used by Buffalo Wild Wings International, Inc, an Ohio corporation governs any transfer of a franchise.²⁸ Moreover, a transfer of a franchise usually is subject to the franchisor's right to safeguard the integrity of the franchise system.²⁹ Thus, a franchise agreement may include a so-called 'non-assignment or anti-assignment clause' that frequently requires the franchisor's prior consent to a transfer.³⁰ For instance, Noodle & Company's franchise agreement provides that a franchisee cannot transfer the rights and duties under a franchise agreement without prior consent, which may be withheld by the franchisor's sole discretion.³¹

Transfer clauses under a franchise contract may be drafted differently by franchisors. Despite the difference, the sample clauses of the ABA's Annotated Franchise Agreement can be taken as examples.³² In a nutshell, a transfer of a franchise cannot be made without the franchisor's prior consent. In this respect, a franchisor is required not to withhold its consent unreasonably.³³ In deciding whether to consent to a transfer, a franchisor may consider the financial history and qualifications, credit standing, franchise and other business experience, education, and ability to operate a franchised business of the proposed transferee. A franchisor may require a business plan of the proposed transferee indicating that the proposed transferee possesses the required level of business experience and skills necessary to operate a franchised business. In this case, the plan may be required to include other evidence showing that

25 Andra Terrell and Trish Treadwell, 'Transfer, Assignment, Death, or Incapacity of the Franchisee' in Nina Greene, Dawn Newton, and Kerry Olson (eds), *The Annotated Franchise Agreement* (2nd edn, American Bar Association 2021) 177.

26 The form of a franchise agreement can be accessed at <<http://bit.ly/3GNeGwR>>.

27 The form of a franchise agreement can be accessed at <<http://bit.ly/3XfIPf7>>.

28 The form of a franchise agreement can be accessed at <<http://bit.ly/3w55eQF>>.

29 Standard 11.2 of the AAFD's Fair Franchising Standards.

30 Kerry L Bundy and Robert M Einhorn, 'Chapter 5: Franchise Relationship Laws' in Rupert M Barkoff and others (eds), *Fundamentals of Franchising* (4th edn, American Bar Association 2016) 219, 224. As far as case law is concerned, US courts have consistently upheld that this type of transfer provision is enforceable. See eg *San Francisco Newspaper Printing Co v Superior Court* 216 Cal Rptr 462, 464, 170 Cal App 3d 438 (Cal App 6 Dist, 1985) 442; *James v Whirlpool Corp* 806 F Supp 835 (ED Mo, 1992) 843; *Taylor Equipment* (n 20) 1032; *Johnson v First Colony Life Ins Co* 26 F Supp 2d 1227 (CD Cal, 1998) 1230; *Johnson v JG Wentworth Originations LLC* 391 P3d 865, 869, 284 Or App 47 (Or App, 2017) 54.

31 The form of a franchise agreement can be accessed at <<http://bit.ly/3H8x1pC>>.

32 Terrell and Treadwell (n 25) 184-96.

33 Although the authors engage in a lengthy discussion about this requirement, they do not offer a clear standard for determining whether the franchisor's withholding consent is unreasonable.

the proposed transferee has the qualifications, apparent ability, and credit standing to operate the business. In reality, not every franchise agreement constrains the franchisor's consent by the reasonableness test.

Despite the lack of contractual constraint, the franchisor's discretion in withholding consent to a transfer may not be absolute. In some states, the franchisor's discretion may be confined to some standards of review. For example, in New Jersey, the court in *Coast Automotive Group* concluded that the franchisor's disapproval of the proposed transferee was subject to a reasonable exercise of the government's police power. In this case, the franchisor was required to act reasonably in withholding its consent to a transfer under the franchise practices law.³⁴ In *Wineinger*, the Wisconsin court accepted that the duty of good faith and fair dealing could be implied despite a consent clause. However, the franchisor's consent would be subject to a lower standard of review than reasonableness. That is, the franchisee had to provide evidence that the franchisor acted unreasonably, arbitrarily, in bad faith or deprived the franchisee of the benefit of the bargain intended by the franchisor and the franchisee.³⁵

5.2.3.4 Conclusions

There are several approaches to controlling the franchisor's consent to a transfer. In the eight transfer states, the franchisor's ability to withhold consent to a transfer is regulated by franchise relationship law. Under the relationship statutes, a franchisor may refuse to consent to a proposed transfer by a franchisee only for specific grounds, namely the unacceptability or unqualification of the proposed transferee and good cause. Most American states do not regulate a franchise transfer through franchise relationship law. In those jurisdictions, a transfer may be governed by the transfer clauses of a franchise contract. Some of those clauses may require a franchisor not to withhold its consent to a transfer unreasonably. In the absence of such terms, the franchisor's consent to a transfer may be constrained by standards of review that would require a franchisor not to refuse to consent to a transfer unreasonably or in bad faith.

34 *VW Credit, Inc v Coast Auto Grp, Ltd*, 346 NJ Super 326, 346, 787 A2d 951 (App Div 2002) 963.

35 *Queen v Wineinger*, No 21-CV-378-WMC, 2022 WL 3027004, (WD Wis Aug 1, 2022) 7.

5.2.4 Australia

5.2.4.1 Introduction

The Franchising Code of Conduct (the Code) contains rules regulating a transfer of a franchise agreement. This section will examine the transfer rules under the Code in subsection 5.2.4.2. Since the rules are mandatory, the parties to a franchise agreement cannot agree otherwise. A franchise agreement may include the terms that play a supportive role in regulating a franchise transfer. Thus, it would be wise to explore how the transfer clauses of a franchise agreement regulate a franchise transfer in addition to the Code's transfer rules. This exploration will be made in subsection 5.2.4.3. In the end, conclusions about the regulation of a franchise transfer in Australia will be made in subsection 5.2.4.4.

5.2.4.2 Regulation of transfer by the transfer rules

Division 4 of the Code contains clauses 24 and 25 providing rules regulating a transfer of a franchise agreement. In essence, the transfer rules regulate specific procedures for transferring and the franchisor's ability to withhold consent to the transfer. Summaries are to be provided in the following two italicized headings.

– *Procedural requirements for a transfer*

In transferring a franchise agreement, a franchisee must acquire the franchisor's consent to a transfer. In this respect, the Code imposes notice requirements on the franchisee and franchisor. Clause 24(1) requires the franchisee to give the franchisor written notice to request the franchisor's consent to a transfer. In the notice, the franchisee must provide all information that the franchisor would reasonably require and expect to be given to make an informed decision.³⁶ Upon the receipt of the franchisee's written notice, the franchisor is required to inform the franchisee of its decision in writing. According to clause 25(1)(a), the franchisor shall notify the franchisee of whether the franchisor consents to the transfer.³⁷ If the franchisor does not give its consent, the franchisor must provide reasons why it does not consent to the proposed transfer.

³⁶ The Code, cl. 24(2).

³⁷ According to clause 25(1)(b), if the franchisor gives consent to a transfer, the franchisor may state that the given consent is subject to one or more conditions that need to be satisfied. However, the franchisor may revoke its consent within 14 days by giving written notice containing reasons for the revocation, pursuant to clause 25(5). In any event, the franchisor is prevented by clause 25(6) from unreasonably revoking its consent.

The Code lays down some procedural rules to ensure that a franchisee will receive an answer whether the franchisor consents to a transfer. First, the Code requires the franchisor to inform the franchisee of its decision within 42 days.³⁸ This 42-day period starts to count on the date the franchisee made the request.³⁹ If the franchisor requires further information, the 42-day period will start on the date the last of the information is provided to the franchisor.⁴⁰ Second, the Code assumes the franchisor's consent if the timeframe has expired. That is, the franchisor will be taken to have given consent to a transfer if the franchisor fails to inform the franchisee within 42 days. In this case, the franchisor's assumed consent cannot be revoked under paragraphs (5) and (6) of clause 25.⁴¹

– *Grounds for withholding consent to a transfer*

The Code restricts the franchisor's ability to withhold its consent to a transfer to some degree. According to clause 25(2), a franchisor cannot withhold consent to a transfer of a franchise agreement unreasonably.⁴² In this respect, the Code provides a list of seven circumstances in which the franchisor may reasonably withhold consent to the transfer.⁴³ In sum, those specified events mainly involve the unqualification of the proposed transferee and the franchisee's failure to perform an obligation. For example, the franchisor may reasonably withhold consent to the transfer if the proposed transferee is unlikely to be able to meet the financial obligations that the proposed transferee would have under the franchise agreement, or if the proposed transferee does not meet a reasonable requirement of the franchise agreement for the transfer of the contract.⁴⁴ The franchisor may also refuse to consent if the franchisee has not paid or made reasonable provision to pay an amount owing to the franchisor, or has not remedied a breach of the franchise agreement.⁴⁵

The listed circumstances under which a franchisor can withhold its consent may not be exclusive since the last passage of clause 25(6A) implies that the franchisor may reasonably withhold consent in other circumstances than those specified events. Grounds for reasonably withholding consent have been exemplified by some court decisions. For example, the court in *Masterclass Enterprises v Bedshed Franchisors (WA)* concluded that it was not unreasonable that the franchisor required the franchised business to be supervised by some-

38 The Code, cl. 25(4).

39 The Code, cl. 25(4)(a).

40 The Code, cl. 25(4)(b).

41 The Code, cl. 25(4)(c)(d).

42 See eg *BB Australia Pty Ltd v Bytan Pty Ltd* [2012] VSC 171 [11]; *RPR Maintenance Pty Ltd v Marmax Investments Pty Ltd*, [2014] FCA 409 (*RPR Maintenance I*) [25].

43 The Code, cl. 25(6A)(a) to (g).

44 The Code, cl. 25(6A)(a) and (b).

45 The Code, cl. 25(6A)(e) and (f).

one with a substantial interest in the franchisee. According to the court decision, it would be reasonable for the franchisor to withhold its consent if the franchisee aims to transfer a franchise agreement to the third person who has no substantial interest in the franchised business.⁴⁶ In *ACCC v Allphones Retail*, the franchisor undertook that it would not refuse to consent to a transfer on the basis that the transferee must conclude a franchise agreement that differs from the agreement between the franchisor and the transferring franchisee. The court interpreted that this undertaking aimed to prevent the franchisor from requiring a new franchisee to enter into a franchise agreement that is different from the transferring franchisee's agreement as a condition of consenting to a transfer of a franchise. Thus, the court found that the franchisor contravened its undertaking because it asked a new franchisee to enter into a new differing franchisee agreement.⁴⁷

5.2.4.3 Regulation of transfer by the terms of a franchise contract

Since the transfer rules under the Code are mandatory, the transfer clauses under a franchise contract are typically drafted by duplicating the mandatory rules.⁴⁸ The Precedent to Franchise agreement (Precedent) may provide some examples of how the transfer clauses are drafted.⁴⁹ In a nutshell, a franchisee who desires to transfer or sell a franchised business must notify a franchisor of a proposed sale in writing.⁵⁰ In this case, the franchisee needs to receive the franchisor's consent to a proposed transfer.⁵¹ Upon the receipt of the franchisee's notification, the franchisor needs to notify the franchisee of its decision in writing within 42 days. Otherwise, the franchisor will be deemed to have given consent to the proposed transfer.⁵²

More importantly, in deciding to consent, the franchisor is required not to withhold its consent to a transfer unreasonably.⁵³ In this case, the Precedent establishes a list of circumstances under which the franchisor may reasonably withhold its consent. Notably, some of the listed events are supplementary

46 *Masterclass Enterprises Pty Ltd v Bedshed Franchisors (WA) Pty Ltd* [2008] WASC 67 [113] – [122].

47 *Australian Competition and Consumer Commission v Allphones Retail Pty Ltd* (No 4) [2011] FCA 338 [42], [56]–[62].

48 In practice, a franchise agreement may provide additional details regarding transfer of a franchise. For example, the contract may provide a formula for calculating the cost of obtaining the franchisor's consent to the transfer or require that a transferee must conclude the franchisor's current franchise agreement.

49 The Precedent is a model, basic franchise agreement prepared by Perrott, Churley, and Giles and updated by Carkeet and Mitchell. The Precedent is available for sale on Lexis-Nexis's website. A copy is also in the author's possession.

50 The Precedent, cl. 25(b)(i).

51 The Precedent, cl. 25(c).

52 The Precedent, cl. 25(d).

53 The Precedent, cl. 25(c).

to those specified by the Code. For instance, the franchisor may withhold consent to a transfer if the agreement of transfer will have a significantly adverse effect on the franchise system.⁵⁴ The franchisor may do so if the transfer is not part of a bona fide sale of the franchised business to the buyer.⁵⁵

5.2.4.4 Conclusions

The Franchising Code of Conduct plays a significant role in regulating a transfer of a franchise agreement by a franchisee. In regulating a transfer, the transfer rules require a franchisee to follow some procedural requirements for transferring a franchise agreement. These procedures are essentially concerned with an exchange of written notice between the franchisor and franchisee. More importantly, the rules require the franchisor not to withhold its consent to a transfer unreasonably. The test of reasonableness is clarified by a list of circumstances under which the franchisor may reasonably withhold consent. The listed events are not exhaustive and leave room for supplementation by the terms of a franchise contract. In this respect, the transfer clauses may enumerate additional circumstances under which the franchisor can withhold consent reasonably.

5.2.5 Comparative analysis

5.2.5.1 Introduction

The descriptive examination of the franchise legal framework of the DCFR, the USA, and Australia demonstrates that the franchisor's consent is widely accepted as a conditional element of a transfer of a franchise contract by a franchisee. Nevertheless, the chosen legal systems do not give a franchisor wide discretion over consenting to the franchisee's transfer. In other words, the franchise legal frameworks regulate the franchisor's consent to a transfer to some extent. This section will compare, contrast, and discuss the legal approaches taken by the selected legal systems in subsection 5.2.5.2 to formulate proposals for enacting comprehensive franchise law's rules regulating procedures for a transfer of a franchise and the franchisor's consent to a transfer. In the end, conclusions and key recommendations for the regulation of a franchise transfer will be provided in subsection 5.2.5.3.

⁵⁴ The Precedent, cl. 25(c)(iii).

⁵⁵ The Precedent, cl. 25(c)(vi).

5.2.5.2 Comparison and discussion

– Similarity

The DCFR and most US states do not regulate a transfer of a franchise contract by a franchisee. In this respect, the franchisee's transfer will be governed by the terms of a franchise contract and general contract law rules. A franchisee is ordinarily required by the terms of a franchise contract to request the franchisor's consent to a transfer. However, the transfer clauses may confer on the franchisor the right to withhold consent to a transfer.⁵⁶ Despite the retention of the right, it seems common that the principle of good faith and fair dealing can be used to confine the franchisor's withholding consent to a transfer.⁵⁷ The principle of good faith recognized by the DCFR and the US contract law is similarly an open standard that needs judicial crystallization. Thus, courts may have to concretize the concept of good faith on a case-by-case basis. In this respect, the utilization of good faith under the DCFR and the US legal system seems to converge. In light of the good faith requirement, a franchisor may be required to have legitimate grounds for withholding consent or not to withhold consent unreasonably.

– Difference

Contrariwise, the eight transfer US states and Australia regulate a franchise transfer by a franchisee through the transfer rules of franchise relationship legislation.⁵⁸ This franchise relationship law is introduced to redress inequality in bargaining power between a franchisor and a franchisee. In this respect, the US and Australian relationship transfer rules similarly protect a transferring franchisee in the two following aspects. Firstly, the transfer rules regulate procedures for transferring a franchise. Under the rules, a franchisee is required to give the franchisor written notice of a transfer. Upon receipt of the notice, the franchisor shall inform the franchisee of its decision whether the consent to a transfer is given. Besides, the franchisor must notify the franchisee within a specific period. If the franchisor fails to inform the franchisee, the franchisor will be presumed to have consented to the proposed transfer. Secondly, the transfer rules regulate the franchisor's withholding consent to a transfer. That is, the franchisor cannot refuse to consent to the transfer unless it has legitimate grounds for withholding its consent. Under the rules, the grounds for a refusal to consent typically involve the unacceptability or unqualification of the proposed transferee and good cause.

⁵⁶ See subsections 5.2.2.3 and 5.2.3.3.

⁵⁷ See subsections 5.2.2.2 and 5.2.3.3.

⁵⁸ See subsections 5.2.3.2 and 5.2.4.2.

– *Discussion*

The comparison shows that a franchise transfer can be regulated by the terms of a franchise contract and the rules of law. This heading will dissect two types of transfer regulation to formulate proposals for incorporating transfer rules into comprehensive franchise law.

(1) *Regulation of a transfer by the terms of a franchise contract*

It is not uncommon for legal systems with no statutory regulation on a franchise transfer to address the issue of a franchise transfer from the perspective of the parties to a franchise contract. Under these legal systems, a franchise contract will be a primary instrument that regulates a transfer of a franchise. In some cases, a franchise contract can protect a franchisee in that it controls the franchisor's discretion in consenting to a transfer. The ABA's publication can be taken as an example in this regard. In the ABA's annotated franchise agreement, the transfer clause of the agreement requires a franchisor not to withhold consent to a transfer unreasonably. This reasonableness standard would confine the franchisor not to act opportunistically in deciding whether to consent to the franchisee's proposed transfer because it requires the franchisor to have legitimate reasons for withholding consent. In practice, some franchise contracts follow this direction.⁵⁹

Nevertheless, a franchise contract is rarely protective of the franchisee's interests since many franchisors ordinarily prefer to retain total control over a franchise transfer, such as control over the selection of a new franchisee or a transferee, for reasons. For example, the franchisee may want to ensure that the transferee has a specific license to operate a franchised business in a regulated industry. The franchisor may need to ascertain that the transferee is not financially unfit for operating a franchised business. Accordingly, a franchise contract may contain a non-assignment clause, prohibiting a transfer of a franchise contract. This arrangement usually is valid in several legal systems. For example, in the USA, the anti-assignment clause usually is valid and enforceable, provided that the language is unambiguous.⁶⁰ Likewise, under the DCFR, the terms of a franchise contract may prohibit a transfer of a franchise contract. These clauses might not be regarded as unfair terms in light of II. – 9:405 because a franchisor may argue that it needs to reserve the absolute right to recruit new franchisees to the franchise network to control a desirable level of quality of its franchisees.⁶¹

59 See eg *Dunkin' Donuts Franchised Restaurants LLC v 1700 Church Avenue Corp* 2009 WL 10695151 (EDNY, 2009) 1; *Ganley v Mazda Motor of America Inc* 367 Fed Appx 616, 618, 2010 WL 697360 (CA6 (Ohio), 2010) 1.

60 *Metroil Inc v ExxonMobil Oil Corp* 724 F Supp2d 70 (DDC, 2010) 80.

61 The test of unfair terms in a contract between businesses includes good commercial practice and good faith and fair dealing. In this case, the contractual terms will be considered unfair if they grossly deviate from those mentioned standards.

In other cases, the terms of a franchise contract may permit a transfer of a franchise contract. However, the terms of a franchise contract may constrain the franchisee's transfer in several ways. For instance, a franchise transfer usually is conditional upon the franchisor's prior consent.⁶² Under the transfer clauses, a franchisee may have to satisfy specific requirements for requesting the franchisor's consent to the transfer.⁶³ Despite the satisfaction of the requirements, a franchisor typically retains absolute discretion in consenting to a transfer since the transfer clauses may not lay down standards for withholding consent to a transfer.⁶⁴ Taking the ICC's Model Contract as an example, there is no constraint on the franchisor's discretion in consenting to a transfer by the franchisee.⁶⁵

As can be seen, a franchise contract may not be protective of a franchisee when it comes to transferring a franchise contract to a third party. This phenomenon is by no means surprising since a franchise contract is ordinarily drafted by a franchisor. In this case, it is common that a franchisor retains absolute or relative control over a franchise transfer to protect its benefits. Although a franchise agreement contains transfer clauses, the incorporation of these clauses is primarily intended to facilitate the franchisor's control over a franchise transfer, which would make a transferring franchisee susceptible to the franchisor's opportunistic conduct. For example, the franchisor may withhold consent to a transfer without any reasonable grounds that would cause financial loss to the franchisee. Therefore, the regulation by the rules of law may be desirable to regulate the franchisor's consent to a transfer.

(2) *Regulation of a transfer by the rules of law*

The regulation of a transfer of a franchise contract by the rules of law is twofold.

First, a transfer of a franchise agreement may be subject to general rules of contract law. Under contract law rules, the requirement of good faith may be used to protect a franchisee against an opportunistic franchisor. Theoretically, the good faith principle would be utilized to prevent a franchisor from withholding consent unreasonably or without reasonable grounds. However, the utilization of the principle of good faith may be constrained from a prac-

62 Mark Abell, *The law and regulation of franchising in the EU* (Edward Elgar Publishing Limited 2013) at [3.17]. See also Jerome L Withered, 'The No-Assignment-without-Consent Clause in Franchise Agreements' (1984) 4 *Franchise Law Journal* 1, 1.

63 For example, a franchise agreement may require the franchisee to pay transfer fees to the franchisor. The payment of the fees is said to help redress any loss that the franchisor will suffer when accepting a new franchisee and losing a chance to sell the franchise itself. See Elizabeth Crawford Spencer, *The Regulation of Franchising in the New Global Economy* (Edward Elgar Publishing Limited 2010) 96.

64 Terrence M Dunn, 'The Franchisor's Control over the Transfer of a Franchise' (2008) 27 *Franchise Law Journal* 233, 233.

65 See subsection 5.2.2.3.

tical viewpoint. According to Hesselink, good faith is an open norm; hence, the content of good faith cannot be formulated in an abstract way. In this respect, good faith needs to be concretized by courts, considering the circumstances of the specific case.⁶⁶ In this respect, courts may be reluctant to apply good faith due to several reasons. For example, in some legal systems, judges may be unwilling to apply the good faith principle in the absence of established precedents. Thus, my view is that the standard of good faith might not be an effective tool in protecting the franchisees.

Second, a transfer of a franchise contract may be regulated by transfer rules of franchise-specific law, particularly franchise relationship law. As can be seen from the comparison, the transfer rules extensively regulate the franchisor's withholding consent and the procedures for transferring a franchise contract. In my view, the transfer rules are much clearer than contract law rules, which would not be sufficient to address transfer of a franchise. For example, the rules require a franchisor not to withhold consent without good cause or for some legitimate grounds. In this case, the rules may also offer tests or standards for determining whether the franchisor withholds consent unlawfully. Upon receipt of the franchisee's notice of a transfer, the franchisor will be taken to have consented to the franchisee's transfer if the franchisor fails to decide and inform the franchisee of the decision within a specific period. Since the transfer rules are mandatory, the franchisor cannot exercise its superior power to exclude or vary the application of the rules by a franchise agreement.

In protecting a franchisee, I propose that the comprehensive franchise law contain the rules regulating a transfer of a franchise by a franchisee. Strictly speaking, the law should contain rules that establish transfer rules regulating the following two aspects of a franchise transfer: the procedure for obtaining the franchisor's consent to a transfer and the franchisor's ability to withhold consent to a transfer. Furthermore, the law should contain the rule establishing the requirement of good faith. In these cases, I also suggest that the franchise provisions are made mandatory to prevent any contractual deviation concluded to the franchisee's detriment. In the following headings (3), (4), and (5), the clarifications of the proposed rules regarding the transfer procedure, the control over the franchisor's withholding consent, and the good faith principle are to be provided.

(3) *Procedural requirements for acquiring the franchisor's consent to a transfer*

'(1) A transfer of a franchise must be effectuated by the franchisor's consent. For the purpose of this rule, a transfer of a franchise includes a situation in which the

66 Martijn W Hesselink, 'Chapter 27: The Concept of Good faith' in Arthur S Hartkamp and others (eds), *Towards a European Civil Code* (Kluwer Law International 2011) 622-23.

franchisee's rights and obligations under a franchise contract are transferred to the proposed transferee during the term of the contract.

(2) The franchisee may request consent to a transfer by giving the franchisor written notice of an intention to transfer. The notice of transfer must include, but is not limited to, information about the name and address of the proposed transferee, statement of financial qualification, and business experience during the previous 5 years. Upon receipt of the franchisee's notice, the franchisor may require more relevant information about the proposed transferee.

(3) Within 30 calendar days after receipt of the notice, the franchisor must give written notice to the franchisee, informing the franchisee whether the franchisor consents to the proposed transfer. The franchisor is deemed to have consented if the franchisor fails to notify the franchisee in writing within a specified period.'

The first paragraph starts with formulating the underlying principle that a franchise transfer by a franchisee needs the franchisor's approval.⁶⁷ In principle, a successful transfer of a franchise will lead to the substitution of the proposed transferee for the existing franchisee. Eventually, the transferee will join a franchise system by way of transfer. In this respect, the requirement that the franchisee needs the franchisor's prior consent is crucial in that it allows the franchisor to evaluate the potential ability of the transferee in operating a franchised business. The franchisor's ability to examine and assess the transferee's qualification would help maintain the high level of quality of the franchise brand by avoiding any potential sub-standard franchisees. Thus, the franchisor's scrutiny of the prospective transferee would benefit all the franchisees in the franchise system.

As can be seen, the first paragraph provides the definition of the expression 'transfer of a franchise'. Defining the term is imperative since legal systems may perceive the term 'transfer' differently. In my opinion, the term 'transfer of a franchise' should, at least, cover a situation in which an existing franchisee transfers an entire franchise contract to a prospective transferee, resulting in the assumption by the transferee of the rights and duties under the existing franchise contract. The transfer provision may broadly outline the term to include other situations. For example, the Australian Franchising Code of Conduct defines a transfer to include a situation in which the existing franchise contract is terminated on the basis that a new franchise agreement is entered into between the franchisor and prospective transferee. Thus, legal systems may define a franchise transfer differently based on policy considerations.

As can be seen, the definition of a transfer of a franchise is not inclusive because the proposed rule uses the an open-ended word 'include'. In this case, I am of the opinion that a transfer of a franchise can be interpreted to include other situations in which an existing franchisee is replaced by other persons. In practice, a franchise transfer may occur when ownership of the franchisee,

⁶⁷ It should be noted that this proposed provision will apply to a transfer of a franchise contract, regardless of whether the contract is concluded for a definite or indefinite period.

as a company, is acquired by a third person. Sometimes, the franchisee agrees to sell its assets to a third party.⁶⁸ As acquisition activities are not unusual in commercial reality, the proposed transfer provision should be poised to capture these practices too because the rule primarily aims to regulate practices that result in swapping an incumbent franchisee with others. Suppose the franchisee intends to sell a majority of its shares to the other party, implicitly changing the franchisee's personal entity. In this case, the franchisee needs to follow transferring procedure imposed by the proposed model rule.

The second paragraph provides that the transferring franchisee is required to give the franchisor written notice of the intention to transfer. This notice requirement would help alert the franchisor that the franchisee starts the process of the transfer.⁶⁹ In the notice of transfer, the franchisee should be required to supply the franchisor with some items of material information. The information to be provided should be sufficient enough to help the franchisor make an informed consent. This requirement is not uncommon in practice. For example, under the Australian Franchising Code of Conduct, a request for the franchisor's consent to transfer must be accompanied by all information that the franchisor would reasonably require and help the franchisor make an informed decision.⁷⁰

The test of reasonableness adopted by the Australian Code of Conduct offers no practical guidance. According to Ship and Sohail, the term 'reasonable' is, by nature, indiscernible; it is highly fact-sensitive and depends on the circumstances of the case.⁷¹ In remedying this flaw, I suggest that the transfer provision makes the list of essential information to be provided in the notice of transfer. Listing the informational items would help avoid diverse interpretations as to whether the information given is reasonable. Thus, the franchisee should, at the very least, be required to provide information about the proposed transferee's name and address, statement of financial qualification, and business experience during the previous 5 years, which would sufficiently demonstrate the transferee's capacity to conduct business. Furthermore, I suggest that the list of information is non-exclusive. The underlying reason is that the franchisor should be allowed to ask for additional information items that help the franchisor decide whether to consent to the transfer. Furthermore, the franchisee would be able to supply more information to convince the franchisor to consent to the transfer.

68 Eric Freedman, 'Hyundai sued over franchise transfer; Carmaker interfered in sale, ex-operators say' (7 March 2022, Automotive News) accessed <<http://bit.ly/3kvDaDw>> 21 January 2023.

69 This written notice also serves an evidentiary function that helps avoid any potential conflict over whether the notice has been lodged to the franchisor.

70 The Code, cl. 24(2).

71 Adam Ship and Mohammed Sohail, 'Franchise Renewal and Transfers in Canada Common Law Provinces' (2015) 35 *Franchise Law Journal* 237, 248.

Upon receipt of the notice of transfer, the third paragraph requires the franchisor to inform the transferring franchisee of its decision in writing and within a specified period. The comparison shows that there has been no uniform timeframe for making consent among the selected legal systems. As can be seen, the DCFR does not require the franchisor to consent to a transfer within any specific period.⁷² Conversely, the US and Australian legal systems specify a period of time for the franchisor's notification. The length of the duration varies among the countries. In the USA, the franchisor may be required to give a 30-day or 60-day notice. Moreover, Australia requires the franchisor to inform the franchisee of its decision within 42 days.

Regarding the timing, I suggest that the transfer provision specifies the timeframe for deciding whether to consent to a transfer. This specificity would help prevent the franchisor's undue delay in consenting to the transfer that would inflict economic damage to the franchisee. For example, the delay in consenting to a transfer would cause the franchisee to breach a transfer agreement with the third party, resulting in the franchisee's liability to the third party. A question arises as to what timeframe should be made under the transfer provision. Since there is no uniform answer to this question, I suggest that a period of 30 calendar days would be reasonable and sufficient enough for the franchisor to process the franchisee's proposal to transfer, study information about the transferee, and decide whether to consent to the transfer.

Additionally, I propose that this transfer provision establishes a sanction for the franchisor's failure to comply with the time requirement. As can be seen in paragraph (2), the franchisor will be presumed to have consented to the proposed transfer if the franchisor fails to notify the franchisee within one month. This presumed consent requirement would protect a transferring franchisee since it would encourage the franchisor to make a timely decision on the proposal to transfer. Otherwise, the franchisor will be presumed to have consented.

(4) *Restriction on the franchisor's withholding consent to a transfer*

'(1) The franchisor must have reasonable grounds for withholding consent to a transfer. The reasonable grounds for withholding consent include, but are not limited to, the commercial unacceptability of the proposed transferee.

(2) The commercial unacceptability of the proposed transferee may be determined by the fact that the proposed transferee is a competitor of the franchisor; the proposed transferee faces financial difficulties, and the proposed transferee lacks sufficient business experience.'

72 The franchisor may be required by the duty of good faith to notify the franchisee within a reasonable period, which will be decided on a case-by-case basis.

The first paragraph formulates the restriction on the franchisor's withholding consent to a transfer. That is, the franchisor can refuse to consent to a transfer, provided that the franchisor has reasonable grounds for doing so. This approach is not peculiar in the regulatory context. In the USA and Australia, franchise relationship laws contain provisions regulating the franchisor's withholding consent to a transfer. Nevertheless, the circumstances under which the franchisor may withhold consent vary from legal system to legal system.⁷³ Despite no uniformity in this regard, I suggest that the transfer provision regards the unacceptability of a proposed transferee as one of the reasonable grounds for withholding consent to a transfer. In practice, the concept of unacceptability is a common prerequisite for the franchisor's approval of a transfer.⁷⁴ More importantly, this criterion makes commercial sense. In most cases, a franchisor wants to maintain a good level of quality of the franchise business. In doing so, the franchisor must be able to evaluate the potential ability of the prospective franchisees to operate a franchised business. This assumption holds true when it comes to evaluating the proposed transferees in the case of transfer. Thus, the franchisor should be able to withhold consent to a transfer if the proposed transferee is commercially unacceptable.

The test of the commercial unacceptability of a proposed transferee is rather broad and allows the franchisor to have wide discretion. Thus, paragraph (2) demonstrates some circumstances under which the franchisor may withhold its consent due to the commercial unacceptability of the proposed transferee. To exemplify, the franchisor may withhold consent to the transfer in the following three circumstances. First, a proposed transferee is a competitor of the franchisor. Second, a proposed transferee has faced financial difficulties that make the transferee fail to meet the financial standards set by the franchisor for recruiting new franchisees. Third, a prospective transferee lacks an acceptable level of business experience. Since the list of circumstances is not inclusive, the franchisor may raise other situations in which the proposed transferee would be regarded as commercially unacceptable. For example, the prospective transferee may be unacceptable because it committed serious crimes, such as fraud, which would harm the franchisor's business goodwill.

As the language in paragraph (1) suggests, reasonable grounds for withholding consent are not limited to the unacceptability of the proposed transferee. Thus, the franchisor is permitted to withhold consent to a transfer for other reasons insofar as they are considered reasonable in the commercial context. In franchising practice, those commercial reasons may include a situation in which the transferring franchisee has not yet remedied any non-compliance of an obligation under a franchise contract. This requirement is not unusual. Some US franchise relationship law, such as the franchise invest-

73 See subsections 5.2.3.2 and 5.2.4.2.

74 Derek W Saunders, 'Franchisee Sales of Existing Franchises' (1991) 11 *Franchise Law Journal* 31, 31.

ment law of Hawaii, requires a franchisee to settle outstanding debts or redress defaults before a transfer.⁷⁵ Furthermore, one commentator says that the satisfaction of all outstanding obligations by a transferring franchisee is one of the prerequisites for approval of a transfer.⁷⁶

(5) *Requirement of good faith*

The requirement of good faith should be introduced under comprehensive franchise law to ensure that the parties to a franchise contract cannot act capriciously towards the other party. In the context of a franchise transfer, the franchisor should be required not to withhold consent to a transfer capriciously.⁷⁷ The franchisor's discrimination in withholding consent may be taken as an example of capricious behaviors. Since franchise contracts are, by nature, contracts in a network, a franchisor may encounter numerous transfer proposals by its franchisees. In this respect, the principle of good faith could help ensure that the franchisor's decision is not abusive by way of discrimination. Moreover, the prohibition against the franchisor's discrimination among its franchisees is not an alien concept. In practice, it has been adopted in some franchise-specific legislation. For example, the franchise relationship statute of Arkansas, Hawaii, Iowa, and Washington contains nondiscrimination provisions preventing a franchisor from discriminating among franchisees.⁷⁸

A question may be raised as to the definition of the term 'discrimination' that could constitute an act contrary to the requirement of good faith and fair dealing. In response to this question, I suggest that the DCFR could provide useful references when defining discrimination. Under the DCFR, Chapter 2 of Book II formulates some principles concerning non-discrimination in relation to a contract or other juridical act.⁷⁹ In this chapter, the conduct constituting discrimination against a person is twofold.⁸⁰

First, discrimination may refer to unequal treatment based on sex or ethnic or racial origin.⁸¹ Some franchise relationship law is seen adopting this pro-

75 HI ST, § 482E-6(2)(iv).

76 Saunders (n 74).

77 Some franchise relationship laws adopt a similar approach in constraining the franchisor's discretion. For example, in America, the franchise relationship statutes of Iowa require the franchisor not to refuse to consent to the transfer arbitrarily or capriciously. See IA ST, § 523H.5(1) and § 537A.10(5)(a).

78 *General Aviation Inc v Cessna Aircraft Co* 13 F3d 178 (CA 6 (Mich), 1993) 181–82. It should be mentioned that those antidiscrimination provisions are ordinarily introduced in the context of non-renewal of a franchise contract.

79 It should be noted that the right not to be discriminated against is introduced in the context of contracts or other juridical acts that provide supply goods, other assets, and services that are made available to the public. Examples can be found in cases where products and services are publicly offered in shops or restaurants. See Bar and Clive (n 9) 168.

80 According to II. – 2:104(1), the discriminated person is entitled to remedies for non-performance of an obligation under Book III, Chapter 3.

81 The DCFR, II. – 2:101.

hibition. For instance, in the USA, the franchise statutes of Iowa prevent a franchisor from discriminating against a proposed transferee based on race, color, national origin, religion, sex, and disability.⁸² As far as case law is concerned, a franchisor may differentiate proposed transferees on the basis of race. For example, the franchisor in *Home Repair v Paul W Davis Systems* was accused of not approving the transfer of a franchise because the transferee was African-American.⁸³ In this case, if the franchisee can prove that the franchisor withholds its consent solely on the basis of racial discrimination, the franchisor could be considered acting in breach of the duty of good faith in the light of the proposed provision of the uniform franchise law.

Second, discrimination may refer to unequal treatment given in a comparable situation. In other words, this second type of discrimination refers to a situation in which one person is treated less favorably than another person would be treated in a comparable situation.⁸⁴ In the American case *BASCO v Buth-Na-Bodhaige*, for example, the franchisor rejected the proposed transferee because the transferee had little retail experience and inability to work full-time in the franchised store. However, the evidence showed that the franchisor approved other transferees despite the lack of retail experience and the ability to work full-time in the franchised shop.⁸⁵ In this case, the franchisor's conduct could be regarded as discrimination against the proposed transferee in that the franchisor treated the transferee less favorably than the others. Accordingly, the franchisor may be considered in breach of the principle of good faith.

The franchisor's unequal treatment for particular reasons may not be considered discriminatory behaviors. Under the DCFR, II. – 2:103 provides that unequal treatment that is a consequence of a legitimate aim is not regarded as discrimination. According to the Comments to this article, the aim will be regarded as legitimate if it intends to protect some societal values, such as privacy, decency, religion, and cultural identity.⁸⁶ In my view, this exception might be adopted in the franchising context as well. Strictly speaking, some legitimate aims may justify the franchisor's practice of unequal treatment in the context of a transfer. In this respect, the franchisor may justify the preferential treatment of some proposed transferees by showing commercial reasons. For example, the franchisor may approve an unqualified transferee, while disapproving others, because of the need to remain competitive in the marketing areas.

⁸² IA ST, § 523H.5(8) and § 537A.10(5)(f).

⁸³ *Home Repair Inc v Paul W Davis Systems Inc* 2000 WL 126905 (ND Ill, 2000) 3.

⁸⁴ The DCFR, II. – 2:102(1)(a).

⁸⁵ *BASCO Inc v Buth-Na-Bodhaige* 198 F3d 1053 (CA8 (Minn), 1999) 1056, 1058.

⁸⁶ In any case, the protection of those values cannot trump the protection of human dignity. See Bar and Clive (n 9) 185.

5.2.5.3 Conclusions

– *Concluding remarks*

The comparative study of the DCFR, the US, and Australian legal systems show that a transfer of a franchise contract can be regulated by the terms of a franchise contract and the rules of law. The level of protection of franchisees varies significantly. In the former case, the franchisees are less protected because the franchisor holds a significant degree of power to control a transfer by the franchisees. Although most franchise contracts allow a transfer of the agreements, the franchisor typically retains the absolute right to withhold its consent to the transfer. In the latter case, the franchisees can be protected by contract law and franchise relationship law rules. The comparative analysis demonstrates that the transfer rules of franchise relationship law could provide greater protection to the franchisees in that the franchisor's withholding consent to a transfer is rigorously regulated. Thus, this regulatory approach is a preferable approach to protecting the franchisees in the context of transfer.

– *Key recommendations*

(1) *Regulation of a transfer of a franchise contract*

Comprehensive franchise law should contain transfer provisions regulating a transfer of a franchise contract by a franchisee. Under the provisions, a franchisee's transfer should be effectuated by the franchisor's consent. In this case, the transfer provisions should regulate the procedure for obtaining the franchisor's consent and restrict the franchisor's ability to withhold consent to a transfer.

(2) *Procedural requirements for a transfer*

A transferring franchisee should be required to give a franchisor written notice of transfer. The written notice should contain material information about the proposed transferee, including the transferee's name and address, statement of financial qualification, and business experience during the previously specified year. Upon receipt of the notice, the franchisor may ask for additional information, but it should be required to notify the franchisee of its decision in writing within 30 calendar days. In this case, the franchisor should be taken to have consented to the transfer if the franchisor fails to notify the franchisee of its decision.

(3) *Constraints on the franchisor's withholding consent*

The franchisor should be required to have reasonable grounds for withholding consent to a transfer. The grounds for withholding consent should include the commercial unacceptability of the prospective transferee. The determinants of the unacceptability of the transferee should include three facts as follows.

First, the prospective transferee is a competitor of the franchisor. Second, the transferee does not meet the franchisor's financial criteria for franchisees. Third, the transferee lacks sufficient business experience for the operation of a franchised business. The grounds for withholding consent should not be inclusive. The franchisor should be permitted to withhold its consent to a transfer based on other commercial grounds.

4) *Requirement of good faith*

Besides regulating a franchise transfer through transfer provisions, comprehensive franchise law should contain a provision establishing the duty of good faith that requires the parties to a franchise contract not to act capriciously towards the other party in the course of a franchise relationship. In the context of franchise transfer, a franchisor should be required not to withhold consent capriciously. For example, the franchisor cannot withhold its consent in a discriminatory manner unless the franchisor has legitimate reasons for that discrimination.

5.3 NON-RENEWAL OF A FRANCHISE CONTRACT

5.3.1 Introduction

A franchise contract may be concluded for a fixed term. When the term of a franchise contract expires, a franchisor may not renew the contract for another term. In some cases, the franchisor's non-renewal of a franchise contract may be detrimental to a franchisee's financial benefits. In some cases, a franchisee has concluded a franchise contract for a long term, thereby developing local goodwill attached to a franchised business during the period. In this case, the franchisor's refusal to renew a franchise could lead to returning the franchisee's goodwill to the franchisor without compensation paid to the franchisee.⁸⁷ Section 5.3 will examine the extent to which the franchise legal framework of the DCFR, the USA, and Australia regulates the franchisor's non-renewal of a franchise contract. In this section, the description of the legal framework of the chosen legal systems will be taken in sections 5.3.2, 5.3.3, and 5.3.4, respectively. Section 5.3.5 will conduct a comparative analysis of the franchise legal frameworks regulating the franchisor's non-renewal of a franchise contract.

⁸⁷ Caroline B Fichter, Andrew M Malzahn, and Adam Matheson, 'Don't Tread on Me: A Defense of State Franchise Regulation' (2018) 38 Franchise Law Journal 23, 37.

5.3.2 The Draft Common Frame of Reference (DCFR)

5.3.2.1 Introduction

The DCFR contains IV.E. – 2:301 that provides a default rule applying to the renewal of a contract for a definite period. The rule in IV.E. – 2:301 is applied to the renewal of a franchise contract by virtue of IV.E. – 1:101(1). Subsection 5.3.2.2 will examine the extent to which the rule is applied to the franchisor's renewal of a franchise contract. Since the rule in IV.E. – 2:301 is not mandatory, the parties to a franchise contract may exclude or vary the effect of the rule under the renewal clauses. In this case, the terms of a franchise contract will regulate the renewal issue. Thus, subsection 5.3.2.3 will explore how the contract's terms regulate the franchisor's renewal. In the end, conclusions about the regulatory character of the DCFR will be provided in subsection 5.3.2.4.

5.3.2.2 Regulation of non-renewal by the rules of the DCFR

A franchise contract with a definite period may be renewed. In this respect, IV.E. – 2:301 prescribes the procedure that would lead to the extension of the term of a franchise contract. Under IV.E. – 2:301, the renewal procedure involves an exchange of notice between the franchisor and franchisee.⁸⁸ In the case of the franchisee's renewal, IV.E. – 2:301 requires the franchisee to provide the franchisor with the notice of renewal in due time. Upon receipt of the notice, the franchisor may elect not to renew the contract. The franchisor is required to inform the franchisee of its decision not later than a reasonable time before the franchise contract expires.⁸⁹ If the franchisor fails to notify the franchisee within a reasonable time, the franchise contract will be renewed for an indefinite period with the same conditions.⁹⁰

Sometimes, a franchisor may be constrained to refuse to renew a franchise contract. Although IV.E. – 2:301 does not require the franchisor to provide any just cause for the non-renewal of a franchise contract, it could be argued

88 I. – 1:109 may be applicable when it comes to giving the notice under IV.E. – 2:301. According to I. – 1:109(2), the parties may provide the notice by any means appropriate to the circumstances. According to para (4) of I. – 1:109, the notice will be effective when it reaches the other party. Circumstances in which the notice reaches the recipient are enumerated in para (5) of I. – 1:109. For example, if the franchisor sends the notice by email, the notice is deemed to reach the franchisee when it reaches an email server of the franchisee.

89 Whether the notice is given in due or reasonable time will be determined by considering the circumstances of the case. However, the latter period is dependent upon the former period. See Bar and Clive (n 6) 2300. In my opinion, the four factors prescribed in IV.E. – 2:302(3) may be taken into account. In light of IV.E. – 2:302(3), the reasonableness of the notice period may depend on (a) the time the contractual relationship has lasted, (b) reasonable investment made, (c) the time it will take to find a reasonable alternative, and (d) usages.

90 Bar and Clive (n 6) 2299.

that the franchisor's discretion in refusing to renew a franchise agreement is to be qualified by the requirement of good faith and fair dealing. Under the DCFR, III. – 1:103(1) provides that a person has a duty to act in accordance with good faith and fair dealing in exercising a right to terminate a contractual relationship. In the context of non-renewal, the franchisor's refusal to renew a franchise contract may be taken as terminating the contract. In this respect, the franchisor may be required to act in accordance with the requirement of good faith and fair dealing in deciding not to renew a franchise contract. In practice, the principle of good faith comes into play in the context of non-renewal as well. In Italy, it is said that the franchisor may breach the good faith principle under the Italian civil code. Suppose the franchisor permits the franchisee to invest based on the assumption that a franchise contract will be renewed. In this case, it will be contrary to good faith if the franchisor later proposes burdensome requirements for the franchisee's renewal.⁹¹

5.3.2.3 Regulation of non-renewal by the terms of a franchise contract

A franchise contract plays an important role in regulating the renewal of the contract. The parties may agree to incorporate the renewal clauses into a franchise agreement that lays down requirements and criteria for renewal.⁹² Under the renewal provisions, a franchisee may hold an option to renew.⁹³ A franchisee typically needs to satisfy specific requirements for the renewal of a franchise agreement. The ICC's Model Contract shows that the option to renew is conditional upon the satisfaction of the following conditions. First, the franchisee has not committed a substantial breach of the agreement. Second, the franchisee must sign the standard contract in effect at that time. Third, the franchisee must exercise the option not less than 9 months before the initial term expires.⁹⁴ Nevertheless, the ICC's Model Contract does not contain the terms restricting the franchisor's ability to refuse to renew. In this case, the

91 Aldo Frignani and John H Pratt, 'Termination and Non-Renewal of Franchise Agreements in the European Union: Italian Law in a Comparative Perspective with Other European Civil Law Systems and England and Wales' (2017) 37(1) *Franchise Law Journal* 15, 19.

92 This contractual arrangement is encouraged by the European Code of Ethics for Franchising. According to clause 5.4, the minimum terms of a franchise contract should include the basis for any renewal of the agreement. See the European Code of Ethics for Franchising <<https://bit.ly/3cZ8dk5>> accessed 17 February 2023.

93 For example, in the English case *Paperlight v Swinton Group*, the franchise contract at issue provides that the franchisee has an option to renew the agreement for another term. Nevertheless, the franchisee must satisfy certain conditions. For example, the franchisee must not be in breach of a substantial term of the contract during the term. See *Paperlight Ltd v Swinton Group Ltd* [1998] CLC 1667, 1669.

94 The Model Contract, art. 25.1AB.

franchisor may not renew a franchise agreement even though the franchisee has met the three requirements mentioned earlier.⁹⁵

5.3.2.4 Conclusions

When it comes to an end of a fixed-term franchise contract, the DCFR's franchise legal framework establishes procedures that allow a franchisee to request the renewal of the term of a franchise contract. The legal framework does not obligate a franchisor to extend or renew the contract for another term. In other words, the franchisor is free not to renew a franchise contract upon the expiry of the contractual term. Despite the fact that the franchisor retains the right not to renew, the franchisor may not exercise the right opportunistically. As can be seen, the franchisor's non-renewal under the DCFR and the ICC's Model Contract can be subject to the requirement of good faith and fair dealing. The practical example shows that this good faith principle could be utilized to constrain the franchisor's non-renewal by requiring the franchisor not to jeopardize the franchisee's reasonable expectation of renewal of franchise contract.

5.3.3 The United States of America (USA)

5.3.3.1 Introduction

In principle, a franchise contract for a definite period will expire as of the agreed date.⁹⁶ In this case, a franchisor has no duty to renew the agreement for another term.⁹⁷ In some states, the franchisor's non-renewal of a franchise contract may be regulated by franchise-specific legislation. In the USA, seventeen US states (non-renewal states) introduce franchise relationship law regu-

⁹⁵ Despite the lack of the terms, I have reviewed earlier in 5.2.2.3 that the franchisor may be required by the applicable law rules to act in accordance with good faith and fair dealing in international trade. Thus, the franchisor may not refuse to renew a franchise contract unless the franchisor has provided some justified reasons for refusing.

⁹⁶ The renewal of a franchise contract may be implied. Suppose the franchisor and franchisee continue to perform the same services after a franchise contract expires. In this case, the parties are presumed to have renewed the contract with the same term. Besides, the franchisor will be prohibited from invoking that the original contract has expired because it treats the expired contract as an operative contract. *See eg BSG LLC v Check Velocity Inc* 395 SW3d 90 (Tenn, 2012) 94; *Miller Construction Equipment Sales Inc v Clark Equipment Company* 2016 WL 2626803 (D Alaska, 2016) 11.

⁹⁷ W Michael Garner, Non-renewal—Generally, 2 Franch & Distr Law & Prac, Westlaw, (November 2019) at § 10:9.

lating the franchisor's non-renewal of a franchise contract.⁹⁸ This section will examine the rules of franchise relationship law regulating the franchisor's non-renewal in subsection 5.3.3.2. In non-regulation states, a franchise contract may play a leading role in regulating the franchisor's non-renewal of a franchise. Subsection 5.3.3.3 will explore how the terms of a franchise agreement regulate the franchisor's non-renewal. Subsection 5.3.3.4 will conclude on the US regulatory system.

5.3.3.2 Regulation of non-renewal by the rules of franchise relationship law

As mentioned in the introduction, the seventeen non-renewal states regulate the non-renewal of a franchise by a franchisor through the rules of franchise relationship legislation.⁹⁹ These rules vary from state to state. Despite the variation, the rules are said to regulate the following two aspects of the franchisor's non-renewal. First, the non-renewal rules require the franchisor to notify the franchisee of the non-renewal of a franchise. Second, the non-renewal rules require the franchisor to support its non-renewal with legitimate grounds.¹⁰⁰

– Notice requirement for non-renewal of a franchise

Except for Hawaii and Michigan, all the non-renewal states (notice states) require a franchisor to give a franchisee notice of non-renewal of a franchise contract within a specific period in advance of the expiration of the franchise contract. This specific period may range from at least 15 days to one year. Some notice states may exempt the franchisor from following this notice requirement. For example, in Washington, a franchisor may not provide a franchisee with notice of non-renewal. The franchisor may do so if it compensates the franchisee for the value of some specified assets.

98 Those non-renewal states are Arkansas, California, Connecticut, Delaware, Hawaii, Illinois, Indiana, Iowa, Michigan, Minnesota, Mississippi, Missouri, Nebraska, New Jersey, Rhode Island, Washington, and Wisconsin.

99 Arkansas: AR ST, § 4-72-204; California: CA BUS & PROF, § 20030; Connecticut: CT ST, § 42-133f; Delaware: DE ST TI 6, § 2552 and 2555; Hawaii: HI ST, § 482E-6(2)(H); Illinois: IL ST CH 815, § 705/20; Indiana: IN ST, 23-2-2.7-1; Iowa: IA ST, § 523H.8 and IA ST § 537A.10(8); Michigan: MI ST, 445.1527(e); Minnesota: MN ST, § 80C.14(Subd.4); Mississippi: MS ST, § 75-24-53; Missouri: MO ST, 407.405; Nebraska: NE ST, § 87-404(1); New Jersey: NJ ST, 56:10-5; Rhode Island: RI ST, § 6-50-4(a); Washington: WA ST, 19.100.180(2)(i); and Wisconsin: WI ST, 135.04.

100 John R F Baer and Pamela J Mills, 'Renewals: Questions and Pitfalls for Franchisors and Some Distributors' (1990) 10 Franchise Law Journal 1, 13.

– *Grounds for non-renewal of a franchise contract*

In all the non-renewal states, the franchisor must have grounds for the non-renewal of a franchise contract. Those grounds could be categorized into three bases as follows.

(1) *Good cause*

Franchise relationship law of ten non-renewal states requires a franchisor to show good cause for non-renewal of a franchise contract.¹⁰¹ Except for Delaware and Indiana, all the ten non-renewal jurisdictions define the term 'good cause'. How the state defines good cause may vary. For example, in Arkansas, the franchise statute provides a list of circumstances that would constitute good cause for the franchisor's non-renewal of a franchise. Some other states, such as Connecticut and Hawaii, define the term 'good cause' to include the franchisee's failure to substantially comply with material obligations or provisions of the franchise contract.

(2) *Good faith*

In Delaware and Indiana, franchise relationship laws provide that the franchisor's non-renewal of a franchise shall not be made in bad faith. Nevertheless, the statutes do not define the term 'bad faith'. Despite the lack of a definition, courts may manage to resort to some sources of reference. For instance, the court of Delaware in *Globe Liquor v Four Roses Distillers* referred to the definition of good faith provided by the Uniform Commercial Code (UCC).¹⁰² Under the UCC, the term good faith is defined to mean honesty in fact and the observance of reasonable commercial standards of fair dealing. Legitimate business reasons may be regarded as indicators of good faith. In *Ray Skillman Oldsmobile*, the franchisor refused to renew a franchise because the franchised business was no longer competitive in the market. In this case, the Indiana court held that the franchisor's non-renewal was made in good faith.¹⁰³

(3) *Satisfaction of established criteria*

In Arkansas, Hawaii, Indiana, and Iowa, the franchise relationship statutes permit a franchisor to refuse to renew a franchise contract, provided that a franchisee does not satisfy the current criteria established by the franchisor. Those criteria may take the form of policies, practices, terms, conditions, requirements, or standards. Furthermore, in Arkansas, Hawaii, and Iowa, the relationship laws ensure non-discrimination of the application of those

101 Those states are Arkansas, Connecticut, Delaware, Hawaii, Indiana, Iowa, Minnesota, Nebraska, New Jersey, and Wisconsin.

102 *Globe Liquor Co v Four Roses Distillers Co* 281 A2d 19 (Del, 1971) 22.

103 *Ray Skillman Oldsmobile & GMC Truck Inc v General Motors Corp* 2006 WL 694561 (SD Ind, 2006) 2.

standards. For instance, in Hawaii, the law requires that the current terms and standards for renewal of a franchise must equally be applied to all franchisees. However, the statute provides an exception in the case the franchisor can prove that any discrimination of the franchisees is reasonable, based on proper and justifiable distinctions, and not arbitrary.

5.3.3.3 Regulation of non-renewal by the terms of a franchise contract

In many cases, the terms of a franchise contract regulate the renewal of the contract.¹⁰⁴ In some cases, a franchise contract may not provide a franchisee with the right to renew a franchise for another term. In other cases, the franchisee's renewal of a franchise agreement may be permitted. Some franchise contracts may provide that the franchisee's renewal is conditional upon the satisfaction of specific requirements. Taking the ABA's publication as an example, the franchisee is provided with an option to renew a franchise agreement for one additional period. In renewing the contract, the franchisee must satisfy the requirements for the renewal of the contract. For example, the franchisee is required to give a franchisor a written notice of an intention to renew not less than six months but no more than twelve months before the contract ends. Besides, the franchisee is required to conclude the franchisor's then-current standard form of a franchise agreement.¹⁰⁵ Since the franchise contract confers the franchisee with the renewal right, the franchisor may not refuse to renew a franchise if the franchisee meets all the conditions set by the franchise agreement.

Although a franchise contract allows a franchisee to ask for the renewal, a franchisor may retain the right to refuse to renew for any reason or even without cause.¹⁰⁶ In this case, a franchisee cannot claim that a franchisor wrongfully refuses to renew a franchise agreement.¹⁰⁷ Some commentators suggest that the franchisor's non-renewal of a franchise may be limited by the covenant of good faith and fair dealing.¹⁰⁸ In practice, however, courts may not follow this proposition. For example, in *Courtesy Oldsmobile v General Motors Corporation*, the Nevada court held that the implied covenant of good

104 Baer and Mills (n 100) 15; Robert W Emerson, 'Franchise Contract Clauses and the Franchisor's Duty of Care toward Its Franchisees' (1994) 72(4) North Carolina Law Review 905, 949.

105 Joseph Sheyka and Elizabeth M Weldon, 'Fees, Initial, Terms, and Renewal' in Nina Greene, Dawn Newton, and Kerry Olson (eds), *The Annotated Franchise Agreement* (2nd edn, American Bar Association 2021) 51.

106 This arrangement is enforceable in several US states, such as New York and Indiana. See eg *Wright-Moore Corp v Ricoh Corp* 980 F2d 432 (CA7 (Ind), 1992) 437; *RWJ Companies Inc v Equilon Enterprises LLC* 2005 WL 3544295 (SD Ind, 2005) 9–10. It is said that franchise contracts rarely include this arrangement. See *ibid* 53.

107 *Chang v McDonald's Corp* 1996 WL 742455 (CA9 (Cal), 1996) 2.

108 Baer and Mills (n 100) 13.

faith and fair dealing was not applied to the case in which the franchisor reserved full discretion in renewing the dealership agreement.¹⁰⁹

5.3.3.4 Conclusions

There are two models of the regulation of the franchisor's non-renewal of a franchise in the USA. First, the franchisor's non-renewal may be regulated by franchise relationship law. As can be seen, the seventeen non-renewal states introduce the relationship statute to regulate the notice of non-renewal of a franchise and the franchisor's refusal to renew. In the latter case, the franchisor can refuse to renew a franchise, provided that the franchisor has legitimate grounds for refusing to renew. In other words, the franchisor may not refuse to renew without just cause. Second, the franchisor's non-renewal of a franchise may be regulated by the renewal clauses of a franchise contract. In reality, a franchisor will have a considerable degree of freedom in deciding whether and the extent to which a franchise contract is to be renewed. In this case, the covenant of good faith and fair dealing may be argued to regulate the franchisor's decision not to renew.

5.3.4 Australia

5.3.4.1 Introduction

In general, a franchise contract for a fixed term will expire at the end of the agreed period.¹¹⁰ A franchisor is not obliged to renew a franchise agreement for another term. However, the Franchising Code of Conduct (the Code) regulates certain aspects of the franchisor's non-renewal of a franchise agreement. Subsection 5.3.4.2 will examine the extent to which the Code regulates the franchisor's non-renewal. Furthermore, the terms of a franchise agreement may also regulate the franchisor's refusal to renew. Subsection 5.3.4.3 will explore how the terms of a franchise contract regulate the franchisor's non-renewal. In the end, conclusions about the regulatory approaches will be made in subsection 5.3.4.4.

5.3.4.2 Regulation of non-renewal by the rules of the Franchising Code of Conduct

The Code imposes a notification requirement on a franchisor when the expiry of the term is approaching. Clause 18(1) requires the franchisor to notify the franchisee in writing of whether the franchisor intends to extend the franchise agreement or enter into a new franchise agreement. According to clause 18(2),

109 *Courtesy Oldsmobile Inc v General Motors Corporation* 2007 WL 9725221 (D Nev, 2007) 7.

110 *Ranoa Pty Ltd v BP Oil Distribution Ltd* (1989) 91 ALR 251.

the franchisor must notify the franchisee of its intention at least six months before the end of the term of the franchise agreement if the term is six months or longer. Conversely, the notification period is reduced to at least one month before the end of the term of the agreement if the term is less than six months.¹¹¹

As can be seen, the Code simply requires the franchisor to give the franchisee the written notification of its intention whether to renew the term of a franchise agreement. In other words, the Code does not require the franchisor to renew the agreement for an additional term. Nor does the Code constrain the franchisor's decision not to renew or require the franchisor to have any good cause for non-renewal. It could be argued that the Code may protect a franchisee *ex-ante* through the disclosure requirement. According to Annexure 1 of the Code, the franchisor must include the item of information about an option to renew a franchise agreement in the disclosure document.¹¹² If the franchisor does not provide that option, the franchisor must include the statement in size 12 font and bold in the disclosure document reminding the absence of the renewal option.¹¹³ This disclosure requirement would help remind a prospective franchisee before the conclusion of a franchise agreement of whether the renewal of the agreement is available.

5.3.4.3 Regulation of non-renewal by the terms of a franchise contract

The preceding subsection reveals that the Code does not regulate the franchisor's discretion in renewing a franchise agreement. In this case, it is said that a franchise agreement will play a primary role in regulating the renewal of the term of the agreement.¹¹⁴ In general, the terms of a franchise agreement require the franchisor's consent to the renewal. The terms normally set up the procedure and requirements for a franchisee to obtain the franchisor's consent. The Precedent to a franchise agreement (Precedent) may illustrate

111 It should be noted that Division 2 of Part 5 of the Code applies if a franchisee is a new vehicle dealer under a new vehicle dealership agreement. According to clause 47(1), the franchisor is required to notify the franchisee in writing if the franchisor intends to extend the agreement, enter into a new agreement or neither of them. If the term of the agreement is 12 months or longer, paragraph (2) of clause 47 provides that the franchisor's notice must be given at least 12 months before the end of the term. If the parties agree on a later time, the franchisor's notice must be given before that later time.

If the term of the agreement is less than 12 months, clause 47(3) provides that the franchisor's notice must be given at least 6 months before the end of the term of the agreement if the term is 6 months or longer. If the term is less than 6 months, the franchisor's notice must be given at least 1 month before the end of the term. In case the franchisor does not intend to extend the term or enter into a new franchise agreement, clause 47(5) requires the franchisor's notice to include the reasons for the intention.

112 Item 18.1(a)(i) of Annexure 1.

113 Item 18.3 of Annexure 1.

114 Australian Competition and Consumer Commission, 'Extending or ending a franchise agreement' <<https://bit.ly/2k73FA8>> accessed 17 February 2023.

these components. In clause 9 of the Precedent, the franchisee is required to notify the franchisor of whether the franchisee desires to renew the term of the agreement. In this case, the franchisee has to inform the franchisor in writing at least seven months before the term of a franchise agreement expires.¹¹⁵ Upon receipt of the request, the franchisor cannot unreasonably withhold its consent to the proposed renewal unless the franchisee does not satisfy some specific requirements.¹¹⁶ For example, the franchisor may withhold consent if the franchisee is in default under the agreement or the franchisee has not substantially complied with all the terms and conditions of the agreement throughout the term.¹¹⁷ In any event, the franchisor shall inform the franchisee of its decision in writing at least six months before the expiration of the contract.¹¹⁸

5.3.4.4 Conclusions

When the term of a franchise agreement is about to expire, the Franchising Code of Conduct regulates the franchisor's non-renewal of the agreement by requiring a franchisor to get a franchisee notified of its decision not to renew within a specified period. However, the Code does not regulate the requirements for renewal or the franchisor's decision not to renew. In these cases, the terms of a franchise agreement will play a significant role; that is to say, the contract's terms may require a franchisee to satisfy some conditions and requirements for renewing the agreement. The renewal clauses may protect the franchisee's interest by requiring the franchisor not to withhold consent to the proposed renewal by the franchisee unreasonably. The renewal clauses may stipulate some exceptions where the franchisor can refuse to renew the term of a franchise agreement although the franchisee satisfies the requirements for renewing.

5.3.5 Comparative analysis

5.3.5.1 Introduction

For a franchise contract with a fixed term, the descriptive sections show that the franchise legal framework of the DCFR, the USA, and Australia allows a franchisor not to renew the term of a franchise contract when the term is about to expire. However, the legal frameworks may provide rules or standards regulating some aspects of the franchisor's non-renewal. This section will

¹¹⁵ The Precedent, cl. 9(a).

¹¹⁶ The Precedent, cl. 9(c).

¹¹⁷ The Precedent, cl. 9(c)(i)(ii).

¹¹⁸ The Precedent, cl. 9(d).

juxtapose and discuss the regulation of the franchisor's non-renewal under the selected legal systems in subsection 5.3.5.2. This subsection will also suggest model rules regulating the renewal of a franchise agreement under comprehensive franchise law. In the end, remarks on the regulation of the renewal of a franchise contract and key recommendations will be provided in subsection 5.3.5.3.

5.3.5.2 Comparison and discussion

– Similarity

The DCFR and most US states are similar in that they do not provide franchise-specific law rules regulating the franchisor's non-renewal of a franchise. The DCFR merely provides the special rule regulating the procedure for renewing commercial contracts, including a franchise contract. This rule by no means regulates the franchisor's decision not to renew.¹¹⁹ Likewise, a majority of the US states do not enact franchise relationship law containing the rules regulating the franchisor's non-renewal of a franchise.¹²⁰ These legal systems will similarly employ general contract law rules to govern the franchisor's non-renewal of a franchise agreement. Under the contract law regimes of the DCFR and the USA, it could be argued in theory that a franchisor may not refuse to renew a franchise contract contrary to the principle of good faith. Strictly speaking, the franchisor may have to provide some legitimate grounds for refusing to renew the agreement. Otherwise, the franchisor's non-renewal would be said to be made in bad faith.

– Difference

Contrariwise, the seventeen US states and Australia regulate the franchisor's non-renewal of a franchise contract through franchise relationship law.¹²¹ Nevertheless, the rules of the US and Australian franchise laws vary. In the seventeen US states, the franchisor's non-renewal of a franchise agreement is constrained in the following two aspects. First, the franchisor is required to inform the franchisee of the intention not to renew in writing before the contract expires. Second, the franchisor is required to have legitimate grounds for non-renewal of a franchise contract. Ordinarily, those grounds include good cause, good faith, or equally applicable requirements laid down in a franchise agreement. Unlike the US legislation, the Australian Franchising Code of Conduct only regulates the process of the franchisor's non-renewal. That is, the franchisor is required to notify the franchisee of its intention in writing

¹¹⁹ See subsection 5.3.2.2.

¹²⁰ See subsection 5.3.3.2.

¹²¹ See subsections 5.3.3.2 and 5.3.4.2.

whether to renew a franchise agreement within a specific period. However, the Code imposes no constraints on the franchisor's decision not to renew. In this case, the regulation of the franchisor's non-renewal will be made under the terms of a franchise agreement.

– *Discussion*

From the comparison, the approach to regulating the franchisor's non-renewal of a franchise contract is twofold. The regulation of the franchisor's non-renewal may be made through the terms of a franchise agreement and the rules of law. The following headings (1) and (2) will discuss these two legal approaches.

(1) *Regulation of non-renewal by the terms of a franchise contract*

Typically, a franchise contract is concluded for a fixed term. In some franchise contracts, the length of the term is relatively long. In this case, it is unsurprising that the option to renew the term of the contract is crucial for both parties.¹²² Thus, a franchise contract frequently incorporates the terms dealing with the issues related to renewal or non-renewal of the contract.¹²³ This express agreement approach would be beneficial to a franchisee in several aspects. One of those benefits is that the terms of a franchise contract can provide a high degree of certainty regarding the consequences of the franchisor's non-renewal, such as the franchisee's right to compensation of goodwill.

Ordinarily, the franchisee's right to compensation for the value of goodwill may be unclear from a statutory standpoint. In other words, franchise-specific legislation may not provide an effective solution for dealing with the ownership of goodwill in the franchising context. For example, in Australia, according to an inquiry submitted to the Australian Productivity Commission, the law does not provide any protection for a franchisee who loses goodwill after a franchisor fails to renew franchise agreements.¹²⁴ In this respect, it would be disputable whether the franchisee may redeem the value of goodwill if the franchisor refuses to renew a franchise contract. In this case, the terms of a franchise contract would provide standards for settling the dispute. For example, the terms of a franchise contract may confer on the franchisee the right to compensation of goodwill upon the expiry of the contract.¹²⁵

From my perspective, the terms of a franchise contract can be protective of a franchisee's benefits only in case the franchisee can bargain for that

122 Spencer (n 63) 92.

123 Bundy and Einhorn (n 30) 210.

124 Tim D Castle, Zali Steggall, and Andrew Terry, *Destruction and Appropriation of Goodwill: The Problem of Non-renewal* (Competitive Foods Australia Limited 2007) at [1].

125 Andrew Terry and P D Giugni, 'Freedom of Contract, Business Format Franchising and the Problem of Goodwill' (1995) 23(4) *Australian Business Law Review* 242, 242.

protection. In reality, many franchisees do not have a chance to bargain for some protection. For instance, the examinations in this section show that a franchise contract rarely constrains the franchisor's non-renewal of a franchise contract. In franchising practice, the terms of the agreement are frequently drafted to protect the franchisor's interests.¹²⁶ Unsurprisingly, the contract's terms are preferable to the franchisor, not the franchisee. In some cases, a franchisee may not have an opportunity to renew a franchise contract.¹²⁷ In other instances, the franchisee may be provided with an option to renew, but the franchisee may have to meet some requirements that would be onerous to the franchisee. These examples suggest that the terms of a franchise agreement may not protect a franchisee against a franchisor, particularly an opportunistic franchisor.

(2) *Regulation of non-renewal by the rules of law*

The comparison demonstrates that the regulation of the franchisor's non-renewal of a franchise contract by the rules of law is twofold.

First, some legal systems, such as the DCFR, may not regulate the franchisor's non-renewal of a franchise contract by specific-franchise law. General contract law may play a protective role for a franchisee in this regard. The comparison shows that, under the law of contract, the requirement of good faith could be utilized to limit the franchisor's discretion not to renew a franchise in the sense that a franchisor cannot refuse to renew a franchise agreement unreasonably. Nevertheless, the use of the principle of good faith as an open standard of conduct may be restricted. Particularly, courts may be reluctant to employ this standard on a regular basis. In other words, judges may confine themselves to using the good faith principle only in limited cases where fairness is exceptionally demanding. Thus, it would not be uncommon in practice that the requirement of good faith has not been utilized in the context of the franchisor's non-renewal.

Second, other legal systems, such as Australia, may have franchise relationship law regulating the franchisor's non-renewal of a franchise contract through renewal rules. In this case, franchise-specific law rules seem to provide a franchisee with a high degree of protection since they are mandatory rules that do not allow the exclusion or deviation from the rules. This character of

126 Francesca R Turitto and others, 'Anatomy of a Franchise Dispute: Lessons for Transactional Lawyers Drafting Franchising Agreements' (2016) 14(5) *International Journal of Franchising Law* 3, 9. It might be possible that an agreement to renew a franchise contract could be made on an ad hoc basis. That is, the extension of the duration of the contract's term could be made at some point during a franchise contract. In doing so, the franchisee may employ the contract law rules of offer and acceptance. For example, the franchisee may propose to extend the term of the contract for a specified period in exchange for some consideration, such as renewal fees. If the franchisor assents to that proposal, this agreement will result in the continuity of the contract after the expiration.

127 Bundy and Einhorn (n 30) 209.

the rules would prevent any harm caused to a franchisee by the franchisor's non-renewal. Therefore, I propose that comprehensive franchise law contain the rules regulating the renewal of a franchise contract with a fixed term in the following two aspects: the procedure for renewing a franchise contract and the franchisor's discretion not to renew a franchise contract. Guidelines for the formulation of these rules will be provided in the following headings (3) and (4).

(3) *Renewal of a franchise contract with a fixed term*

'(1) A franchise contract with a definite term is extinguished at the end of the agreed period. Nevertheless, the term of the contract may be renewed by virtue of paragraph (2).

(2) The franchisee may give the franchisor written notice of its wish to renew at least 90 calendar days before the date of the expiry of the contract. Upon receipt of the franchisee's notice, the franchisor must notify the franchisee of its intention in writing within 30 calendar days. If the franchisor fails to notify the franchisee of its intention within a specified period, the term of the contract is deemed to have been renewed for an indefinite period.'

The first paragraph of the proposed model rules formulates a general principle that a franchise contract with a definite period will automatically expire at the end of that period.¹²⁸ This principle aims to create certainty concerning the end of a franchise relationship. This certainty would help the parties to a franchise contract shape their expectations at the beginning of the contract and prepare themselves when the expiration date is approaching. Thus, according to this principle, there is no need for a franchisor to give a franchisee warning notice to assert the expiry of the term of a franchise contract. In this regard, the franchisor's failure to renew a franchise contract or enter into a new contract will not constitute any liability for breach of contract unless the franchisor commits to do so.

The proposed rules provide that a franchisee may renew a franchise agreement by following the notification procedure enumerated in the second paragraph. According to the second paragraph, the franchisee who wishes to renew a franchise contract should notify the franchisor in writing of the intention to renew. More importantly, the franchisee should give the franchisor notice of its wish at least 90 calendar days before the agreement expires. A requirement of 90 days is set to provide the franchisee with sufficient time to prepare for some exit strategies. For example, this notice requirement will remind the

128 In terms of constructing a franchise contract's term, the franchisor and the franchisee may agree upon the expiration date in several ways. In general, the parties may specify the expiry date by referring to calendar days. For example, a franchise contract may state that the contract shall expire on October 31, 2005. See *Hubbard Auto Center Inc v General Motors Corp* 422 F Supp 2d 999, 1001 (ND Ind, 2006) 1001.

franchisee that it can renew a franchise contract before the 90-day period is approaching. The franchisee will also have enough time to prepare to shut the franchised business down or advertise the business to a replacement franchisee in case the franchisor refuses to renew the contract.

Upon receipt of the franchisee's notice of its wish to renew, the notified franchisor should be required to decide whether to renew the franchise contract and inform the franchisee of its intention within 30 calendar days. A requirement of 30 days aims to urge the franchisor not to ignore the franchisee's wish to renew. Without a compulsory timeframe, the franchisor may delay deciding on the franchisee's proposal, which would cause harm to the franchisee's benefits. For example, the requesting franchisee may spend some expenses to its detriment because the franchisee anticipates that the franchisor will renew a franchise contract. Thus, the franchisor must decide and inform the franchisee within a specified period.¹²⁹ Otherwise, a franchise contract will be deemed to have been renewed for an indefinite term. To illustrate, if a 5-year franchise contract ends on 31 May 2023, a franchisee shall inform the franchisor of its wish to renew the term of the agreement in writing by 8 March 2023 at the latest. Suppose the franchisee's letter is delivered to the franchisor on 8 March 2023. In that case, the franchisor shall notify the franchisee of its intention by 4 April 2023. If the franchisor does not inform the franchisee by 4 April 2023, the expiring franchise contract will be deemed to have been renewed for another successive term after the expiry of the contract.

(4) *Requirement of good faith*

A question may arise as to whether the franchisor should be required to have legitimate grounds for refusing to renew a franchise contract. In my opinion, the renewal rules should not require the franchisor to have grounds for the non-renewal of the agreement because constraining the franchisor's intention not to renew may induce the franchisor to offer prospective franchisees a franchise contract for an indefinite period. The possible argument is that strict regulation over the franchisor's non-renewal of a franchise contract would make the franchisor struggle to control the quality and standards of franchised businesses. For example, underperforming franchisees may be retained in a franchise system if the franchisor is required to renew a franchise contract with those franchisees unless the franchisor can state grounds for the non-renewal.¹³⁰ Thus, the franchisor would prefer an indefinite term of a franchise contract because, in some legal systems, a franchise agreement with an indeter-

¹²⁹ It should be mentioned that the proposed rule does not require the franchisor to renew the term of the agreement for another successive term. Nor does the rule require the franchisor to provide reasons for its intention. In this respect, the franchisor will always have choices to make. For example, the franchisor may refuse to renew the term of an expiring franchise agreement if the franchisor intends to abandon a franchising business model in the future.

¹³⁰ Bundy and Einhorn (n 30) 209 – 11.

minate term is conveniently terminated. For example, under the DCFR, IV.E. – 2:302(1) permits the franchisor to terminate a franchise contract with an indefinite term by giving the franchisee notice.¹³¹

Nevertheless, it does not mean that a franchisor can refuse to renew a franchise contract opportunistically. As proposed in 5.2.5.2, the franchisor should be required to act towards the franchisee in accordance with the principle of good faith. This good faith requirement also applies when the franchisor decides not to renew a franchise agreement. In this case, the franchisor cannot arbitrarily refuse to renew a franchise. For instance, it should be contrary to good faith if the franchisor refuses to renew a franchise contract with the aim of unfairly forfeiting the franchisee's local goodwill.¹³² The principle of good faith and fair dealing may require the franchisor to provide reasonable grounds for the non-renewal of a franchise agreement in some exceptional cases. Thus, I believe that the requirement of good faith can constrain the franchisor's non-renewal of a franchise contract that would inflict harm or damage to the franchisee's legitimate interests.

5.3.5.3 Conclusions

– Concluding remarks

The comparative examination shows that the franchise legal framework of the DCFR, the USA, and Australia reasonably protects a franchisee in the event of the franchisor's non-renewal of a franchise contract. Although the franchisor is free not to renew a franchise contract, the franchisor's non-renewal may be regulated to protect a franchisee in two cases. First, the franchisor may be required to give the franchisee written notice of its decision not to renew. This requirement can be imposed on the franchisor by the terms of a franchise contract or the rules of franchise relationship law that would prepare the franchisee for the end of a franchise relationship. Second, the franchisor's refusal may be constrained. A franchise contract may require the franchisor not to refuse to renew unreasonably or against the requirement of good faith. The franchisor's refusal may be regulated by franchise relationship law rules that require the franchisor to have justified grounds for the non-renewal.

¹³¹ Paragraph (2) of that provision ensures the fairness of the franchisor's termination by conferring a right to damages on the franchisee in the case of an unreasonable notice period. That is, the franchisor may be held liable for damages if a period of the notice is not of reasonable length, considering some factors enumerated in IV.E. – 2:302(3).

¹³² Bundy and Einhorn (n 30) 209.

– *Key recommendations*

(1) *Regulation of renewal of a franchise contract*

For a franchise contract with a definite term, comprehensive franchise law should contain a renewal provision, affirming that the term of a franchise contract expires on the expiration date. In this case, a franchisor is free to decide whether to renew an expiring franchise contract for an additional term. The renewal provision should regulate the procedure for renewing a franchise contract by a franchisee to protect the franchisee's legitimate interests. Under the rule, the renewing procedure should be based on an exchange of written notice between the franchisor and franchisee.

(2) *Procedure for renewing a franchise contract*

A franchisee may propose to renew the term of a franchise contract before the term expires. In renewing a franchise contract, the franchisee should give the franchisor written notice of its wish to renew at least 90 calendar days before the expiration date. Upon receipt of the franchisee's notice, the franchisor should be required to inform the franchisee of its intention in writing within 30 calendar days. If the franchisor fails to notify the franchisee within 30 calendar days, the term of an incumbent franchise contract should be deemed to have been renewed for an indefinite period.

(3) *Requirement of good faith*

Besides regulating the renewal process, comprehensive franchise law should contain a provision constituting the duty to act in good faith, requiring the franchisor not to refuse to renew a franchise contract against the requirement of good faith. This good faith obligation may obligate the franchisor to provide reasonable grounds for the non-renewal of a franchise contract in some exceptional cases.

5.4 TERMINATION OF A FRANCHISE CONTRACT

5.4.1 Introduction

The continuation of a franchise relationship is generally essential to a franchisee. In reality, some franchisees may need to spend some time to operate a franchised business so that the franchisees can gain recoup their investment. Nevertheless, some franchisors may decide to discontinue a franchise relationship by terminating a franchise contract.¹³³ In these cases, the franchisor's

133 In this section, the term 'termination' is used as a generic term to mean a party's act of cancelling or discharging a franchise contract, resulting in the cessation of a franchise relationship.

termination of a franchise agreement would inflict loss on the franchisee's financial benefits, thereby triggering conflict between the franchisor and franchisee. Section 5.4 will examine the extent to which the franchise legal framework of the DCFR, the USA, and Australia regulates the franchisor's termination of a franchise contract.¹³⁴ In examining the selected legal systems' legal frameworks, the description of the rules of law and the terms of a franchise contract regulating the franchisor's termination will be taken in sections 5.4.2, 5.4.3, and 5.4.4, respectively. Then, the comparative analysis of the franchise legal frameworks will be conducted in section 5.3.5.

5.4.2 The Draft Common Frame of Reference (DCFR)

5.4.2.1 Introduction

The DCFR's franchise legal framework regulates the franchisor's termination of a franchise contract through the rules of the DCFR and the terms of a franchise contract. Under the DCFR, the specific contract law rules in Book IV will apply to the termination of a franchise contract for an indefinite period.¹³⁵ Conversely, the termination of a franchise contract for a fixed period will be subject to the general contract law rules in Book III. This section will examine these applicable rules in subsection 5.4.2.2. A franchise contract may contain termination clauses establishing the franchisor's right to terminate. This section will also explore how the termination clauses of a franchise contract regulate the franchisor's termination in subsection 5.4.2.3. In the end, conclusions about the regulation of the franchisor's termination of a franchise contract under the DCFR will be drawn in subsection 5.4.2.4.

5.4.2.2 Regulation of termination by the rules of the DCFR

– Franchise contract for a definite period

A franchisor may terminate a franchise agreement with a fixed term by following requirements for termination laid down by general contract law rules in Book III. In principle, a franchisor must have grounds for terminating a fixed term franchise contract.¹³⁶ In Section 5 of Book III, the franchisor may terminate a franchise contract for the franchisee's fundamental non-performance of

¹³⁴ For the sake of comprehensiveness, this section will examine the regulation of the franchisor's termination of a franchise contract that is concluded for an indefinite and definite period.

¹³⁵ According to the Definitions, termination is defined to mean bringing an existing right, obligation, or legal relationship to an end with prospective effect except in so far as otherwise provided. See Bar and Clive (n 9) 81.

¹³⁶ The DCFR, III. – 3:502 to III. – 3:505.

an obligation.¹³⁷ In terminating a franchise contract for the franchisee's fundamental non-performance, the franchisor may terminate the contract with an immediate effect.¹³⁸ In other words, the franchisor needs not to provide the franchisee with the right to cure if the time for performance has expired.¹³⁹ For example, the franchisor may terminate a franchise contract immediately if the franchisee breaches a franchise contract by selling the others' goods in competition with the franchisor's products.¹⁴⁰

A franchisor may terminate a franchise contract for other grounds prescribed by III. – 3:503, 3:504 and 3:505. For example, III. – 3:503 establishes the right to terminate in the case of a delay in performance, which is not fundamental. According to this article, the franchisor may terminate a franchise contract for the franchisee's late performance if the franchisor gives the franchisee a reasonable period for performing, but the franchisee fails to perform the obligation within a specified period. The franchisor may terminate a franchise contract for the franchisee's anticipated non-performance. According to III. – 3:504, the franchisor may terminate the contract if the franchisee has declared that the performance of an obligation will not be made or if it is clear that there will be no performance by the franchisee. In both cases, the franchisee's non-performance must be material.

– *Franchise contract for an indefinite period*

A franchisor may terminate a franchise contract with an indefinite term by giving a franchisee notice of termination.¹⁴¹ In Book IV, IV.E. – 2:302(1) provides that the parties to a contract with an indefinite term may terminate the contractual relationship by giving notice to the other.¹⁴² Nevertheless, the franchisor is not required to provide good reasons for the purported

137 The right to terminate for fundamental non-performance is recognized by III. – 3:502(1). Paragraph (2) of III. – 3:502 defines the expression 'fundamental non-performance' to include two independent situations. In short, the first situation is that the debtor's non-performance deprives the creditor of what the creditor was entitled to expect under the contract. In this case, the debtor must foresee or could reasonably be expected to have foreseen that result at the time of conclusion of the contract. The second situation is that the debtor's non-performance was intentional or reckless and gives the creditor reasons to believe that the debtor's future performance cannot be relied on.

138 Bar and Clive (n 9) 856.

139 The DCFR, III. – 3:203, in conjunction with III. – 3:202(2). These provisions are not mandatory. In light of II. – 1:102(2), the parties may agree to deviate from or vary the effect of the provisions. For example, under a franchise contract, the franchisor may be required to provide the franchisee with a reasonable period for correcting the substantial default before terminating a franchise contract.

140 Bar and Clive (n 9) 855.

141 According to the commentaries, the term of a contract will be considered indefinite if the parties do not specify the duration of the contract or the parties explicitly provide that the term is indefinite. See Bar and Clive (n 6) 2303-304.

142 This provision is applied to a franchise contract by virtue of IV.E. – 1:101.

termination since the drafters of the DCFR provide that a good reason is not a conditional element of the right to terminate under IV.E. – 2:302.¹⁴³ Theoretically speaking, the franchisor may terminate a franchise contract even for no good reason. Despite this, it could be argued that the franchisor is still required to act in accordance with the requirement of good faith and fair dealing by virtue of III. – 1:103(1). In this case, the franchisor may not be able to terminate a franchise contract in a way that harms the franchisee's interests.

It should be noted that reasonable notice of termination is not a prerequisite for valid termination. In other words, a franchisor is not required to notify a franchisee reasonable time before a franchise contract is terminated. Thus, a franchise contract can validly be terminated even though the franchisor does not give the franchisee reasonable notice of termination.¹⁴⁴ In case of unreasonable notice, the liability rules may protect the franchisee's interests. According to IV.E. – 2:302(2), in conjunction with IV.E. – 2:303(1), the franchisor will be liable for damages if the franchisor does not provide the franchisee with reasonable notice of termination. In the context of the franchisor's termination, the reasonableness of the notice is designated as IV.E. – 2:302(5) imposes a minimum period of notice for termination of a franchise contract by a franchisor.¹⁴⁵ That is, the franchisor is required to provide the franchisee with a one-month notice for the first year, two-month notice for the second, three-month notice for the third, four-month notice for the fourth, five-month notice for the fifth, and six-month notice for the sixth and subsequent years during which the contractual relationship has lasted. Thus, the franchisor's failure to follow this requirement would expose the franchisor to liability for damages.

5.4.2.3 Regulation of termination by the terms of a franchise contract

The terms of a franchise contract may regulate the franchisor's termination of a franchise contract. Under the DCFR, the principle of party autonomy is expressly recognized by II. – 1:102. Paragraph (1) of II. – 1:102 provides that parties are free to make a contract and determine its contents, subject to any applicable mandatory rules. In terminating a contract, the drafters of the DCFR suggest that the parties may agree on the contractual clause conferring the right to terminate for any reason or even for no reason.¹⁴⁶ In light of this principle, a franchise contract may incorporate the termination clauses providing the franchisor with the right to terminate a franchise contract. In this

¹⁴³ Bar and Clive (n 6) 2306.

¹⁴⁴ Ibid 2305.

¹⁴⁵ This requirement is mandatory; hence, the parties may not exclude the application of the requirement or derogate from or vary its effects.

¹⁴⁶ Bar and Clive (n 9) 704.

respect, the DCFR regulates the conferment of the franchisor's right to terminate to some extent.

According to IV.E. – 2:304(1), the right to terminate for non-performance of an obligation can only be constituted if the non-performance is fundamental.¹⁴⁷ In this case, the terms of a franchise contract establishing the right to terminate for minor non-compliance will produce no effect. The rationale underlying the rule is that it would be inappropriate to terminate a long-term relationship for a minor breach of contract. The drafters of the DCFR elucidate that the contracting parties typically invest considerable money in a long-term contract. Furthermore, the parties often rely on the continuity of the contractual relationship. Accordingly, terminating a contract for non-performance of an obligation should be permitted only in the case of fundamental non-performance of an obligation.¹⁴⁸

IV.E. – 2:304 does not define the expression 'fundamental non-performance'. Despite the lack of definition, the drafters of the DCFR suggest that the reference can be made to the tests under III. – 3:502.¹⁴⁹ In the franchising context, a franchisor may retain the right to terminate a franchise contract in the following two situations. First, the franchisee's non-performance is intentional or reckless and gives the franchisor reason to believe that the franchisor cannot rely on the franchisee's future performance. Second, the franchisee's non-performance substantially deprives the franchisor of what the franchisor was entitled to expect under the agreement.¹⁵⁰ As can be seen, IV.E. – 2:304 restricts the incorporation of the termination clauses permitting a party to terminate a contract for minor non-performance. In other words, this article does not prevent the parties from incorporating the termination provisions allowing termination of a contract on other bases. For example, the franchisor may hold the right to terminate a franchise contract for the franchisee's insolvency or liquidation.

IV.E. – 2:304 does not regulate the procedure under which the parties exercise the right to terminate. In this respect, the franchisor may retain the right of immediate termination upon the occurrence of the franchisee's sub-

147 This article applies to a franchise contract by virtue of IV.E. – 1:101(1). Since IV.E. – 2:304 is mandatory, any agreement that excludes the application of the rule will be invalid by virtue of IV.E. – 2:304(2), in conjunction with II. – 1:102(1).

148 Bar and Clive (n 6) 2317.

149 Ibid 2317.

150 The franchisee's non-performance of an obligation that does not meet the two tests mentioned earlier would be considered insignificant and does not allow the franchisor to terminate a franchise contract on the basis of non-performance. The example of the franchisee's minor non-performance may be taken from Illustration 1 of the Comments to IV.E. – 2:304. This Illustration exemplifies that a hamburger restaurant franchisor provides its franchisees with a sales manual with hundreds of pages and thousands of very detailed instructions. Although the franchise contract states that all the instructions are of the essence of the contract, the franchisor may not terminate a franchise contract if the franchisee sells hamburgers that are on average 2% too hot. See *ibid* 2318.

stantial non-performance. However, the franchisee may hold the right to cure. Taking the ICC's Model Contract as an illustration, article 26.1 provides that a substantial breach of the obligation by the other party justifies an immediate termination of the franchise contract.¹⁵¹ This provision makes an exception in case the breach is, by nature, curable. Thus, if a franchisor purports to terminate a franchise contract for the franchisee's breach of contract, the franchisor shall give the franchisee 30 days to rectify the curable breach. If the franchisee fails to cure the breach within that period, the franchisor's termination will become effective.¹⁵²

5.4.2.4 Conclusions

The DCFR regulates the franchisor's termination of a franchise contract with an indefinite and definite term differently. On the one hand, the DCFR permits a franchisor to terminate a franchise contract with an indefinite term any time without cause. In this case, the franchisor is required to give the franchisee notice of termination. The franchisor will be liable for damages towards the franchisee if the notice is unreasonable. On the other hand, a franchisor needs to have grounds for terminating a franchise contract with a definite term. Typically, the franchisor may terminate a franchise contract for the franchisee's non-performance of an obligation. In this case, the franchisee's non-performance must be fundamental because the DCFR does not allow the franchisor to terminate a franchise contract or retain the contractual right to terminate a franchise contract for the franchisee's insignificant non-performance. The franchisor may terminate or hold the contractual right to terminate a franchise contract on other grounds, such as terminating a franchise contract due to the franchisee's anticipated non-performance or the franchisee's insolvency. In the latter case, the terms of a franchise contract will play a vital role in enumerating grounds for termination.

5.4.3 The United States of America (USA)

5.4.3.1 Introduction

The rules of law regulating the franchisor's termination of a franchise contract vary. In seventeen US states (termination states), franchise relationship law

151 Article 26.2 of the ICC's Model Contract defines the expression 'substantial breach' to mean any failure of a party to carry out all or part of the obligations under a franchise contract resulting in such detriment to the other party as to substantially deprive such other party of what it is entitled to expect under the contract.

152 International Chamber of Commerce (n 12) 40.

contains the rules regulating the franchisor's termination.¹⁵³ In other jurisdictions, common contract law rules will apply to the franchisor's termination of a franchise contract. In this case, the terms of a franchise contract may play a significant role in regulating the franchisor's right to terminate. This section will examine the extent to which the rules of franchise law and contract law apply to the franchisor's termination in subsection 5.4.3.2 and 5.4.3.3, respectively. Subsection 5.4.3.4 will explore how the termination clauses of a franchise contract govern the franchisor's termination. In the end, conclusions about the regulation of the franchisor's termination in the USA will be made in subsection 5.4.3.5.

5.4.3.2 Regulation of termination by the rules of franchise relationship law

The seventeen termination states regulate the franchisor's termination through termination rules of franchise relationship legislation.¹⁵⁴ These termination rules have been introduced to protect franchisees against the franchisor's unfair termination or termination without good cause.¹⁵⁵ Thus, the termination rules will apply to the termination of a franchise agreement, irrespective of whether a franchise contract is concluded for a definite or indefinite period.¹⁵⁶ Some courts affirm this application. For example, in *7-Eleven v Dar*, the court held that the termination requirement of the Illinois franchise law applied equally to the early termination of a fixed-term franchise contract and any termination of a franchise contract for an indefinite period.¹⁵⁷ In the termination states, the franchisor's termination of a franchise contract with a definite and in-

153 These termination states are Arkansas, California, Connecticut, Delaware, Hawaii, Illinois, Indiana, Iowa, Michigan, Minnesota, Mississippi, Missouri, Nebraska, New Jersey, Rhode Island, Virginia, and Wisconsin.

154 Arkansas: AR ST, § 4-72-204(b); California: CA BUS & PROF, § 20020; Connecticut: CT ST, § 42-133f (a); Delaware: DE ST TI 6, § 2555; Hawaii: HI ST, § 482E-6(2)(H); Illinois: IL ST CH 815, § 705/19(b); Indiana: IN ST, 23-2-2.7-3(Sec.1); Iowa: IA ST, § 523H.7(2) and IA ST, § 537A.10(b); Michigan: MI ST, 445.1527(c); Minnesota: MN ST, § 80C.14(Subd.3); Mississippi: MS ST, § 75-24-53; Missouri: MO ST, 407.405; Nebraska: NE ST, § 87-404(1); New Jersey: NJ ST, 56:10-5; Rhode Island: RI ST, § 6-50-4(a); Virginia: VA ST, § 13.1-564; and Wisconsin: WI ST, 135.04.

155 Jason J Stover, 'No Cure, No Problem: State Franchise Laws and Termination for Incurable Defaults' (2004) 23 Franchise Law Journal 217, 217. See also *Wright-Moore Corp v Ricoh Corp* 908 F2d 128 (CA7 (Ind), 1990) 137-38; *Capital Equipment Inc v CNH America LLC*, 471 F Supp 2d 951 (ED Ark, 2006) 957-58.

156 The franchisor's termination of a franchise agreement can be actual and constructive termination. In some cases, the franchisor may not officially terminate a franchise contract. In other words, the franchisor may engage in certain conduct that constructively terminates the agreement. For example, the realignment of franchisee's sales territory could constitute constructive termination of a franchise. See eg *Petereit v SB Thomas Inc* 63 F3d 1169 (CA2 (Conn), 1995) 1181-182; *In re Kirkwood Kin Corp v Dunkin' Donuts Inc* 1997 WL 529587 (Del Super, 1997) 9.

157 *7-Eleven Inc v Dar* 757 NE 2d 515, 521-22, 258 Ill Dec 826, 832-33, 325 Ill App 3d 399 (Ill App 1 Dist, 2001) 407.

definite term will fall within the ambit of the termination rules. The termination rules generally regulate the franchisor's termination in the following two aspects.

– *Procedural requirements for termination*

The franchisor's notice of termination is regulated in all the seventeen termination states (notice states), except for Virginia. In the notice states, the termination rules require a franchisor to give a franchisee notice of termination when seeking to terminate a franchise contract.¹⁵⁸ In all the notice states, the termination rules establish a so-called 'wind-up period' requiring the franchisor to provide the franchisee with the notice within a specified period in advance of the termination.¹⁵⁹ In the notice states, the wind-up duration is designated, ranging from a minimum of 24 hours to a maximum of 90 days.¹⁶⁰ This notice requirement may not apply in some cases, which vary among the notice jurisdictions. For example, in Wisconsin, the grantor (franchisor) does not have to give the dealer (franchisee) at least 90 days' prior termination notice if the reason for termination is insolvency, the occurrence of an assignment for the benefit of creditors or bankruptcy.¹⁶¹ In Rhode Island, the 60 days prior notice requirement will not apply if the reason for termination is in the event the dealer (franchisee) voluntarily abandons a franchise relationship; the franchisee is convicted of a felony offense related to the franchised business; to name a few.¹⁶²

Some notice states may not allow a franchisor to terminate a franchise contract immediately without a cure. In nine notice states, the franchisor is required to allow the franchisee to cure or rectify the alleged defaults within a specified period before the termination is effective.¹⁶³ The duration for the rectification varies, ranging from a minimum of 24 hours to a maximum of 90 days. For instance, in Rhode Island, if the reason for the franchisor's ter-

158 Arkansas: AR ST, § 4-72-204(b); California: CA BUS & PROF, § 20020; Connecticut: CT ST, § 42-133f (a); Delaware: DE ST TI 6, § 2555; Hawaii: HI ST, § 482E-6(2)(H); Illinois: IL ST CH 815, § 705/19(b); Indiana: IN ST, 23-2-2.7-3(Sec.1); Iowa: IA ST, § 523H.7(2) and IA ST, § 537A.10(b); Michigan: MI ST, 445.1527(c); Minnesota: MN ST, § 80C.14(Subd.3); Mississippi: MS ST, § 75-24-53; Missouri: MO ST, 407.405; Nebraska: NE ST, § 87-404(1); New Jersey: NJ ST, 56:10-5; Rhode Island: RI ST, § 6-50-4(a); and Wisconsin: WI ST, 135.04.

159 These eleven states are Arkansas, California, Connecticut, Delaware, Illinois, Indiana, Iowa, Michigan, Minnesota, Mississippi, and Missouri.

160 However, in Hawaii, the franchise relationship statute opts for the test of a reasonable period, which will be decided on a case-by-case basis.

161 WI ST, 135.04.

162 RI ST, § 6-50-4(a).

163 Arkansas: AR ST, § 4-72-204(b); California: CA BUS & PROF, § 20020; Hawaii: HI ST, § 482E-6(2)(H); Illinois: IL ST CH 815, § 705/19(b); Iowa: IA ST, § 523H.7(2) and IA ST, § 537A.10(b); Michigan: MI ST, 445.1527(c); Minnesota: MN ST, § 80C.14(Subd.3); Rhode Island: RI ST, § 6-50-4(a); and Wisconsin: WI ST, 135.04.

mination is the franchisee's violation of law, regulation, or standard relating to public health or safety, the dealer (franchisee) shall be provided 24 hours to cure that violation. Furthermore, the dealer (franchisee) has 30 days to cure the general defaults. A question arises whether the franchisor must give the franchisee the right to cure if the franchisee's default is incurable.¹⁶⁴ In this case, it seems to me that case law is not uniform. According to Stover, there are two diverse trends in court decisions. Summarily, some courts provide that the notice and cure requirement may not strictly be enforced; the opportunity to cure is not provided if the default is unlikely to be fixed. Others provide that the requirement of notice and rectification must strictly be followed; a franchisor must provide a franchisee with the right to cure a default, irrespective of whether the default is correctable.¹⁶⁵

– *Legitimate grounds for termination*

In all the termination states, a franchisor must have legitimate grounds for termination of a franchise contract. The grounds for termination can be characterized into three groups as follows.

(1) *Just cause*

Fourteen termination states require a franchisor to have just cause for termination of a franchise contract.¹⁶⁶ In all fourteen states (good cause states), except for Virginia, the franchisor is required to have good cause for the termination.¹⁶⁷ Although the definition of good cause may vary from state to state, the franchisee's failure to comply with a franchise contract primarily constitutes good cause for the franchisor's termination.¹⁶⁸ For example, in Michigan,

164 The term 'incurable default' is used in the sense that the default cannot practicably be cured within a statutory cure period. For example, a franchisee may fail to achieve the volume of sales of products in the past financial year, which is incurable in the present fiscal year.

165 Stover (n 155) 221-22.

166 Arkansas: AR ST, § 4-72-202(a)(1); California: CA BUS & PROF, § 20020; Connecticut: CT ST, § 42-133f(a); Delaware: DE ST TI 6, § 2552(a); Hawaii: HI ST, § 482E-6(2)(H); Illinois: IL ST CH 815, § 705/19; Indiana: IN ST, 23-2-2.7-1(7); Iowa: IA ST, § 523H.7(1) and IA ST, § 537A.10(7)(a); Michigan: MI ST, 445.1527(c); Minnesota: MN ST, § 80C.14(Subd.3(b)); Nebraska: NE ST, § 87-404(1); New Jersey: NJ ST, 56:10-5; Virginia: VA ST, § 13.1-564, and Wisconsin: WI ST, 135.04.

167 The law of Virginia opts for the term 'reasonable cause' for cancellation. However, the statute does not define the expression. Despite the lack of definition, case law may provide a useful example. For instance, the Court in *GM Garrett Realty* held that failure to pay fees might be considered a reasonable cause for termination of a franchise agreement. See *GM Garrett Realty Inc v Century 21 Real Estate Corp* 17 Fed Appx 169, 172, 2001 WL 980558 (CA4 (Va), 2001) 2.

168 The good cause states may differ as to what constitutes the franchisee's failure to comply with a franchise agreement. For example, in Connecticut, Hawaii, and Minnesota, the laws require that any requirement, obligation, or provision of a franchise contract must be material. In California, Illinois, and Michigan, the franchise statutes require that the require-

the franchisee's failure to pay royalties, advertising fees, as well as the franchisee's failure to file monthly sales reports are sufficient to constitute good cause under the state relationship law.¹⁶⁹ Some good cause states may define the term 'good cause' to include other circumstances. For example, in Illinois and Minnesota, the franchisor may terminate a franchise contract for good cause if the franchisee voluntarily abandons the franchise business or engages in any conduct that substantially impairs the goodwill associated with the franchisor's trademark, trade name, service mark, logotype or other commercial symbols.

(2) *Good faith*

Among the termination states, Delaware and Indiana employ the concept of good faith as a basis for termination of a franchise contract by a franchisor. In Delaware, the rule of Franchise Security Law provides that any contractual provision that permits the franchisor to make an unjust termination of a franchise is unenforceable because of the violation of public policy.¹⁷⁰ Likewise, in Indiana, the Deceptive Franchise Practices Law's rule makes it unlawful for a franchise agreement to contain a provision that permits unilateral termination of a franchise in bad faith.¹⁷¹ The laws of these two states do not define the term 'bad faith'. Despite the lack of definition, the Delaware court in *Globe Liquor v Four Roses Distillers* provided that the definition of a similar expression provided by other statutes could be followed. For example, the definition of good faith provided by the Uniform Commercial Code (UCC) can be referred to.¹⁷² According to section 1-201(20) of the UCC, good faith means honesty in fact and the observance of reasonable commercial standards of fair dealing. Emerson suggests that the lack of good faith may characterize conduct in bad faith, meaning behaviors that violate community standards of decency, fairness, or reasonableness.¹⁷³

ment, obligation, or provision of a franchise contract must be lawful. Some states, such as Iowa, combine the materiality and lawfulness elements. That is, the franchisee's failure to comply with any material lawful requirement of the franchise agreement will constitute good cause in Iowa. Additionally, the law of most good cause states requires that the franchisee's failure in compliance with a franchise contract must be substantial. The law of Hawaii, Illinois, Iowa, and Michigan is silent in this regard.

169 *Two Men and a Truck/International Inc v Two Men and a Truck/Kalamazoo Inc* 949 F Supp 500 (WD Mich, 1996) 505.

170 DE ST TI 6, § 2552(a). Under the Delaware Franchise Security Law, the franchisor's termination in bad faith is deemed to be unjust or to have been made unjustly.

171 IN ST, 23-2-2.7-1(7). Unlike the law of Delaware, the Indiana franchise statute prohibits unilateral termination in bad faith made by both parties.

172 *Globe Liquor* (n 102) 22.

173 Robert W Emerson, 'Franchise Terminations: Good Cause Decoded' (2016) 51 Wake Forest Law Review 103, 115-16.

(3) *Reasons for immediate termination*

A franchisee's specific conduct may provide grounds for the franchisor's termination without prior notice. The conduct that provides bases for immediate termination may vary from state to state. For example, in Missouri, a franchisor can terminate a franchise contract without providing the franchisee with a 90-day notice if the grounds for the termination are, for example, criminal misconduct, fraud, abandonment, bankruptcy, or insolvency of the franchisee.¹⁷⁴ In Rhode Island, a franchisor may immediately terminate a franchise agreement when the franchisee engages in any substantial act that would significantly impair the goodwill of the franchisor's trade mark, tradename, service mark, logotype, or other commercial symbol.¹⁷⁵ In sum, the franchisee's conduct that adversely affects the franchise business operation typically permits the franchisor's immediate termination of a franchise contract.

5.4.3.3 *Regulation of termination by the rules of common law*

Non-termination states do not have franchise relationship legislation regulating the franchisor's termination of a franchise contract for an indefinite and definite period. In these states, common contract law will apply to the franchisor's termination of a franchise contract. This subsection will explore how the rules of contract law regulate the franchisor's termination of a franchise contract in the following two italicized headings.¹⁷⁶

– *Franchise contract for a definite period*

In common law, unless a franchise contract provides otherwise, a franchisor may terminate a franchise contract with a definite term by way of common law rescission.¹⁷⁷ However, common law rules would not allow a franchisor to rescind a fixed-term franchise contract conveniently. First, the rules require the franchisor to have grounds for rescinding the contract. In common law, the franchisor may rescind a franchise agreement based on two grounds: the franchisee's material breach of a franchise agreement and the franchisee's repudiation of the agreement.¹⁷⁸ In this case, it seems that the franchisor cannot rescind a franchise contract without justifiable cause. Second, a franchisor may be constrained in rescinding a franchise contract for several reasons.

¹⁷⁴ MO ST, 407.405.

¹⁷⁵ RI ST, § 6-50-4(a).

¹⁷⁶ It should be noted that common contract law rules may not be applied uniformly throughout the USA. Some state courts may adopt different common law rules or take different views when deciding the case.

¹⁷⁷ The effects of rescission of a contract in American law will be addressed later in 5.5.3.4.

¹⁷⁸ Reviews on general common law rules on rescission of a contract for these two grounds and its limitations have been conducted in 4.4.3.4 in chapter 4. These general rules can be applied in the context of this subsection too.

For example, the franchisor may not rescind a franchise contract because of the unclean-hands doctrine, which would bar the franchisor from seeking equitable relief.¹⁷⁹ Alternatively, the franchisor may not rescind a franchise contract if it waives the right of rescission by pursuing an award of damages.¹⁸⁰

– *Franchise contract for an indefinite period*

Some state courts recognize that a franchise contract with an indefinite period is valid.¹⁸¹ Unless a franchise contract provides otherwise, a franchisor has to comply with the following general contract law rules when terminating the contract. That is, the franchisor may terminate a franchise contract with an indefinite period after the contract runs for a reasonable period. In this case, the franchisor may terminate the contract at will by giving the franchisee reasonable notice of termination.

First, the contract law's rule provides that a contract's term will run for a reasonable time before it can be terminated.¹⁸² In this respect, the franchisor may have to wait until a franchise contract has lasted for a reasonable period before the agreement is terminable. The idea behind this rule is that a reasonable period would allow the party to recoup its labor, investment, expenditure incurred in reliance upon the contract.¹⁸³ For example, in *A R Dervaes Co v Houdaille Industries*, the Delaware court held that the franchisee could expect that the franchise agreement continues for a reasonable time because the franchisee has to assume the risk of inventory destruction, maintain warehouse

179 See eg *Wuliger v Manufacturers Life Ins Co*, 567 F 3d 787 (6th Cir. 2009) 797; *Rocky Mountain Chocolate Factory, Inc v SDMS, Inc*, No. CIV A 06-CV01212PAB, 2009 WL 579516 (D Colo Mar 4, 2009) 12; *Kennedy v Dabbieri*, 545 F Supp 3d 269 (ED Va 2021) 286.

180 *Larchmont Holdings, LLC v N Shore Servs, LLC*, 292 F Supp 3d 833, 859 (WD Wis 2017) 859.

181 Some courts may require the intention of the parties that a contract is effective indefinitely. See eg *Consumers Ice Co v US* 475 F2d 1161, 1166–67, 201 Ct Cl 116 (Ct Cl, 1973) 126; *Capital Investments Inc v Whitehall Packing Co Inc* 280 NW 2d 254, 261, 91 Wis 2d 178 (Wis, 1979) 193.

182 *Metal Associates Inc v Eastside Metal Spin & Stamp Corp* 165 F2d 163, 165 (CA2, 1948) 165, cited by *Diematic Mfg Corp v Packaging Industries Inc* 381 F Supp 1057 (DCNY, 1974) 1060; *Rothberg v Bernstein* 1990 WL 58902 (SDNY, 1990) 3. Whether a contract has run for a reasonable time is a matter of fact. Thus, the reasonable period will be determined by considering the circumstances surrounding the contract, the situation of the parties, and the subject matter of the agreement. See eg *William B Tanner Co Inc v Sparta-Tomah Broadcasting Co Inc* 716 F2d 1155 (CA Wis, 1983) 1159; *Uintah Basin Medical Center v Hardy* 54 P3d 1165, 1173, 2002 UT 92 (Utah, 2002) 30.

183 *Schultz v Onan Corp* 737 F2d 339 (CA Pa, 1984) 346; *Cambee's Furniture Inc v Doughboy Recreational Inc* 825 F2d 167 (CA8 (SD), 1987) 173; *Tapered Insulation Systems Inc v Schuller Intern Inc* 1998 WL 892238 (Tex App-San Antonio, 1998) 3.

facilities, and spend a substantial amount of money in inventory and accounts receivable.¹⁸⁴

Second, the contract law's rule provides that both parties may terminate an indeterminate contract at will and without cause.¹⁸⁵ In some states, this rule has been applied to terminating a franchise agreement with an indeterminate period as well.¹⁸⁶ However, at-will termination of an indefinite franchise contract may be subject to the requirement of good faith and fair dealing, and public policy. In this case, a franchisor could be held liable to a franchisee if the franchisor's termination at will is motivated by bad faith, retaliation, or malice, or violates public policy.¹⁸⁷

Third, in terminating an indefinite contract at will, the contract law's rule provides that the terminating party must provide the other party with reasonable notice of termination.¹⁸⁸ This rule is also applied to require the franchisor to give the franchisee reasonable notice of termination. In *McGinnis Piano & Organ Co v Yamaha Intern Corp*, the court explained that a reasonable notice period means the time period necessary to close out the franchise and minimize losses.¹⁸⁹ The interpretation of a reasonable notice period provided by the court in *McGinnis Piano & Organ Co* is said to be a well-developed principle in the franchising context.¹⁹⁰

184 In this case, the court concluded that the reasonableness requirement is satisfied because the franchise contract has lasted more than ten years. See *A R Dervaes Co v Houdaille Industries Inc* 7 Del J Corp L 173, 180, 1981 WL 7625 (Del Ch, 1981) 5.

185 See eg *Tanenbaum Textile Co v Sidran* 423 SW2d 635 (Tex Civ App, 1968) 637; *Lura v Multiplex Inc* 179 Cal Rptr 847, 849, 129 Cal App 3d 410 (Cal App 1 Dist, 1982) 413; *Jackson v Action for Boston Community Development Inc* 525 NE 2d 411, 412, 403 Mass 8 (Mass, 1988) 9; *Haynes Trane Service Agency Inc v American Standard Inc* 51 Fed Appx 786, 792, 2002 WL 1972281 (CA10 (Colo), 2002) 4.

186 See eg *McGinnis Piano & Organ Co v Yamaha Intern Corp* 480 F2d 474 (CA8, 1973) 479; *Trient Partners I Ltd v Blockbuster Entertainment Corp*, 83 F 3d 704 (C.A.5 (Tex.), 1996) 708; *Haynes Trane Service Agency*, *ibid*; *Sensormatic Sec Corp v Sensormatic Electronics Corp*, 249 F Supp 2d 703, 714 (D Md, 2003) 714.

187 See eg *Monge v Beebe Rubber Co* 316 A.2d 549, 551, 114 N.H. 130 (NH, 1974) 133; *Fortune v National Cash Register Co* 364 NE2d 1251, 1256, 373 Mass 96 (Mass 1977) 101; *DeRose v Putnam Management Co Inc* 496 NE2d 428, 429, 398 Mass 205 (Mass, 1986) 206; *Lang v Wal-Mart Stores East LP* 2015 WL 898026 (DNH, 2015) 9.

188 See eg *Benson Co-op Creamery Ass'n v First Dist Ass'n* 151 NW2d 422, 426, 276 Minn 520 (Minn, 1967) 526; *WKT Distributing Co v Sharp Electronics Corp* 746 F2d 1333 (CA Minn, 1984) 1335; *Elogren Paint Supply Co v Benjamin Moore & Co* 948 F2d 1082 (CA8 (Minn), 1991) 1084; *Italian & French Wine Co of Buffalo Inc v Negociants USA Inc* 842 F Supp 693 (WDNY, 1993) 698; *Sensormatic Sec Corp* (n 186); *Day Distributing Co v Nantucket Allserve Inc* 2008 WL 2945442 (D Minn, 2008) 8; *Latin American Music Co v American Soc of Composers Authors and Publishers* 593 F3d 95 (CA1 (Puerto Rico), 2010) 100.

189 *McGinnis Piano & Organ* (n 186).

190 *PC Connection, Inc v Syngy Ltd*, 2021 WL 57016 (Del Ch, 2021) 20.

5.4.3.4 Regulation of termination by the terms of a franchise contract

As the preceding subsection mentions occasionally, non-termination states may employ common contract law to govern the franchisor's termination.¹⁹¹ The law of contract generally permits a franchise contract to provide for the franchisor's right to terminate. In practice, Emerson says that a franchise contract normally plays a leading role in regulating the franchisor's right to terminate through the termination clauses.¹⁹² The franchisor's right of termination may be constructed under a franchise contract as the right to terminate at will, meaning the termination provisions allow a franchisor to terminate a franchise contract without cause.¹⁹³ In general, a franchisor can exercise this right at will without any restriction. Furthermore, some state courts may be reluctant to assert the requirement of good faith and fair dealing to constrain a franchisor from exercising its contractual right to terminate.¹⁹⁴ The reason is that courts do not want to interfere with what the parties unmistakably agree upon under a contract.¹⁹⁵

Other state courts may regulate the franchisor's exercise of the right to terminate at will through the principle of good faith. For example, in Georgia, a franchisor is able to terminate a franchise contract in good faith if the contract is terminable at will.¹⁹⁶ Thus, a franchisor may be held liable for breach of a contract if it terminates the agreement, which is motivated by bad faith or malice.¹⁹⁷ If the termination clauses do not expressly permit a franchisor to terminate a franchise contract at will, courts may be more willing to use the requirement of good faith and fair dealing to regulate the franchisor's right

191 Conversely, in the termination states, the rules of franchise relationship law will regulate the conclusion of termination clauses in a franchise contract. W Michael Garner, Relationship of common law of contracts to state and federal statutes, 2 Franch & Distr Law & Prac, §8:2, Westlaw Next, (October 2018). See also *General Motors Corp v New AC Chevrolet Inc* 263 F3d 296 (CA3 (NJ), 2001) 319. Thus, some franchise relationship statutes explicitly provide that the contractual terms will be unenforceable if the terms are prohibited by the laws. For example, the law of Michigan provides that a provision that permits a franchisor to terminate a franchise except for good cause is void and unenforceable. See MI ST, 445.1527(c).

192 Emerson, 'Franchise Contract Clauses and the Franchisor's Duty of Care toward Its Franchisees' (n 104) 949.

193 This at-will termination clause is generally held to be valid. See eg *J R Watkins Co v Rich* 235 NW 845, 846, 254 Mich 82 (Mi, 1931) 84; *Zapatha v Dairy Mart Inc* 408 NE2d 1370, 1376, 381 Mass 284 (Mass, 1980) 293.

194 See eg *Bushwick-Decatur Motors v Ford Motor Co* 116 F2d 675 (CA2, 1940) 676-77; *Dayan v McDonald's Corp* 466 NE2d 958, 971, 81 Ill Dec 156, 169, 125 Ill App 3d 972 (Ill App 1 Dist, 1984) 989; *Devery Implement Co v J I Case Co* 944 F2d 724 (CA10 (Ok), 1991) 728-29; *Applied Technology Inc v US JVC Corp* 1995 WL 433162, (CA10 (Utah), 1995) 2.

195 *Lindale Auto Supply Inc v Ford Motor Co* 1998 WL 104953, (Tex App-Hous (14 Dist), 1998) 8.

196 *Sheldon v Munford Inc* 950 F2d 403 (CA7 (Ind), 1991) 407.

197 *Fortune* (n 187) 104.

to terminate. For instance, in Utah, the Supreme Court in *Seegmiller v Western Men* held that, if there were no express provision of a franchise contract that allowed the franchisor to terminate without cause, it would be fair and reasonable to assume that the parties concluded the contract in good faith, intending that the agreement would not be canceled arbitrarily.¹⁹⁸ Notably, highest courts in other states have concurred with this precedent.¹⁹⁹

5.4.3.5 Conclusions

The regulation of the franchisor's termination of a franchise contract in the USA is twofold. First, a franchise relationship statute will strictly regulate the franchisor's termination in the termination states. Under the laws, a franchisor must follow some procedural requirements for terminating a franchise agreement. The franchisor must have legitimate grounds for termination, such as just cause and good faith. Since the rules are mandatory, a franchisor cannot exclude the termination rules through a contractual arrangement. Second, the franchisor's termination of a franchise contract will be governed by the terms of a franchise contract and common contract law rules in non-termination states. If a franchise contract's termination clauses provide for the franchisor's right to terminate, a franchisor may exercise that right without constraints unless some courts have compelling reasons to regulate the right to terminate by the covenant of good faith and fair dealing. If the termination clauses do not exist, a franchisor may resort to common law rules for terminating a franchise agreement with an indefinite term or rescinding a franchise contract for a definite period.

5.4.4 Australia

5.4.4.1 Introduction

The Franchising Code of Conduct (the Code) regulates the franchisor's termination of a franchise contract for a fixed period through certain termination rules in Division 5.²⁰⁰ In this case, the franchisor's termination of a franchise contract for an indefinite period will then be governed by common contract law rules. In both cases, a franchise contract may include the terms regulating the

198 *Seegmiller v Western Men Inc* 437 P2d 892, 894, 20 Utah 2d 352 (Utah, 1968) 353–54.

199 See eg *J R Watkins* (n 193) 84–85; *Atlantic Richfield Co v Razumic* 390 A2d 736, 742, 480 Pa 366 (Pa, 1978) 378.

200 The Code does not explicitly provide for the termination rules applying to the franchisor's termination of a franchise contract for an indefinite period. Furthermore, no court decision has been found, showing that the termination rules are utilized to regulate the franchisor's termination of an indefinite franchise agreement. Thus, it could be concluded at the outset that the Code does not apply to an indeterminate franchise agreement.

franchisor's termination insofar as the laws permit. This section will examine the rules of the Code and common law rules in subsections 5.4.4.2 and 5.4.4.3, respectively. Then, subsection 5.4.4.4 will explore the termination clauses of a franchise agreement regulating the franchisor's termination. In the end, conclusions about the regulation of the franchisor's termination of a franchise contract in Australia will be provided in subsection 5.4.4.5.

5.4.4.2 Regulation of termination by the rules of the Franchising Code of Conduct

Division 5 contains clauses 27, 28, and 29 regulating the franchisor's termination of a franchise agreement. Those three provisions prescribe termination rules applying to the franchisor's termination of a franchise agreement in three cases as follows: termination of a franchise agreement in case of breach by a franchisee, termination of a franchise agreement in case of no breach by a franchisee, and termination of a franchise agreement on particular grounds. The rules applying to these three cases are different and will be examined in the following three italicized headings.

– Termination in case of breach

A franchisor must follow the rules on the notice and cure in clause 27 if the franchisor proposes to terminate a franchise agreement based on the franchisee's breach of a franchise agreement.²⁰¹ As a starting point, the franchisor will have to follow the rules in clause 27 if the franchisee's breach is the basis for the franchisor's termination. According to the court in *Aura Enterprises v Frontline Retail*, the term 'breach' has two components: an obligation imposed on a franchisee by a franchise contract and a state of affairs that is inconsistent with that obligation. Thus, the court in *Frontline Retail* concluded that the terminating events under clause 27 would be triggered only when the franchisee engaged in conduct that was prohibited by a franchise contract or failed to perform what was required by the contract.²⁰²

When terminating a franchise agreement for breach by a franchisee, a franchisor must comply with the notice and cure requirements under paragraph (2) of clause 27. First, the franchisor must notify the franchisee in writing that the franchisor proposes to terminate a franchise contract because of the franchisee's breach.²⁰³ According to the court in *Frontline Retail*, the franchisor must sufficiently elaborate on the alleged breach in the written notice.²⁰⁴ Second, the franchisor must inform the franchisee of what the franchisee is

201 The Code, cl. 27(1).

202 *Aura Enterprises Pty Ltd v Frontline Retail Pty Ltd* [2006] 202 FLR 435 [20].

203 The Code, cl. 27(2)(a).

204 *Aura Enterprises* (n 202) [24].

required to remedy the breach.²⁰⁵ In this case, the franchisor must give the franchisee reasonable time with no more than 30 days to cure the breach.²⁰⁶ More importantly, in the notice, the franchisor must inform the franchisee that the franchisor will terminate the agreement if the franchisee does not remedy the breach within a reasonable time specified. Otherwise, the franchisor's failure to inform would result in an invalid termination notice.²⁰⁷

– *Termination in case of no breach*

If the ground for the franchisor's termination is not the franchisee's breach of contract, then Clause 28 will apply. Generally, paragraph (1) of clause 28 specifies two conditions when the termination rule in clause 28 will apply. First, the rule in clause 28 will apply if a franchisor aims to terminate a franchise agreement in accordance with the terms of the agreement before the term expires.²⁰⁸ Moreover, the franchisor's purported termination must be made without the consent of the franchisee.²⁰⁹ Second, the rule in clause 28 will apply if a franchisor aims to terminate a franchise agreement because of no breach of a franchise agreement by a franchisee.²¹⁰ It should be noted that, if the grounds for termination for no breach are the listed grounds under clause 29, then clause 29 will apply to the franchisor's termination.

According to paragraph (3) of clause 28, a franchisor must give a franchisee reasonable notice when terminating a franchise contract. That is, the franchisor must provide the franchisee with reasonable written notice of the proposed termination and the reasons for the termination. Whether the notice is reason-

205 The Code, cl. 27(2)(b).

206 The Code, cl. 27(2)(c), in conjunction with cl. 27(3).

207 In *National Security Training Academy (GC)*, the court found that the franchisor did not inform the franchisee that it would terminate the contract if the fee was not paid within a reasonable time. Thus, the court concluded that the notice of breach was not duly given to the franchisee for the purpose of the Code. See *National Security Training Academy (GC) Pty Ltd v National Security Training Academy Pty Ltd* [2013] QSC 245 [27].

208 This condition implies that clause 28 applies to the franchisor's termination of a franchise contract with a fixed term. This conclusion is affirmed by the court in *W Hoy v WTH*. See *W Hoy Pty Ltd v WTH Pty Ltd* [2018] FCA 310 [7] – [75]. Thus, a franchisor needs not to follow the requirements in clause 28 if the franchisor terminates a franchise contract for an indefinite period.

209 The Code, cl. 28(1)(a). In practice, a franchise contract typically specifies events of no breach by a franchisee in which a franchisor has the right to terminate. See *Aura Enterprises* (n 202) [20]. Furthermore, it is said that the franchisor typically retains the right to terminate a franchise agreement for commercial reasons, such as regaining all franchised stores and driving underperformed franchisees out of a franchise system. See Peter Buberis, *Australian Franchising Code of Conduct: A Critical Analysis with Current Case law* (Emerald Publishing 2020) 213.

210 The Code, cl. 28(1)(b). In this case, what is meant by the term 'breach' has been addressed in the preceding heading.

able may have to be decided on a case-by-case basis.²¹¹ In any event, Giles suggests that the notice must provide the notified franchisee with a sufficiently long period so that the franchisee may

‘[d]eploy its labor and equipment in alternative employment; carry out its commitments; bring negotiations to fruition; wind up the association in a businesslike manner; and recoup extraordinary expenditure or effort.’²¹²

– *Termination for particular grounds*

A franchise agreement may permit a franchisor to terminate the agreement for the grounds listed in clause 29(1). For example, a franchise agreement may allow a franchisor to terminate the agreement if a franchisee no longer holds a license that the franchisee must hold to carry on the franchised business or if the franchisee becomes bankrupt, an insolvent under administration, or a Chapter 5 body corporate.²¹³ In these cases, the franchisor’s termination will be regulated by clause 29 that imposes on the franchisor the notice and hold requirements prescribed. According to paragraph (2) of clause 29, the franchisor who proposes to terminate a franchise agreement based on the listed events in clause 29(1) must give the franchisee 7 days’ written notice of the proposed termination and the ground for it. Despite the franchisor’s notification under clause 29(2), the franchisor may not terminate a franchise agreement until after the end of 28 days if the franchisee gives the franchisor written notice of dispute under clause 40A(1).²¹⁴

5.4.4.3 *Regulation of termination by the rules of common law*

Unlike a franchise agreement for a definite period, the franchisor’s termination of a franchise contract with an indefinite term will be regulated by common contract law rules unless the contract provides otherwise. In terminating the indeterminate franchise agreement, the implied terms principle formulated by McHugh JA in *Crawford Fitting v Sydney Valve and Fittings* may apply.²¹⁵

211 Clause 28(4) provides that Part 4 concerning resolving disputes will apply to a dispute arising from the franchisor’s termination for no breach by a franchisee. According to clause 3, if the franchisee has a dispute as regards the franchisor’s purported termination, the franchisee may take action under the franchisee agreement’s complaint handling procedure, which is mandatorily required to be established by clause 34. Alternatively, the franchisee may take action in accordance with the procedure set out in Division 3 of Part 4.

212 Stephen Giles, *Annotated Franchising Code of Conduct* (2nd edn, LexisNexis Butterworths 2021) 72.

213 The Code, cl. 29(1)(a) and (b).

214 The Code, cl. 29(4)(a).

215 *Crawford Fitting Co v Sydney Valve & Fittings Pty Ltd* [1988] 14 NSWLR 438. The principles reinstated in this case have been adopted in other court decisions, such as *Pacific Products Pty Ltd v Howard* [2005] SASC 290 [11] – [34].

In this case, McHugh JA provided that a commercial contract for an indefinite period usually contains an implied term that the agreement is terminable on reasonable notice. In determining whether the notice is reasonable, the judge provided that the notice period must be sufficiently long enough to allow the recipient of the notice to find alternative employment, perform outstanding obligations, negotiate for better results, or close its business.

In addition, McHugh JA said that a contract, particularly a distribution or agency contract, might contain an implied term that the agreement will continue for a reasonable period. This implication is said to be based on the reasonable expectation of the parties that frequently need sufficient time to recoup their initial and extraordinary expenditure or effort.²¹⁶ If applying this rule in the context of the franchisor's termination, it could be said that the franchisor may be entitled to terminate an indefinite franchise contract provided that the agreement has continued for a reasonable period. After this period has passed, the franchisor must give the franchisee reasonable notice that sufficiently permits the franchisee to prepare for the end of a franchise relationship.

5.4.4.4 Regulation of termination by the terms of a franchise contract

As mentioned in the preceding subsection, an indefinite franchise agreement may contain the terms specifying conditions under which a franchisor can terminate the contract. In practice, the agreed events may vary. In some cases, a franchise contract may provide that the contract is terminable at will. For example, clause 22 of the franchise agreement in *Freier v Australian Postal* provided that the parties might terminate the agreement at any time and without cause by giving the other party a 90-day notice of termination.²¹⁷ The Code may regulate the franchisor's exercise of this contractual right in that the franchisor must act in good faith when exercising the right to terminate.²¹⁸ According to Dietrich, the principle of good faith could prevent the franchisor from disenfranchising the franchisee in the case the franchisee has a reasonable expectation of an opportunity to recoup its investments, and the terms of the agreement do not protect that opportunity properly.²¹⁹

In a fixed-term franchise contract, the termination clauses of the agreement may expressly provide for the franchisor's right to terminate. The termination

216 In *Crawford Fitting v Sydney Valve and Fittings*, the court held that a six-month period was not reasonable for terminating the distributorship contract that had continued for almost fifteen years. See *Crawford Fitting*, *ibid*.

217 The court held that the right to terminate at will was not regarded as unconscionable. See *Freier v Australian Postal Corporation (No 2)* [2012] NSWSC 61; BC201200575 [22] – [24]. Thus, the agreement on the at-will termination under a franchise contract will be enforceable.

218 The Code, cl. 6(1) and (3).

219 Joachim Dietrich, 'Giving Content to General Concepts' (2005) 29 Melbourne University Law Review 218, 229.

provisions usually replicate the Code's provisions regulating the franchisor's termination.²²⁰ For example, a franchise agreement in *Bingham v 7-Eleven Stores* demonstrated that the franchisor may terminate the agreement for breach by the franchisee. In terminating the agreement, the franchisor must follow the process prescribed in article 25(f) of the agreement. That is, the franchisor shall give the franchisee written notice identifying and giving particulars of the alleged breach. In this case, the franchisor shall allow the franchisee a reasonable time to cure.²²¹ In the notice, the franchisor shall inform the franchisee of steps to remedy the alleged default. In requiring the franchisee to correct the breach, the franchisor shall specify not less than 30 days and ask the franchisee to rectify the breach within this period. If the franchisee fails to remedy the deficiency within the timeframe, the franchise agreement is terminated.²²²

5.4.4.5 Conclusions

The regulation of the franchisor's termination under the Australian legal system is twofold. First, the Franchising Code of Conduct regulates the franchisor's termination of a franchise contract for a fixed period. Essentially, the franchisor must comply with the notice requirement when terminating a franchise agreement. This requirement applies to the franchisor's termination for breach by a franchisee, for no breach by a franchisee, and for particular grounds. Nevertheless, the detailed requirement differs among the three cases. Second, the common law rules and the terms of a franchise contract will regulate the franchisor's termination of an indefinite franchise agreement. Under these legal regimes, a franchise agreement is typically terminable at will. When it comes to exercising the right to terminate, the Code may require the franchisor to terminate the agreement in accordance with good faith and fair dealing.

5.4.5 Comparative analysis

5.4.5.1 Introduction

The descriptive examination of the franchise legal framework of the DCFR, the USA, and Australia shows that several legal approaches are taken to regulate the franchisor's termination of a franchise contract for a definite and indefinite

²²⁰ See subsection 5.4.4.2.

²²¹ In some cases, the franchisor terminated a franchise contract after giving the franchisee notice of termination for 24 hours. In this case, there was a question of whether the franchisor afforded the franchisee a reasonable time to cure the breach. See *YSC United Pty Ltd v Top Juice Franchising Pty Ltd*, [2019] VSC 524 [7] – [8].

²²² *Bingham v 7-Eleven Stores Pty Ltd* [2003] QCA 402 [100].

period. These approaches may vary. Section 5.4.5 will compare, contrast, and discuss the approaches taken by the selected legal systems in subsection 5.4.5.2. The comparison will be conducted to formulate guidelines for regulating the franchisor's termination of a fixed-term and indefinite franchise contract under comprehensive franchise law. Subsection 5.4.5.3 will draw concluding remarks on the comparison and put forward key recommendations.

5.4.5.2 *Comparison and discussion*

– *Similarity*

The DCFR, the non-termination US states, and Australia are similar in that a franchise contract and general contract law will regulate the franchisor's termination of a franchise contract for an indefinite period. In general, the termination clauses of an indefinite franchise contract will confer on a franchisor the right to terminate the agreement.²²³ In this case, the conditions under which the franchisor may terminate a franchise contract may vary. For example, the franchisor may hold the right to terminate a franchise contract at will or without cause. Alternatively, the franchisor may terminate a franchise contract only for the franchisee's breach of contract or under the listed circumstances. Suppose the parties do not agree upon the termination provisions under a franchise agreement. In that case, general contract law rules will apply by default.²²⁴ Under the realm of contract law, it is common that an indeterminate franchise agreement is terminable at will or without cause. However, it does not mean that the franchisor can terminate the agreement immediately. In other words, the rules of contract law typically require the franchisor to give the franchisee reasonable notice of termination that would allow the franchisee to prepare for the cessation of a franchise relationship.

– *Difference*

The US termination states and Australia employ a different approach to regulating termination of a franchise contract with a definite term by a franchisor. These jurisdictions regulate the franchisor's termination through the rules of franchise-specific law. In US termination states, state franchise relationship statutes contain termination provisions regulating the franchisor's termination of a franchise contract with a definite term.²²⁵ Under the termination rules, the franchisor will be required to have legitimate grounds for termination, including just cause, good faith, and specific reasons for immediate termination. This requirement would make it impossible for the franchisor to terminate

223 See subsections 5.4.2.3, 5.4.3.4, and 5.4.4.4.

224 See subsections 5.4.2.2, 5.4.3.3, and 5.4.4.3.

225 See subsection 5.4.3.2.

a franchise contract without cause. In Australia, the Franchising Code of Conduct regulates the franchisor's termination of a fixed-term franchise agreement.²²⁶ However, the Australian Code differs from the US laws in that the Code does not require the franchisor to show legitimate grounds for termination of a franchise agreement. Instead, a franchise agreement will play a vital role in elaborating on particular grounds that permit the franchisor to terminate the agreement. In this regard, the Code merely requires the franchisor to comply with the reasonable notice requirements.

– *Discussion*

The comparison demonstrates that the franchisor's termination of a franchise contract may be regulated by the terms of the contract and the rules of law, be it contract law rules or franchise-specific law rules. This subsection will discuss these two approaches and formulate guidelines for regulating the franchisor's termination in the following paragraphs.

(1) *Regulation of termination by a franchise contract*

A franchise contract may contain termination provisions that establish the franchisor's right to terminate the contract and formulate grounds for termination. In some cases, a franchise contract may provide a franchisor with the right to terminate at will or without cause. The examination in this section shows that the right of at-will termination is frequently given under a franchise agreement that is concluded for an indefinite period. In other cases, the franchisor's right to terminate is conditional upon the satisfaction of grounds for termination. According to Appleby and Rosario, the ground for termination by a franchisor is normally threefold: the ground for immediate termination without notice, the ground for immediate termination with notice, and the ground for termination with notice and an opportunity to cure.²²⁷

The termination clauses under a franchise contract are frequently franchisor-friendly since they usually give the franchisor the exclusive right to terminate.²²⁸ From a practical perspective, a franchisor may need to hold the right to terminate for the purpose of controlling quality in a franchise system. According to Blair and Lafontaine, a franchisor typically concerns the consistency of the franchise system's operation, service, and product quality that

226 See subsection 5.4.4.2.

227 Bethany L. Appleby and Iris Figueroa Rosario, 'Termination and Default' in Nina Greene, Dawn Newton, and Kerry Olson (eds), *The Annotated Franchise Agreement* (2nd edn, American Bar Association 2021) 214.

228 The franchisor's right to terminate is regarded as an integral element of a franchise contract. See Roger D Blair and Francine Lafontaine, *The Economics of Franchising* (Cambridge University Press 2005) 269; Appleby and Rosario, *ibid* 211.

attracts customers.²²⁹ A franchisor may want to ensure the effective protection of its valuable trademark. According to Fern and Klein, the franchisor may have successfully developed a 'second meaning' of the trademark among the public, which is financially valuable.²³⁰ Thus, retaining the right to terminate a franchise contract with a substandard franchisee will enable the franchisor to maintain the uniform quality in a franchise system and protect the valuable trademark for the benefit of the franchisor and other franchisees.

From the perspective mentioned above, a franchise contract would be less protective of a franchisee because a franchisor can hold the right to terminate a franchise contract, regardless of the franchisee's default. For example, a franchisor may terminate a franchise contract at will, meaning the franchisor may terminate the contract at any time for no cause. From a legal viewpoint, some legal systems, such as Italy, will not treat this contractual arrangement as unfair.²³¹ Additionally, a franchise agreement may not confer on the franchisee the right to terminate in an equal fashion. According to Appleby and Rosario, many franchise contracts provide the franchisee with fewer rights to terminate than the franchisor. In many instances, the franchisee's right to terminate is confined to termination for the franchisor's material breach of a franchise contract.²³² For example, a franchise agreement in the Australian case *Swim Loops* provided that the franchisee may terminate the agreement if the franchisee is in substantial compliance with the agreement and the franchisor breaches a material and fundamental term of the agreement.²³³ In this case, the franchisee cannot terminate a franchise contract on the grounds that are not considered the franchisor's breach of a franchise contract; for instance, the franchisor becomes insolvent or is convicted for serious crimes. In the end, the franchisee would face big hurdles in successfully terminating a franchise contract according to the termination clause.

(2) Regulation of termination by contract law

Generally speaking, general contract law does not play a vital role in constraining the franchisor's termination of a franchise contract. Instead, the law plays a supplementary role in providing default rules for terminating a contract, such as a rule on termination for non-performance of an obligation of breach of contract. Nevertheless, contract law may control the franchisor's termination

229 Roger D Blair and Francine Lafontaine, 'Understanding the Economics of Franchising and the Laws That Regulate' (2006) 26 *Franchise Law Journal* 55, 60.

230 Martin D Fern and Philip Ian Klein, 'Restrictions on Termination and Nonrenewal of Franchises: A Policy Analysis' (1981) 36 *The Business lawyer* 1041, 1041-042.

231 Frignani and Pratt (n 91) 19.

232 In terminating a franchise agreement for the franchisor's material breach of contract, the franchisee usually has to provide the franchisor with reasonable notice and time to cure. In other words, the franchisee cannot terminate a franchise contract with an immediate effect. See Appleby and Rosario (n 227) 223.

233 *H2O Learning Pty Ltd v Swim Loops Pty Ltd (t/as Jump Swim Schools)*, [2019] NSWDC 165 [44].

to some extent. For example, in the USA and Australia, a franchisor may terminate a franchise contract with an indefinite term until after the contract has lasted for a reasonable period. In terminating the contract, the franchisor also has to give the franchisee reasonable notice of termination. Despite this restrictive procedure, the franchisor may manage to exclude or deviate from this termination rule because the rule is ordinarily not mandatory. In reality, therefore, a sophisticated franchisor will eventually find a way to escape this procedural constraint.

In some legal systems, such as the DCFR, contract law adopts the principle of good faith as a behavioral standard in a contractual relationship. In this case, the franchisor's exercise of the right to terminate may be constrained by the requirement of good faith and fair dealing. Dietrich exemplifies that a franchisor may be prevented from terminating a franchise contract if the franchisee has reasonable expectations to recoup its investments, provided that the terms of the agreement do not protect the franchisee appropriately.²³⁴ From a practical viewpoint, the role of good faith in regulating the franchisor's termination is uncertain because no case law has illustrated that courts have utilized the principle of good faith to limit the franchisor's right to terminate. Thus, it could be concluded that a contract law regime will not properly protect the franchisee's interests in operating a franchised business.

(3) *Regulation of termination by franchise relationship law*

Some legal systems, such as the termination states of the USA and Australia, enact franchise relationship law to specifically regulate the franchisor's termination of a franchise contract. This regulatory approach would effectively protect a franchisee against an opportunistic franchisor since the introduction of franchise relationship legislation usually aims at protecting a weaker franchisee. Thus, all the rules under the legislation will be made mandatory. In this respect, a franchisee will operate a franchised business without fear that a franchisor may take away a franchised business without justified reasons. The termination rules under franchise relationship law vary from legal system to legal system. In other words, there has been no uniformity in enacting the relationship law's termination provisions. Thus, it will depend on the legal policy of each legal system as to how termination rules are constructed.

In my view, comprehensive franchise law should contain provisions that provide the rules regulating termination of a franchise contract. These rules should be made mandatory, nondiscriminatory, predictable and comprehensive.

Firstly, the termination rules should be mandatory. The compulsory character of the provisions would prevent a franchisor from excluding the application of the provisions or varying or deviating from their effect. In this respect, the mandatory rules would bar the franchisor from proposing favorable termination clauses of a franchise contract at the expense of the franchisee.

234 Dietrich (n 219) 229.

As mentioned earlier, the franchisor may exercise its superior power to introduce termination provisions that allow the franchisor to terminate a franchise contract at will.²³⁵ According to Emerson, the existence of at-will termination provisions would be inconsistent with the goal of the protection of franchisees from undue termination because the termination clauses permit the franchisor to have much control over the franchisee, which would lead to abuse of power.²³⁶ In *Westfield Centre Service v Cities Service Oil*, the US court pointed out that franchisors might draft franchise contracts that enable them to terminate the contracts at will. The franchisor's ability to terminate a franchise contract at will would leave franchisees with no return for their investment.²³⁷

Secondly, the termination rules should equally apply to termination of a franchise contract by a franchisor and a franchisee. As can be seen, some franchise relationship law exclusively deals with the franchisor's termination of a franchise contract. That is, the law usually elaborates on when and how a franchisor can terminate a franchise contract. In contrast, the franchisee's right to terminate is not equally addressed by the law and is left for a franchise contract or general contract law to determine. Recently, in Australia, this inequality issue has been raised and discussed in the Report of Fairness in Franchising of the Parliamentary Joint Committee on Corporations and Financial Services (the Report). In the Report, the committee suggests that the Franchising Code of Conduct should include a provision for a franchisee to have the right to terminate a franchise contract in special situations.²³⁸ In response to the Report, the Code has now been amended to include clauses 26A and 26B providing the mechanism for the franchisee to terminate a franchise agreement. Thus, it would be wise for comprehensive franchise law to equally regulate termination of a franchise by a franchisee so that the franchisee's interests are reasonably protected.

Thirdly, the termination rules should be predictable and comprehensive. First, the rules should enable a franchisor and a franchisee to have prior awareness of the circumstances under which a franchise contract can be terminated. As will be seen, the parties should be able to predict that a franchise contract can be terminated if the other party materially breaches a franchise contract or becomes bankrupt or insolvent. Second, the rules should comprehensively regulate the termination of a franchise contract. That is, the rules should regulate terminating a franchise contract concluded for an indefinite and definite period. Some franchise relationship law specifically regulates the

235 The incorporation of at-will termination clauses is permissible in several jurisdictions that have no franchise relationship law, such as the US state of Louisiana. See *Corenswet Inc v Amana Refrigeration Inc* 594 F2d 129 (CA La, 1979) 134.

236 Emerson, 'Franchise Contract Clauses and the Franchisor's Duty of Care toward Its Franchisees' (n 104) 951; Emerson, 'Franchise Terminations: Good Cause Decoded' (n 173) 152.

237 *Westfield Centre Service Inc v Cities Service Oil Co* 432 A2d 48, 53, 86 NJ 453 (NJ, 1981) 462.

238 Parliamentary Joint Committee on Corporations and Financial Services, *Fairness in Franchising* (Senate Printing Service 2019) 150-65.

termination of a franchise with a definite term. In this case, the termination of an indefinite franchise agreement will be subject to the terms of the agreement or contract law rules. This situation would result in the lack of uniformity in applying comprehensive franchise law rules regulating the termination of a franchise agreement.

The following paragraphs will suggest formulating termination rules under comprehensive franchise law based on the abovementioned principles. The model termination rules will be suggested to cover termination of a franchise contract with an indefinite term, termination of a franchise contract for non-performance of an obligation, and termination of a franchise contract for other commercial reasons.

(3.1.1) Termination of a franchise contract with an indefinite term

‘(1) A party to a franchise contract with an indefinite term may terminate the contract by giving the other party written notice under the conditions set out in paragraph (2).

(2) A party may terminate a franchise contract with an indefinite term only after an existing franchise relationship has existed for a reasonable period. When intending to terminate the contract, the terminating party shall give notice to the other party a reasonable period before the termination is effective.’

This model rule is proposed to regulate termination of a franchise contract for an indefinite period by a party to a franchise contract. At the outset, the character of a franchise contract with an indefinite term and the nature of termination should be made clear. In light of this model provision, the term of a franchise contract can be regarded as indeterminate in the following three circumstances. First, the parties do not specify a duration or expiration date of a franchise agreement. Second, the parties explicitly incorporate a so-called ‘evergreen clause’ into a franchise contract that makes the term of a franchise agreement perpetual.²³⁹ Third, a franchise contract is renewed by the operation of the rule of law.²⁴⁰ By its nature, termination of a franchise contract for an indefinite period is termination for convenience. The concept underlying the right to terminate in this case is that some contracts are concluded for a long term. Sometimes, a party needs a great deal of flexibility to address unforeseen difficulties in performing the contract. Thus, the party should have

²³⁹ Sheyka and Weldon (n 105) 52.

²⁴⁰ For example, this chapter has proposed the model franchise rule that a fixed-term franchise contract may automatically be renewed indefinitely upon satisfaction with the conditions prescribed by the rule. *See* subsection 5.3.5.2.

the power to terminate the contract at discretion, regardless of the other's party default, by giving notice of termination.²⁴¹

Paragraph (1) of the proposed rule sets forth a general principle that the termination of an indefinite franchise contract is effective upon the provision of written notice of termination. It is said that the notice requirement can guarantee fairness because the termination notice helps remind the recipient of the end of a business operation.²⁴² This awareness would enable the party, particularly the franchisee, to prepare for the shutdown of the business operation and find a new investment opportunity. Nevertheless, a franchise relationship typically involves a contribution of the capital and labor made by a franchisee. Thus, I am of the opinion that the notice requirement may not suffice to protect the franchisee's interests. In other words, the notice requirement should be reinforced by other requirements imposed in paragraph (2).

The second paragraph sets out two procedural requirements for terminating an indefinite franchise contract. First, a party may terminate a franchise contract for an indefinite period only after a reasonable time has elapsed since the conclusion or renewal of the contract. In this case, it would not be possible for the parties to terminate an indefinite franchise contract on the second or third day after the agreement has been entered into or renewed.²⁴³ Second, after a reasonable period has passed, the party may terminate the franchise agreement by giving the other party reasonable notice of termination. The reasonableness element is relatively elusive and must be concertized on a case-by-case basis. In any case, a reasonable period should be sufficiently long enough to enable the terminated party to protect its legitimate interests. For example, the franchisor may terminate a franchise contract after allowing the franchisee to have sufficient time to gain revenues and make profits in the operation of a franchised business or to effectively disassociate itself from the franchisor and any potential consequences of the termination to the franchisee.²⁴⁴

241 Ben Curtin, 'Recent developments in termination for convenience clauses: the role of good faith' (2010) 24(3) *Commercial Law Quarterly* 23, 23; Ruth Loverranes, 'Termination for Convenience Clause' (2012) 14 *University of Notre Dame Australia Law Review* 103, 103.

242 Emerson, 'Franchise Terminations: Good Cause Decoded' (n 173) 147.

243 Comprehensive franchise law may provide some exceptions in this respect. For example, the law may permit a franchisee to terminate a franchise agreement within a grace or cooling-off period. This model is not unusual as it is adopted in the Australian Franchising Code of Conduct. Under the Code, clause 26(1) provides that a franchisee may terminate a franchise agreement within 14 days after concluding a franchise agreement.

244 Giles (n 212) 71-72. Furthermore, the factors enumerated by the Australian court in the case *Crawford Fitting v Sydney Valve and Fittings* could be taken as guidelines. According to the court, a period of notice would be considered reasonable if it is sufficiently long to allow the recipient to deploy labor and equipment in alternative employment, perform obligations, conduct fruitful negotiation, and wind up the association in a businesslike manner. See *Crawford Fitting* (n 215).

(3.1.2) *Termination of a franchise contract with a definite term*

Unlike termination of an indefinite franchise agreement, two general considerations should be considered when introducing the rules regulating the termination of a franchise contract with a fixed term under comprehensive franchise law. First, the parties to a franchise contract should be permitted to terminate the agreement only with certain causes. In other words, it might not be plausible for the party to terminate the agreement at will. This consideration aims to prevent the parties, particularly a franchisor, from retaining the right to terminate a franchise contract for no grounds. Second, the grounds for terminating a franchise contract for a definite period should be divided into two independent cases: termination for material non-performance of an obligation and termination for other commercial reasons.²⁴⁵

(3.1.2.1) *Termination for material non-performance of an obligation*

‘(1) A party may terminate a franchise contract with a definite term for the other party’s material non-performance of an obligation.

(2) When intending to terminate the contract, the terminating party must allow the other party to cure an alleged non-performance. In this case, the terminating party must give the other party written notice of termination. In the notice, the terminating party must specify a reasonable manner in which the other party may cure the alleged non-performance. Besides, the terminating party must fix a reasonable period of not less than 15 calendar days after receipt of the notice for the cure. If the other party fails to cure the alleged non-performance within a specified period, the contract is automatically terminated.

(3) The terminating party may not allow the other party to cure by virtue of (2) if the alleged non-performance is incurable, considering the circumstances of the case. In this case, the terminating party may terminate a franchise contract by giving the other party written notice of termination with immediate effect.’

The abovementioned paragraphs formulate rules regulating termination of a franchise contract with a fixed term for material non-performance of an obligation. The first paragraph states the general rule that a non-performance of an obligation may provide a basis for termination of a fixed-term franchise contract. The termination is permissible only if the alleged non-performance is material.²⁴⁶ The idea behind the materiality requirement is that it would be contrary to good faith to terminate a franchise relationship, which is typically a long-term relationship, for minor defaults. In this relationship, the parties may invest considerable money in reliance upon the continuation of the extended relationship. In this respect, terminating a franchise contract for an insignificant breach would inflict any financial harm to the terminated party,

245 The idea behind the differentiation is that each category deserves different requirements for termination.

246 This formulation can be found under IV.E. – 2:304(1) of the DCFR.

particularly the franchisee. Thus, the principle should be that the parties are not allowed to allege the other party of committing a minor or insignificant non-performance of an obligation to terminate a franchise relationship.

Since legal systems may perceive the expressions ‘non-performance’ and ‘material’ differently, it would be wise to provide some clarity to facilitate the interpretation of the rule in paragraph (1). First, the phrase ‘non-performance’ should be understood in the broadest sense to include situations in which a party delays in performing an obligation imposed by a franchise contract or the rules of law, performs the obligation that falls short of what is required, or does not perform the obligation altogether. Second, the term ‘material’ may follow the test adopted by the rule of the DCFR.²⁴⁷ That is, the non-performance is material if it substantially deprives the terminating party of what the party was entitled to expect under a franchise agreement. In this case, the non-performing party should foresee or could have foreseen that expectation at the time of the conclusion of the contract. The non-performance is also material if the non-performing party intentionally or recklessly fails to perform the obligation. Furthermore, the terminating party should have reasons to believe that the breaching party’s future performance cannot be relied on.

In the context of the franchisor’s termination, a franchisor may be permitted to terminate a franchise contract on several occasions related to the franchisee’s material non-performance. Among other things, the franchisor may terminate the agreement because of two following reasons: the franchisee’s inability to operate a franchised business and the franchisee’s conduct that adversely affects a franchise business.

– *Franchisee’s inability to operate a franchised business*

A franchise contract may allow a franchisor to terminate a franchise agreement if a franchisee is incompetent in operating a franchised business. The determinative factors of the franchisee’s incompetency may include (1) the franchisee’s loss of a license or the denial of authorization necessary for the operation of a franchised unit, (2) the franchisee’s financial failure, and (3) the franchisee’s voluntary abandonment of a franchised business. From a regulatory perspective, it is not uncommon that a franchisor may terminate a franchise agreement because of those three grounds. For example, the Australian Franchising Code of Conduct permits the franchisor to retain the right to terminate a franchise agreement upon the occurrence of those three circumstances.²⁴⁸

Firstly, a franchise may terminate a franchise contract if a franchisee loses a license necessary to operate a franchised business in the entire relationship. For example, in Thailand, a person who operates a hotel business must be

²⁴⁷ The DCFR, III. – 3:502.

²⁴⁸ The Code, cl. 29(1).

granted a license under the Hotel Act, B.E. 2547 (2004).²⁴⁹ The license is valid for five years from the date of issuance.²⁵⁰ In this case, it is possible that, after the current license expires, the franchisee who operates a hotel franchise business is refused to renew the license under the second paragraph of section 21 of the Hotel Act. Thus, the hotel franchisor may reserve the right to terminate if the franchisee is refused to renew the hotel license under the Hotel Act.

Secondly, a franchisor may terminate if a franchisee encounters serious financial difficulties. From a practical viewpoint, the franchisor may develop some indicators of the franchisee's financial failure under the terms of a franchise contract. The indicators to be adopted under the contract may include the franchisee's bankruptcy or insolvency. The commencement of the bankruptcy or insolvency vary from jurisdiction to jurisdiction. For example, in Thailand, the Thai Bankruptcy Act, B.E. 2483 (1940) provides that the bankruptcy will take effect after the court issues a receivership.²⁵¹ In case the franchisee is declared bankrupt, the power to manage the franchised business will devolve to a government official called the Receiver, who will exercise the sole power in managing the business of the franchisee.²⁵² In this case, the franchisor may retain the right to terminate if the franchisee is issued the court's receivership order under the Bankruptcy Act.²⁵³

The third factor concerns the franchisee's voluntary abandonment of a franchised business. However, the abandonment of a franchised business is a matter of fact. Thus, a franchisor is encouraged to elaborate in a franchise contract on situations in which a franchisee is deemed to leave its business voluntarily. For example, the franchisee may be treated as having abandoned a franchised business if the franchisee has intentionally shut down the operation of the business for two consecutive weeks. A franchise contract may make exceptions in which a franchisee is not considered having deserted the franchise business operation. For instance, the franchisee's voluntary abandonment of a franchised business is not triggered if the franchisee does not operate a franchised store because of illness or other compelling reasons.

249 Paragraph (1) of section 15 of the Act states that no person shall operate a hotel unless he has obtained a license issued by the Registrar. An unofficial English translation of the Hotel Act, B.E. 2547 (2004) can be accessed at <<https://bit.ly/33tmm1S>>.

250 The Hotel Act, B.E. 2547 (2004), s. 19.

251 The Bankruptcy Act, B.E. 2483 (1940), s. 62. An unofficial English translation of the Bankruptcy Act can be accessed at <<https://bit.ly/2OQfNmi>>.

252 The Bankruptcy Act, B.E. 2483 (1940), s. 22(1).

253 The ABA's Annotated Franchise Agreement may offer another example. The ABA's publication provides that the franchisor may terminate a franchise agreement if the franchisee is instituted a lawsuit to foreclose any lien or mortgage and the suit is not dismissed within thirty days, or if the franchisee's real or personal property is sold after levy by any sheriff, marshal, constable or equivalent governmental authority. See Appleby and Rosario (n 227) 215.

– *Franchisee's conduct that adversely affects a franchise business*

A franchisor may terminate a franchise contract because of the franchisee's damaging conduct. During an ongoing franchise contract, a franchisee may engage in conduct that harms the reputation of the franchisor's business or the franchise network. From a customer's perspective, all the franchised stores are characteristically considered stores with single ownership. Suppose an individual franchisee has engaged in any harmful conduct. In this case, the whole franchise system will be adversely affected, not to mention that individual franchisee. In Thailand, there was a case where an employee of an individual franchised unit of a café franchise branded '*Café Amazon*' was exposed to reuse some coffee cups taken from a trash bin. Not surprisingly, reusing these wastes provoked customers' backlash against the franchise system, not the store in trouble.²⁵⁴ From this example, it would be justified that the franchisor may terminate the franchise agreement for the franchisee's substandard service. In other cases, the franchisee's illegal and immoral conduct could be regarded as conduct that adversely affects a franchise business, which justifies the franchisor's termination.

In the former case, the franchisee's illegal conduct may justify the franchisor's termination. This conduct may be determined by the fact that the franchisee has violated criminal law rules and is convicted of a felony or serious offense. For example, in the USA, a franchisor may terminate a franchise contract because of the franchisee's conviction of possession of heroin for sale²⁵⁵, third-degree assault²⁵⁶, and bribery and conspiracy.²⁵⁷ A conviction needs not to be made by a judgment of the final or highest court. Since the idea is not to punish the franchisee criminally, the franchisor may terminate a franchise contract even though the franchisee is convicted by a trial court judgment. For instance, the US court in *Humboldt Oil Co* interpreted the term 'conviction' under the Petroleum Marketing Practices Act, which is federal franchise law regulating a petroleum industry, to mean the judgment delivered by a trial court. In reaching such a construction, the court concluded that:

'[G]ood faith belief of the franchisor that the franchisee is untrustworthy or engages in fraudulent practices undermines the entire franchise relationship. Conviction in the trial court provides a reasonable basis for such a belief. The Act does not provide a franchisee with total protection against termination but only with protection against unreasonable or arbitrary termination. The franchisee need not lose

254 'Café Amazon apologizes for substandard employees of the franchised outlet and decides to halt the outlet's operation for three days for investigation' [in Thai] MGROnline (31 August 2019) <<https://bit.ly/31dZOkv>> accessed 17 February 2023.

255 *Atlantic Richfield Co v Guerami* 820 F2d 280 (CA9 (Cal), 1987) 282.

256 *Glenside West Corp v Exxon Co USA A Div of Exxon Corp* 761 F Supp 1118 (DNJ, 1991) 1131.

257 *Lewis v Exxon Corp* 716 F2d 1398, 1398, 230 US App DC 280 (CADCA, 1983) 280.

all possible appeals before the franchisor might reasonably think him untrustworthy.²⁵⁸

In the latter case, the ground for the franchisor's termination of a franchise contract could be constituted when a franchisee engages in utterly immoral or unethical conduct.²⁵⁹ Generally speaking, the franchisee's immoral or unethical behaviors could badly damage or cause substantial harm to the reputation or credibility of a franchise business. In practice, this terminating ground is seemingly acceptable. Some self-regulatory associations, such as the Franchising Council of Australia (FCA), have adopted the standard of ethical conduct. In the FCA Member Standards, the Members are expected to refrain from illegal, unethical, or improper dealings or otherwise act contrary to the image of franchising.²⁶⁰ In addition, the ABA's Annotated Franchise Agreement offers a sample clause that permits a franchisor to terminate the agreement if a franchisee engages in any conduct or practice that includes unethical practices.²⁶¹

The expression 'utterly immoral or unethical conduct' is relatively broad. In this regard, it is suggested that a franchise agreement enumerates the listed circumstances under which the parties are allowed to terminate the contract. In the franchising context, fraudulent or dishonest practices could be taken as utterly immoral behaviors that may provide a basis for terminating a franchise contract.²⁶² From a regulatory perspective, termination for this particular ground is not uncommon. Some franchise relationship laws allow the franchisor to terminate a franchise agreement upon the occurrence of the franchisee's fraudulent conduct. For instance, the Australian Franchising Code of Conduct permits a franchisor to retain the right to terminate a franchise contract if a franchisee acts fraudulently in connection with the operation of a franchised business.²⁶³

258 *Humboldt Oil Co Inc v Exxon Co USA* 695 F2d 386 (CA Nev, 1982) 389, cited and followed by *Lewis v Exxon Corp* 716 F2d 1398, 1399, 230 US App DC 280 (CADC, 1983) 281.

259 In my opinion, it is not necessary that the franchisee's utterly immoral or unethical conduct would lead to the conviction of a serious crime.

260 The text of the FCA Member Standards can be accessed at <<https://bit.ly/2QfxWtb>>.

261 Appleby and Rosario (n 227) 218.

262 A practice of animal cruelty could be taken as another instance. For example, in the USA, it was reported that the pet store franchisor terminated the franchise agreement with its franchisee, who was accused of animal abuse. See Darcy Spencer and Miranda Jackson, 'Petland Ends Franchise Agreement With Virginia Store Accused of Animal Abuse' (NBC Washington, 3 April 2019) <<https://bit.ly/2VFOMNi>> accessed 17 February 2023.

263 The Code, cl. 29(1)(g). Furthermore, some factual circumstances may point out that a franchisee has engaged in fraudulent practices. For example, in Australia, a number of franchisees of several franchise businesses, such as those of 7-Eleven, were alleged of fraudulently engaging in systematic underpayment of wages to their employees. See Fair Work Ombudsman, *A Report of the Fair Work Ombudsman's Inquiry into 7-Eleven* (Commonwealth of Australia 2016).

Paragraph (2) sets forth the notice and cure requirement for terminating a franchise contract for a material non-performance of an obligation. In terminating the agreement, the terminating party should be required to give the other party written notice of termination and allow the other party to cure an alleged non-performance of an obligation. Providing an opportunity to cure is said to be consistent with the principle of good faith and help uphold a contractual relationship where possible and appropriate.²⁶⁴ Thus, the terminating party should be required to permit the correction of the alleged non-performance of an obligation. In the notice of termination, the terminating party should provide the other party with the following two instructions so as to cure the alleged non-performance.

First, the terminating party should specify means by which the other party may cure the alleged non-performance. For example, if the franchisee fails to pay a monthly royalty fee, the franchisor may ask the franchisee to pay the due sum by a bank transfer. Second, the terminating party should also fix a reasonable period within which the cure can be made. In this respect, the terminating party may consider the nature of the breach and the possibility of the breach being rectified within the fixed period. However, the specified period should not be fixed for less than 15 calendar days after the receipt of the notice. In the preceding example, the franchisor may demand the franchisee to pay the unpaid sum within 15 calendar days, which would be deemed to be reasonable.

Upon receipt of the notice, the breaching party needs to cure the alleged non-performance within a specified period. If the party fails to do so, a franchise contract will be terminated automatically so that the terminated party disputes whether the contract is terminated. In some cases, it turns out that the breaching party tenders the performance after the fixed period has expired. For example, the franchisor gives the franchisee notice of termination, demanding the franchisee to transfer the unpaid royalty fee by 16 November 2023. Assuming that the franchisee manages to pay the outstanding sum on 20 November 2023, a question might be raised whether the franchise contract is actually terminated if the franchisor receives the franchisee's payment without any objection. In this case, my view is that the franchisor may be prevented from asserting that the agreement is effectively terminated because the good faith principle would require the franchisor not to change its position on which the franchisee has reasonably relied.²⁶⁵

Paragraph (3) deals with the incurability of an alleged non-performance of an obligation. In franchising, it is possible that a franchisee's defaults are

²⁶⁴ Bar and Clive (n 9) 812.

²⁶⁵ It should be mentioned that this research has proposed that comprehensive franchise law should require the parties to a franchise contract to act in good faith when exercising their rights.

incurable.²⁶⁶ In this respect, a question may be raised what is meant by the term 'incurable'. Examples from the US legal system may be taken. In the USA, Doellinger has summarized that the approach taken by American courts is distinctively twofold. On the one hand, attention will be paid to the possible ability of the defaulting party to cure the breach. The determination of the incurability is to be made by using a logical construction. For example, the franchisee's failure to meet a sales quota within a specified time is incurable. On the other hand, the seriousness of a breach is used as a test of an incurable default. In this case, a breach is incurable if its effect is so vital and destructive to a franchise relationship. From the standpoint of the second approach, the franchisee's fraud is said to be an example of an incurable breach.²⁶⁷

In my view, whether a breach or non-performance is incurable is a matter of fact. In determining whether a non-performance of an obligation is incurable, the test of inappropriateness should be adopted. That is, the non-performance will be considered incurable if it would be inappropriate for the defaulting party to cure the alleged breach under the circumstances of the case. This sweeping test is not peculiar. Under the DCFR, in the case of non-conforming performance, the creditor needs not to allow the debtor to cure a non-conforming performance if the cure would be inappropriate in the circumstances.²⁶⁸ If applying this test in the context of the franchisee's non-performance, the franchisor may not allow the franchisee to cure in some cases. For example, the franchisee cannot be allowed to cure if it abandoned a franchised business; was convicted of a serious criminal offense; became bankrupt or insolvent, and engaged in multiple breaches of a franchise contract. In these cases, I suggest that the party who intends to terminate a franchise contract may give the other party written notice of termination that terminates a franchise contract immediately.

(3.1.2.2) *Termination for other commercial reasons*

'(1) A party may terminate a franchise contract with a definite term for reasons other than material non-performance of an obligation of the other party insofar as the reasons for termination are of commercial significance.

(2) When intending to terminate the contract, the terminating party must give the other party a written notice of termination for a reasonable period before the termination is effective. In the notice, the terminating party must include the reasons on which the proposed termination is based.'

266 Stover (n 115) 219; John Pratt, 'Franchising in the United Kingdom' (2012) 32 Franchise Law Journal 95, 96; Chad J Doellinger, 'Incurable Breaches: A Fresh Look at an Old Problem' (2013) 32 Franchise Law Journal 119, 119.

267 Doellinger, *ibid* 123.

268 The DCFR, III. – 3:203(d).

The abovementioned paragraphs intend to offer sweeping rules regulating termination of a franchise contract for reasons other than a non-performance of an obligation. The first paragraph of the proposed rules accepts that the termination of a franchise contract can be made for reasons other than non-performance of an obligation. However, those reasons should satisfy the test of commercial significance. Since a franchise is a commercial relationship, it would be reasonable to require the parties to terminate the relationship for business-related grounds. From a franchisor's standpoint, a full-scale market withdrawal could justify the franchisor's termination of a franchise contract.

For example, in the USA, courts permit the franchisor to terminate a franchise agreement for an entire market withdrawal. The New Jersey court in *Freedman Truck Center* held that the franchisor's termination in the context of a general market withdrawal was allowable. That is, the franchisor might terminate a franchise agreement if it withdrew entirely from the business of manufacturing and marketing the franchised product uniformly across a geographic area. Nevertheless, the court provided that the franchisor's termination could not be abusive to the franchisee. That is, the franchisor was not allowed to terminate the contract to exploit its stronger bargaining power to maximize gains on the franchisee's property without compensating the franchisee.²⁶⁹

Paragraph (2) establishes the notice requirement for terminating a franchise contract for other commercial reasons. In terminating the agreement, the terminating party should be required to give the other party written notice for a reasonable period before the termination date. This requirement implies that immediate termination is not be allowed. The idea behind the reasonable notice requirement is that the parties, particularly the franchisee, should have some time to prepare for exit strategies. For instance, the franchisee should be given a reasonable time to sell off its current stocks or to find an alternative business. This time allowance is vital to a weaker franchisee because the franchisee usually is subject to a non-compete obligation, preventing the franchisee from selling the stocks or doing business in competition with the franchisor's franchise business. In that case, it would be harsh and devastating to the franchisee if the franchisor is permitted to terminate the contract immediately.

In the notice of termination, the terminating party should be required to provide the reasons for the purported termination of a franchise contract. The idea behind this formal requirement is that an informed party should be allowed to know specific reasons that lead to the dissolution of a franchise relationship. This requirement could benefit the terminated party when it decides to bring the case to court. The specified reasons in the notice of termination would provide the grounds for challenging under the lawsuit and

269 *Freedman Truck Center Inc v General Motors Corp* 784 F Supp 167 (DNJ, 1992) 170-73.

enable the court to determine whether the purported termination has been made for significantly commercial reasons. Thus, the purported termination should not be effective if the terminating party does not provide the other party with reasonable notice of termination or the notice does not include the reasons on which the termination is based.

(4) *Requirement of good faith*

The requirement of good faith may apply in the case of termination of a franchise contract. In the context of the franchisor's termination, the franchisor may be prevented from terminating a franchise contract because of the principle of good faith. For example, the franchisor's discriminatory termination may be prohibited. In practice, this situation may occur when the franchisor decides to withdraw the products or services from some geographical areas.²⁷⁰ In the USA, the court in *Freedman Truck Center v General Motors* exemplified how the franchisor could abuse its franchisees by way of discriminatory termination. According to the court, the franchisor might not leave the franchise business or discontinue its goods entirely. Instead, the franchisor might discriminately terminate particular franchisees while leaving others in the business. This market strategy was said to serve the franchisor's interest at the expense of the terminated franchisee. That is, the franchisor might terminate a franchise agreement by withdrawing the goods or services to appropriate the franchisee's goodwill.²⁷¹ Thus, the franchisor's selective termination that is contrary to good faith will not be effective.

5.4.5.3 *Conclusions*

– *Concluding remarks*

The comparison of the franchise legal framework of the DCFR, the USA, and Australia shows that a franchise agreement primarily regulates the franchisor's termination of a franchise contract for an indefinite or definite period through termination clauses. However, those termination provisions are typically formulated in favor of the franchisor. The franchisor may retain the right to terminate a franchise contract with or without cause. In theory, courts may employ the requirement of good faith to constrain the franchisor's exercise of the right to terminate. Nevertheless, the practical solution seems to be the introduction of franchise relationship law to regulate the franchisor's termination. Essentially, franchise relationship law is introduced to provide termination rules regulating the franchisor's ability to terminate a franchise contract. Under the rules, the franchisor will be required to follow certain procedures for

270 In addition, the franchisor's termination for selective withdrawal of goods or services may not satisfy the standard of commercial significance proposed in this section.

271 *Freedman Truck Center* (n 269) 171.

terminating the agreement. The rules may constrain the franchisor's termination by requiring the franchisor to have some legitimate grounds for the termination.

– *Key recommendations*

Regulation of termination of a franchise contract: Comprehensive franchise law should contain the termination provisions regulating termination of a franchise contract by a franchisor and a franchisee. These termination provisions should be made mandatory, nondiscriminatory, predictable and comprehensive. These provisions should also provide the different rules dealing with the termination of a franchise agreement for an indefinite period and the termination of a franchise agreement for a definite period.

Termination of a franchise contract for an indefinite period: In the case of terminating an indefinite franchise contract, the termination rules should permit the parties to terminate the agreement for any reason or even for no reason. The rules should require the terminating party to follow the notice requirement so that the other party's legitimate interests are adequately protected.

Requirement for terminating a franchise contract for an indefinite period: The terminating party should be permitted to terminate a franchise contract only after the contract has lasted for a reasonable period. When intending to terminate the contract, the terminating party should be required to give the other party written notice of termination for a reasonable period before the termination is effectuated.

Termination of a franchise contract for a definite period: In principle, a fixed-term franchise contract ends at the expiration date of the agreement. The parties should reasonably expect that the relationship will last until the expiry of the contract. In this respect, any premature termination should be permitted only for legitimate grounds, categorized into material non-performance of an obligation and other commercial reasons. In this case, the requirements for terminating a franchise contract for both types of legitimate grounds will differ.

Requirement for terminating for non-performance of an obligation: Terminating a franchise contract for non-performance of an obligation should be permitted only when the non-performance is material. Before terminating the contract, the terminating party should allow the other party to cure the alleged material non-performance. In doing so, the terminating party should provide the other party with written notice specifying a reasonable manner by which the non-performance is cured and a reasonable period of not less than 15 calendar days for the cure. The contract should be terminated automatically if the notified party fails to cure the non-performance within the specified period. In the case the alleged non-performance is incurable, the terminating party may terminate a franchise contract, following the notice requirement

prescribed by the rule regulating termination of a franchise agreement for other commercial reasons.

Requirement for terminating for other commercial reasons: Terminating a franchise contract for other commercial reasons should be permitted when these reasons are of commercial significance, such as a full-scale market withdrawal by a franchisor. When intending to terminate the contract, the terminating party should give the other party written notice of termination for a reasonable period before the termination is effective. In the notice, the terminating party should provide the reasons on which the proposed termination is based for the evidence's sake.

Requirement of good faith: When exercising the right to terminate a franchise contract, the terminating party should be required to act in accordance with the requirement of good faith. Strictly speaking, the party may be prevented from terminating the agreement capriciously. For example, the franchisor's discriminatory termination may be prohibited in light of the principle of good faith and fair dealing.

5.5 PRIVATE LAW REMEDIES

5.5.1 Introduction

Metaphorically speaking, rights and remedies are two sides of the same coin. Thus, it would be incomplete for a piece of research to study the regulation of the franchisor's conduct without examining potential sanctions for contravening conduct. In the event of the franchisor's violation of the franchise legal framework of the DCFR, the USA, and Australia, a question may be raised whether and to what extent the franchisee may compel the franchisor's performance, seek monetary compensation, and cancel a franchise agreement. It is questionable whether and to what extent the franchisee may resort to specific remedies that aim to protect the franchisee's intangible and tangible assets when a franchise relationship comes to an end.²⁷² This section will examine the remedial rules of the DCFR, the US, and Australian legal systems in sections 5.5.2, 5.5.3, and 5.5.4, respectively. A comparative analysis of the remedial regimes under the chosen legal systems will be conducted in section 5.5.5.

²⁷² Attention in this section will be paid to the remedies that permit an aggrieved franchisee to get an indemnity for the value of goodwill and to demand the franchisor to repurchase some tangible assets.

5.5.2 The Draft Common Frame of Reference (DCFR)

5.5.2.1 Introduction

In the DCFR, Book III contains model contract law provisions that entitle an aggrieved franchisee to enforce the franchisor's performance, recover monetary compensation and terminate a franchise contract. This section will examine the provisions governing these three private law remedies in subsections 5.5.2.2, 5.5.2.3, 5.5.2.4, respectively. Book IV contains model provisions that provide the franchisee with the right to compensation for a transfer of goodwill and the right to repurchase of stock, spare parts, and materials. The examination of these provisions will be made in 5.5.2.5. In the end, conclusions about the DCFR's remedial system will be provided in subsection 5.5.2.6.

5.5.2.2 Enforcement of performance

According to III. – 3:302(1), an aggrieved franchisee may enforce specific performance of the franchisor's obligation. In enforcing the franchisor's performance, the franchisee needs to prove that the franchisor owes the duty to perform to the franchisee.²⁷³ Taking the ICC's Model Contract as an example, clause 25.1AB provides that the franchisee is granted an option to enter into a new franchise contract upon satisfaction of some terms and conditions.²⁷⁴ In this case, the franchisor is obliged to enter into a new franchise agreement with the franchisee if the franchisee has satisfied the terms and conditions for the renewal. If the franchisor fails to renew a franchise agreement, the franchisor would be considered engaging in non-performance of the obligation. Consequently, the franchisor's non-performance would permit the franchisee's enforcement of specific performance of the obligation under clause 25.1AB.

The franchisee's right to enforce the franchisor's specific performance is not unqualified. The exercise of the right to enforce specific performance may be excluded in two occurrences.²⁷⁵ First, a franchisor may successfully raise defense by illustrating circumstances prescribed in para (3) of III. – 3:302. For instance, the franchisor may argue that it cannot renew a franchise contract because it has become bankrupt, which makes it financially impossible for the franchisor to continue a franchise relationship with the franchisee.²⁷⁶ Second, the franchisee may lose the right to enforce specific performance because of the time bar. According to III. – 3:302(4), the franchisee must enforce

²⁷³ The DCFR, III. – 1:102(1).

²⁷⁴ International Chamber of Commerce (n 12) 39.

²⁷⁵ However, the franchisee does not lose the right to damages. According to III. – 3:303, the franchisee may claim damages despite the exclusion of the right to enforce specific performance.

²⁷⁶ The DCFR, III. – 3:302(3)(a).

the franchisor's performance within a reasonable time after the franchisee has become, or could reasonably be expected to have become, aware of the franchisor's non-performance.²⁷⁷ In this case, the franchisee's failure to observe the prescription would exclude the right to demand the franchisor's performance.

5.5.2.3 Monetary compensation

Under the DCFR, a franchisee who suffers loss or damage may claim monetary compensation in the form of damages. The right to damages is provided both in Book III and in Book IV.²⁷⁸ The following two italicized headings will examine the requirements for the recovery of damages and the principles concerning a measure of damages.

– *Requirements for recovery of damages*

Firstly, an aggrieved franchisee may claim damages for the franchisor's non-performance of an obligation, which is not excused.²⁷⁹ In this regard, the franchisee may lose the right to damages if the franchisor's non-performance is justified. According to III. – 3: 104(1), the franchisor's failure to perform is excused if the franchisor's default results from an impediment beyond its control and if the franchisor could not reasonably be expected to have avoided or overcome that impediment. In reality, some supervening events may prevent the franchisor from performing its obligation. For example, the franchisee exercises an option to renew an existing franchise contract, which would require the execution of a new franchise contract in a written form. Suppose the franchisor or the franchisor's authorized representative cannot execute a new franchise contract due to travel restrictions amidst the COVID-19 pandemic. In this case, the franchisor's failure to conclude the new agreement would be excused because of these unforeseen circumstances; hence, the franchisee may not claim damages for the franchisor's non-performance of the obligation.

Secondly, an injured franchisee may seek an award of damages for the franchisor's termination with inadequate notice. As can be seen, IV.E. – 2:302(1)(2) requires the franchisor to provide the franchisee with a notice for a period of reasonable length when terminating a franchise contract for an

277 The DCFR does not provide any indication as to the reasonableness of the duration. In this regard, the franchisee needs to have recourse to the general principle in I. – 1:104. Under that section, the reasonableness shall objectively be determined, taking into account the nature and purpose of the obligation, the circumstances of the case, and any relevant usages and practices. In any case, this reasonableness should be decided on a case-by-case basis.

278 In the Definitions, damages are defined to mean a sum of money to which a person may be entitled to, or which a person may be awarded by a court, as compensation for some specified type of damage. See Bar and Clive (n 9) 68.

279 The DCFR, III. – 3:701(1).

indefinite term. IV.E. – 2:302(5) required the franchisor to observe a minimum period of notice.²⁸⁰ According to IV.E. – 2:303(1), the franchisee will be entitled to damages if the franchisor failed to observe these requirements.²⁸¹ Here I will take Illustration 1 to IV.E. – 2:303 as an analogous example in the franchising context. Assuming an indefinite franchise contract has lasted for four years, a franchisor is required to provide a franchisee with a four-month notice when terminating the agreement. Thus, the franchisor may be liable for damage if the franchisor gives the franchisee one month's notice.²⁸²

More importantly, when seeking damages in cases mentioned above, the claimant franchisee must prove that it has suffered loss or damage.²⁸³ According to paragraphs (2) and (3) of III. – 3:701, the recoverable loss or damage includes future loss that is reasonably likely to occur, economic and non-economic loss.²⁸⁴ Furthermore, there must be a causal link between the franchisee's loss or damage and the franchisor's unlawful conduct.²⁸⁵ That is, the franchisee has to demonstrate that the franchisor's non-performance of an obligation or the franchisor's termination with inadequate notice attributes to the loss or damage suffered. Thus, no award of damages will be granted if the franchisee does not suffer any loss or damage, or if the loss or damage suffered by the franchisee is not attributable to the franchisor's wrongful conduct.

– *Principles governing a measure of damages*

In Book III and Book IV, damages are compensatory in that the amount of money is not awarded to punish the damaging party.²⁸⁶ When calculating compensable damages, the general measurement of damages is relatively similar in that an aggrieved franchisee may recover some expectation interests. In claiming damages under III. – 3:701(1), a general measure prescribed by III. – 3:702 will apply. This article provides that the sum of money shall put the creditor as nearly as possible into the position in which the creditor would have been if the obligation had been duly performed. According to that article, the franchisee may claim damages for the loss of gains or profits caused by the franchisor's non-performance of an obligation.

A general measure formulated by IV.E. – 2:303(2) will apply to a claim for damages under IV.E. – 2:303(1). IV.E. – 2:303(2) provides that damages

280 The DCFR, IV.E. – 2:302(5).

281 Unless IV.E. – 2:303 provides otherwise, the general rules on damages for non-performance in Book III apply with any appropriate adaptations, pursuant to paragraph (4) of IV.E. – 2:303.

282 Bar and Clive (n 6) 2314.

283 Bar and Clive (n 9) 915.

284 The DCFR, III. – 3:701(2) and (3).

285 Bar and Clive (n 9) 916.

286 Ibid 68.

will be measured by the sum as corresponds to the benefit which the aggrieved party would have obtained during the extra period for which the relationship would have lasted if a reasonable period of notice had been given. Furthermore, IV.E. – 2:303(3) provides a special estimation of the benefit that would have been gained during the non-observed period of notice. The rule provides that the yearly benefit is presumed to be the average benefit that the injured party has obtained from the contract during the last three years. Nevertheless, the estimation is just a presumption. Thus, the average benefit may be increased or reduced, considering several factors, such as the aggrieved party's transfer benefit.²⁸⁷

5.5.2.4 Cancellation of a contract

An aggrieved franchisee may cancel a franchise contract by way of termination. In the context of this chapter, a franchisee may want to end a franchise relationship because a franchisor refuses to consent to a proposed transfer of a franchise contract, allowing the franchisee to leave a franchise relationship. In this case, terminating a franchise contract would benefit the franchisee as the franchisee can cease to pay payments, which are not due under a franchise contract. However, the franchisee may cancel a franchise contract, provided that the terms of the contract or the rules of the DCFR confer on the franchisee the right to terminate. The following three italicized headings will examine the franchisee's contractual and legal rights to terminate and the effects of exercising those rights.

– *Contractual right to terminate*

A franchise agreement may permit a franchisee to terminate the contract. In most cases, the franchisee has to provide the grounds for termination set out by the agreement. The termination clause of the ICC's Model Contract may be taken as an illustration. In the Model Contract, article 26.1 permits a franchisee to terminate a franchise contract in the case of the franchisor's substantial breach of obligations arising out of the agreement.²⁸⁸ In terminating a franchise agreement, the franchisee needs to demonstrate that the franchisor is required to perform under the franchise contract. For example, the franchisor is required to enter into a new franchise contract if the franchisee satisfies the preconditions for renewal.²⁸⁹ In this case, the franchisee may

287 Bar and Clive (n 6) 2313.

288 This clause conforms to IV.E. – 2:304(1). This article prevents the parties from incorporating the term of a contract that allows a party to terminate the contractual relationship for insubstantial non-performance. As can be seen, article 26.1 explicitly provides that a breach can be a basis for termination if it is substantial. Thus, this clause is enforceable under the DCFR.

289 The Model Contract, art. 25.1AB.

exercise the right to prematurely terminate a franchise contract if the franchisee loses faith in maintaining an existing relationship and wants to find a new franchise opportunity instead.

Additionally, the franchisee must plead that the franchisor's failure to perform is considered a substantial breach of an obligation. The Model Contract defines the term 'substantial breach' by reference to the test of substantial deprivation of the interest.²⁹⁰ Article 26.3 permits the parties to agree that a breach of particular contractual provisions is considered *prima facie* evidence of a substantial breach. In this case, the authors of the Model Contract recommend that the specification is limited to significant obligations. In any case, the franchisee has to allow the franchisor 30 days to remedy the breach, provided that the default is curable.²⁹¹

– *Legal right to terminate*

Despite the lack of the contractual right of termination, an aggrieved franchisee may terminate a franchise contract by resorting to the provisions governing termination of a contract. The application of these provisions depends upon types of the term of a franchise agreement.

(1) *Franchise contract for a definite period*

A aggrieved franchisee must have grounds for terminating a definite franchise contract. In Book III, the terminating franchisee may have to satisfy the requirements for termination of elaborated in III. – 3:502 to III. – 3:505. For example, the franchisee may choose to terminate the franchise agreement for the franchisor's fundamental non-performance under III. – 3:502. According to III. – 3:502(1), the franchisee has to plead that the franchisor's non-compliance with a franchise contract is substantial. In doing so, the franchisee may prove that the franchisor failed to perform its duty that substantially deprives the franchisee of what the franchisee was entitled to expect under the franchise contract. However, the franchisee must demonstrate that the franchisor foresaw or could reasonably be expected to have foreseen the substantial deprivation at the time of conclusion of the agreement.²⁹² Alternatively, the franchisee may terminate a franchise contract under III. – 3:502 by proving that the franchisor's non-performance is intentional or reckless and gives the franchisee reason to believe that the franchisor's future performance cannot be relied on.²⁹³

290 Article 26.2 defines a substantial breach to mean any failure by a party to carry out all or part of obligations under a franchise contract resulting in such detriment to the other party as to substantially deprive the other party of what it is entitled to expect under the contract. See International Chamber of Commerce (n 12) 40.

291 Ibid 40.

292 The DCFR, III. – 3:502(2)(a).

293 The DCFR, III. – 3:502(2)(b).

The franchisee may terminate a franchise contract for anticipated non-performance under III. – 3:504. According to that article, the franchisee needs to demonstrate the franchisor's anticipated non-performance, divided into two aspects. First, the franchisee may prove that, before the due date of performance of an obligation, the franchisor has declared that there will be no performance of the duty. Second, the franchisee may show that it is clear from the circumstances that there will be no performance.²⁹⁴ In both cases, the franchisor's non-performance of an obligation must be fundamental. In other words, only the franchisor's anticipated non-performance of the main obligation permits the franchisee to terminate a franchise contract under III. – 3:504.²⁹⁵

(2) *Franchise contract for an indefinite period*

An aggrieved franchisee may terminate an indefinite franchise contract irrespective of the franchisor's wrongful conduct. In terminating the franchise agreement, the franchisee has to follow the process prescribed by IV.E. – 2:302.²⁹⁶ According to paragraph (1) of IV.E. – 2:302, the franchisee must give the franchisor the notice of termination. The franchisee needs to observe the requirement of a reasonable period for notice to avoid liability for damages.²⁹⁷ Whether the notice is reasonably given depends upon the four factors prescribed by paragraph (3) of IV.E. – 2:302. According to IV.E. – 2:302(3), the franchisee may have to consider (a) the time the franchising relationship has lasted, (b) the reasonable investments made by the franchisor, (c) the time it will take to find a reasonable alternative, and (d) other usages.²⁹⁸

– *Effects of termination*

The plain effect of the valid termination of a franchise contract is that the franchise relationship between the franchisor and the franchisee will be dissolved. Furthermore, the termination will end the relationship with future

294 For example, the franchisor may terminate a franchise contract, alleging the franchisee's minor non-performance of duties. As examined in subsection 5.4.2.3, the DCFR regulates the termination of a definite franchise contract for non-performance. In this respect, the parties may agree to terminate the agreement only for the other party's fundamental non-performance of an obligation. Thus, the franchisor's termination of a franchise contract for the franchisee's minor non-performance of an obligation is deemed to be wrongful. In this case, the franchisor's wrongful termination could permit the franchisee to terminate the agreement for the franchisor's anticipated non-performance under III. – 3:504. Suppose the franchisor actually abandons a franchise relationship after committing the wrongful termination. In this case, the franchisee may also terminate a franchise contract on the basis of the franchisor's actual non-performance of an obligation in III. – 3:502.

295 Bar and Clive (n 9) 868.

296 This article is applied in the franchising context by virtue of IV.E. – 1:101(1).

297 The DCFR, IV.E. – 2:303.

298 Unlike the case of the franchisor's termination, the franchisee's termination of an indefinite franchise contract is not subject to the minimum period requirement prescribed by IV.E. – 2:302(5).

effect.²⁹⁹ According to III. – 3:509(1), the franchisor and the franchisee will be released from any outstanding obligation under a franchise agreement. According to the drafters of the DCFR, the term ‘outstanding obligation’ refers to an unperformed obligation. That is, the obligation is outstanding if it is not performed in a way that conforms with the terms of the contract.³⁰⁰ For instance, the termination will discharge the franchisee from an obligation to pay upcoming royalty fees. III. – 3:509(3) affirms that the franchisee will never lose the right to damages for the franchisor’s non-performance that is the basis for the franchisee’s termination.

In practice, a franchise contract may play a supplementary role in elaborating on obligations upon termination. Those duties are likely to be placed on the franchisee. Taking the ICC’s Model Contract as an example, article 27 provides for the effects upon termination.³⁰¹ Upon the termination of a franchise contract, the franchisee may be required to perform some obligations. For example, the franchisee shall immediately remove any material indicating a relationship with the franchisor from the franchised premises or other locations and stop using the franchise system or names or trademarks that may cause confusion.³⁰² Furthermore, the franchisee shall immediately return all materials, including the manual, instructions, profile material, to the franchisor.³⁰³ Besides, the franchisee shall promptly pay all outstanding sums to the franchisor.³⁰⁴

5.5.2.5 *Specific remedies*

The DCFR provides a franchisee with the following remedial rights upon the cessation of a franchise relationship. In Book IV, IV.E. – 2:305 and IV.E. – 2:306 confer on the franchisee the right to compensation for a transfer of goodwill and the right to repurchase of stock, spare parts and materials, respectively.³⁰⁵ This subsection will examine those entitlements and make some remarks on the character of the remedial provisions in the following three italicized headings.

299 Bar and Clive (n 9) 887.

300 Ibid 886.

301 Ibid 41.

302 The Model Contract, art. 27.2.

303 The Model Contract, art. 27.3.

304 The Model Contract, art. 27.4.

305 These two provisions are applied to the end of a franchise relationship by virtue of IV.E. – 1:101(1).

– *The right to indemnity for goodwill*

According to IV.E. – 2:305(1), the franchisee may claim an indemnity for the transfer of goodwill against the franchisor.³⁰⁶ The drafters of the DCFR explain that the idea behind the establishment of the right is that the goodwill has its own value that should always be refunded when a contractual relationship is ended.³⁰⁷ In claiming the indemnification of goodwill, the franchisee has to demonstrate that a franchise relationship comes to an end. Nevertheless, the way the relationship is ended is irrelevant. In other words, a mere fact that the franchise relationship ceases to exist would suffice.³⁰⁸ Thus, the franchisee would be entitled to the indemnity for goodwill if an existing franchise relationship is extinguished because of transfer, non-renewal, and termination of the franchise contract.

The franchisee needs to satisfy the following two prerequisites when claiming an indemnity for the value of goodwill.

The first requirement is that the franchisee has generated goodwill that is transferred to the franchisor. According to IV.E. – 2:305(1), the franchisee must prove that it has significantly increased the franchisor's volume of business. However, it might be difficult for the franchisee to plead that it has played an active role in generating goodwill. According to the drafters of the DCFR, customers of a franchised store are attracted by the image of the franchise brand and the network. In that case, it can be said that the franchisee does not meaningfully increase the franchisor's volume of the franchise business.³⁰⁹ Besides, the franchisee must prove a transfer of goodwill. That is, the franchisee needs to demonstrate that the franchisor continues to derive substantial benefits from the generated goodwill.³¹⁰ In the franchising context, the drafters of the DCFR exemplify that a transfer of goodwill takes place when the franchisor has acquired the lists of clients and other equivalent information during, or at the end of, the relationship.

The second requirement is concerned with the reasonableness test. According to IV.E. – 2:305(b), the payment of the indemnity must be reasonable.³¹¹ According to the drafters of the DCFR, the test of reasonableness is prescribed by I. – 1:104. In this case, the franchisee must show that the indemnity for the transfer of goodwill is objectively reasonable, taking into account the nature and purpose of what is being done, the circumstances of the case, and any relevant usages and practices.³¹² Unlike the case of commercial agency, no

306 The DCFR, IV.E. – 2:305(1).

307 Bar and Clive (n 6) 2321 – 322.

308 Ibid 2322.

309 A franchisee may claim compensation for goodwill if the franchisee has created the market for the franchisor's products. See *ibid* 2322 – 323.

310 The DCFR, IV.E. – 2:305(1)(a).

311 The DCFR, IV.E. – 2:305(1)(b).

312 Bar and Clive (n 6) 2323.

rule of Book IV provides a specific formula for calculating the reasonable amount of the indemnity in the franchising context.³¹³ Thus, the extent to which the amount is reasonable will be determined on a case-by-case basis, considering the circumstances of the case.

– *The right to repurchase of stock, spare parts and materials*

According to IV.E. – 2:306, a franchisee may be entitled to the repurchase of the excess stock, spare parts, and other materials. The franchisee will hold the right to repurchase if a franchise relationship is ended because of the franchisor's avoidance and termination. In other words, the franchisee will not have the right to repurchase if the franchise agreement comes to an end because of the franchisor's non-renewal of a franchise agreement. The rationale behind the provision is that, in the case of pre-mature avoidance or termination, a franchisee may lose the right to use or resell some items because of post-contractual non-compete clauses. Thus, the policy should be that the franchisor bears an obligation to repurchase the assets from the franchisee.³¹⁴

When repurchasing the remaining items, the franchisor is required to pay a reasonable price. The drafters of the DCFR provide that the price may be measured by referring to the price that the franchisor can resell the objects in question to new franchisees.³¹⁵ Nevertheless, IV.E. – 2:306 grants an exemption for the franchisor. The franchisor will have no obligation to buy back stock, spare parts, and materials if the franchisor proves that the franchisee can reasonably resell the objects. In this regard, the drafters of the DCFR define the term 'reasonably' to mean reselling without great effort, for a reasonable price and within a reasonable time. For example, the franchisor does not have an obligation to repurchase if the franchisee has an opportunity to use the remaining items or to resell them to the public or other franchisees.³¹⁶

– *Remarks on the character of the remedial rules*

Neither IV.E. – 2:305 and IV.E. – 2:306 nor their commentaries elaborate on the character of the rules. Clarifying the nature of these specific remedies would be vital for the franchisor and the franchisee to be certain whether they can contract around the rule's application by the terms of a franchise agreement. From my viewpoint, it could be argued that IV.E. – 2:305 and IV.E. – 2:306 are provisions that offer default rules. The reason is that those two provisions do not indicate that the rules are made mandatory, nor are the

313 In the context of commercial agency, IV.E. – 3:312 provides a method for measuring the amount of indemnity for which the agent may claim under IV.E. – 2:305.

314 Bar and Clive (n 6) 2329.

315 Ibid 2330.

316 Ibid 2330-331.

provisions intended to limit any derogation from rules. Furthermore, the DCFR always makes clear if model provisions are made mandatory. For example, IV.E. – 4:202(1) requires the franchisor to provide the franchisee with the know-how, which is necessary to operate the franchise business. In this article, paragraph (2) expressly states that the parties may not exclude the application of that requirement or derogate from or vary its effect.

Therefore, it could be concluded that the franchisor and the franchisee may exclude the application of IV.E. – 2:305 and IV.E. – 2:306. Alternatively, the parties may derogate from or vary the effects of the provisions. Taking the ICC's Model Contract as an illustration, article 28 provides that the franchisee cannot indemnify for the value of goodwill or similar compensation in the case of termination of the agreement.³¹⁷ However, the exclusion under article 28 is applicable in the case a franchise contract is terminated by the exercise of the right to terminate under the agreement. In other words, the franchisee may be entitled to the remedy under IV.E. – 2:305 if a franchise contract comes to an end under other circumstances, such as termination of a contract by the rules of contract law.

5.5.2.6 Conclusions

In the DCFR, an aggrieved franchisee may resort to contract law remedies in Book III that permit the franchisee to enforce the franchisor's specific performance, claim damages, and terminate a franchise contract. Nevertheless, these three contract law remedies are ordinarily the remedies for non-performance of an obligation. In this case, the franchisee usually must plead that the franchisor engages in fundamental non-performance of an obligation when seeking the remedies. Additionally, the remedial provisions in Book IV provide the franchisee with special protection of intangible and tangible assets. Under the specific rules, the franchisee may be entitled to an indemnity from the franchisor for the value of goodwill upon the cessation of a franchise relationship. In the event of the franchisor's termination, the franchisee may ask the franchisor to repurchase the remaining stock, spare parts, and materials.

5.5.3 The United States of America (USA)

5.5.3.1 Introduction

The US legal system allows an aggrieved franchisee to compel the franchisor's performance and forbearance, claim monetary compensation and cancel a franchise contract under common law and franchise relationship law. This section will examine the rules of common law and franchise-specific law

317 International Chamber of Commerce (n 12) 42.

regulating those private law remedies in subsections 5.5.3.2, 5.5.3.3, and 5.5.3.4, respectively. In some relationship states, franchise relationship law entitles the franchisee to compensation for the value of goodwill and the repurchase of some tangible items. These specific remedies will be explored in subsection 5.5.3.5. Conclusions about the US remedial system will be made in subsection 5.5.3.6.

5.5.3.2 Enforcement of performance

In most US states, an aggrieved franchisee may compel the franchisor's action and inaction by seeking specific performance and injunctive relief under common law rules. Some relationship states may make these remedies available under state franchise relationship law. The following two italicized headings will examine the enforcement of the franchisor's performance under common law and franchise relationship laws.

– *Specific performance and injunctions under common law*³¹⁸

In common law, the franchisee may seek a decree of specific performance in contract to enforce the franchisor's action. In this respect, the existence of the franchisor's breach of contract is imperative. Thus, the claimant franchisee needs to prove that the franchisor fails to comply with the terms of a franchise agreement that impose obligations on the franchisor. Failure to prove the franchisor's breach of contract would not entitle the franchisee to the remedy of specific performance. For example, in the case *Shred-It America*, the appellate court affirmed the lower court in concluding that the franchisor breached the franchise contract by failing to timely submit proposed renewal terms to the franchisee and ordering specific performance that resulted in renewing the contract at the original royalty rate.³¹⁹

Nonetheless, the claimant franchisee may not succeed in seeking specific performance. As mentioned in chapter 4, courts may refuse to decree specific performance because, for example, a franchise contract is a personal service contract. In Florida, the court in *Burger King Corp v Agad* provided that, under Florida law, a franchise contract was not subject to a claim for specific performance because of the nature of personal service contracts. Consequently, the franchisee could not compel the franchisor to enter into a new franchise contract upon the expiry of an existing franchise agreement.³²⁰ However, there is still room for a grant of specific performance in the franchising context.

318 This heading should be read in conjunction with subsection 4.4.3.2 in chapter 4, which has generally reviewed contract law rules on the remedy of specific performance and injunctions in the USA at the state level.

319 *Prudence Corp v Shred-It Am, Inc*, 365 F App'x 859 (9th Cir 2010) 860.

320 *Burger King Corp v Agad* 911 F Supp 1499 (SD Fla, 1995) 1506.

An aggrieved franchisee may seek an order of specific performance if the franchisee can demonstrate the inadequacy of a remedy of damages.³²¹ In any event, it would seem that there has been no case law to exemplify how a court refuses to grant specific performance in the context of this chapter.

In common law, an aggrieved franchisee may also sue the franchisor for injunctive relief, enjoining the franchisor from doing something, such as terminating a franchise agreement.³²² Taking the most cited case *Semmes Motors v Ford Motor* as an example, the New York Court of Appeals held that the dealer (franchisee) was entitled to a grant of a temporary injunction against wrongful termination of the manufacturer (franchisor). In this case, the court found that the right to continue a business in which the dealer (franchisee) had engaged for two decades and into which the son of the dealer had entered was not measurable entirely in monetary terms. Moreover, the hardship to the franchisor in continuing a relationship with the franchisee was relatively small.³²³ In many cases, courts deny granting an injunction because the franchisees fail to prove the condition of irreparable injury. In those cases, the courts typically find that money damages suffice to redress any loss incurred by the franchisees.³²⁴

– *Specific performance and injunctions under state franchise relationship law*

In some relationship states, an aggrieved franchisee may compel the franchisor's action and inaction by seeking an order of specific performance and injunctions under franchise relationship laws. For example, in New Jersey, it is said that the franchise relationship statute permits a grant of specific performance. In *VW Credit v Coast Automotive Group*, the court found that the franchisor unreasonably refused to consent to the franchisee's proposed transfer in violation of the New Jersey Franchise Practices Act. In this case, the court broadly interpreted that the Franchise Practices Act contemplated a remedy of specific performance in which the franchisee might enforce a transfer of a franchise.³²⁵ In Missouri, the franchisor's failure to comply with the rules of the franchise law will expose the franchisor to equitable relief, the remedy

321 *Pepsi-Cola Bottling Co of Pittsburg, Inc v PepsiCo, Inc*, 175 F Supp 2d 1288, (D Kan, 2001) 1294-295.

322 *Bray v QFA Royalties LLC* 486 F Supp2d 1237 (D Colo, 2007) 1241.

323 *Semmes Motors Inc v Ford Motor Co* 429 F2d 1197 (CANY, 1970) 1205.

324 See eg *C-B Kenworth Inc v General Motors Corp* 675 F Supp 686 (D Me, 1987) 686-87; *Augusta News Co v News America Pub Inc* 750 F Supp 28 (D Me, 1990) 32; *Foreign Motors Inc v Audi of America Inc* 755 F Supp 30 (D Mass, 1991) 33; *Clemente v Pearle Vision Inc* 762 F Supp 1518 (D Me, 1991) 1519; *Mfr Direct LLC v DirectBuy, Inc*, No 2:05-CV-451, 2006 WL 319254 (ND Ind Feb 10, 2006) 7.

325 *VW Credit* (n 17) 341-42. Moreover, the construction of the court in *VW Credit v Coast Automotive Group* has been followed by subsequent cases. See eg *Crawford v SAP America Inc* 147 Fed Appx 234, 237, 2005 WL 775802 (CA3 (Pa), 2005) 2; *Maple Shade Motor Corp v Kia Motors America Inc* 2006 WL 2320705 (DNJ, 2006) 4.

of which courts have interpreted to include injunctions. This remedy can be issued to enforce the franchisor's action. In practice, some courts may grant injunctive relief to compel the franchisor to continue to do business with the franchisee, provided that the franchisor fails to notify the franchisee in writing at least ninety days in advance of the cancellation or termination.³²⁶

Besides enforcing specific performance, an aggrieved franchisee may prevent the franchisor from engaging in certain conduct by claiming injunctions under franchise relationship law. For instance, in California, section 20035(b) of the Franchise Relations Act states that a court may grant preliminary and permanent injunctions for a violation or threatened violation of the law. In the litigation, the franchisee may strategically request injunctive relief to restrain the franchisor from terminating a franchise agreement.³²⁷ Nevertheless, injunctions are, by nature, equitable remedies. Thus, the availability of the relief depends upon the satisfaction of certain preconditions, which may vary from state to state. Despite the variation, a claimant franchisee may need to satisfy the widely-accepted four-factor test.³²⁸ For example, the Delaware court in *Sandhu v 7-Eleven* conceded that the plaintiff franchisee had to demonstrate the following four elements to prevent the franchisor from wrongfully terminating a franchise contract. First, the franchisee must show that there is some probability that the franchisor is attempting to terminate the franchise in bad faith or without just cause. Second, the franchisee will suffer irreparable harm if the injunction is denied.³²⁹ Third, the franchisor will not be caused greater harm because of the relief. Fourth, the public interest favors injunctive relief.³³⁰

326 See eg *Maude v General Motors Corp* 626 F Supp 1081, 1086 (WD Mo, 1986) 1086; *In re Tornado Pizza LLC* 431 BR 503, 517 (Bkrtcy D Kan, 2010) 517.

327 *Mahroom v Best Western Intern Inc* 2009 WL 2216578 (ND Cal, 2009) 4.

328 See eg *C-B Kenworth* (n 324) 686-87; *Augusta News* (n 324) 32; *Clemente* (n 324) 1519; *Foreign Motors* (n 324) 33; *Bray* (n 322) 1241; *Dunkin' Donuts Franchised Restaurants LLC v D & D Donuts Inc* 566 F Supp2d 1350 (MD Fla, 2008) 1355; *Romper Room Inc v Winmark Corp* 60 F Supp 3d 993 (ED Wis, 2014) 995-96; *Winmark Corp v Brenoby Sports Inc* 32 F Supp3d 1206 (SD Fla, 2014) 1218; *7-Eleven Inc v Grewal* 60 F Supp3d 272 (D Mass, 2014) 279.

329 In practice, several factors can be used to show that the franchisee is likely to suffer irreparable harm. For example, in *Romper Room v Winmark*, the court identified some suggestive factors, including the five following facts:

- (1) the franchisee will become insolvent;
- (2) any award of damages would be too late to save the franchisee's business;
- (3) the franchisee cannot fund its lawsuit against the franchisor without income from the franchise business;
- (4) it is difficult or impossible to calculate damages because of the nature of the franchisee's losses; and
- (5) damages may not be recoverable from the franchisor because the franchisor might become insolvent before the entry of judgment. See *Romper Room*, *ibid* 996.

330 *Sandhu v 7-Eleven Inc* 45 F Supp3d 426 (D Del, 2014) 429-30.

5.5.3.3 Monetary compensation

A franchisee who has incurred loss or damage may claim damages against the franchisor. In all US states, the franchisee may resort to state common law rules when seeking damages.³³¹ In some relationship states, the franchisee may claim damages under the rules of franchise relationship legislation. The following two italicized headings will examine the requirements for recovering common law and statutory law damages and the principles governing a measure of two types of damages.

– Requirements for recovery of damages

Firstly, an injured franchisee may bring an action for damages for breach of contract.³³² In seeking contract law damages, it would be imperative for the franchisee to prove the franchisor's breach of a franchise contract; otherwise, the franchisee would fail to claim monetary compensation against the franchisor. For example, in *Kumon North America v Timban*, the franchisee claimed that the franchisor breached a franchise contract by terminating the agreement and failing to approve the transfer of the franchisee's business. The court found that, first, the franchisor's termination was justified because the franchisee had failed to pay the due royalties. Second, the franchisor was not required by the terms of a franchise agreement to approve any transfer. Conversely, the transfer was conditional upon the franchisor's prior consent. Consequently,

331 An aggrieved franchisee may also resort to a remedy of damages under other legal frameworks. For example, the franchisee may claim treble damages under section 4 of the Clayton Act (15 USCA § 15(a)). In claiming antitrust damages, the franchisee may have to prove that it has suffered loss or damage because of the franchisor's conduct, and the franchisee is better situated to bring a claim. See *Doctor's Hospital of Jefferson Inc v Southeast Medical Alliance Inc* 123 F3d 301 (CA5 (La), 1997) 305. The loss or damage sustained must be an antitrust injury, which is an injury that the antitrust laws aim to prevent and results from the franchisor's anticompetitive acts. See *Brunswick Corp v Pueblo Bowl-O-Mat Inc* 97 S Ct 690, 697, 429 US 477 (USNJ, 1977) 489. In establishing the franchisor's unlawful conduct, the franchisee may demonstrate that the franchisor has engaged in the practice of unreasonable restraint of trade in light of section 1 of the Sherman Act, which has been examined in subsection 4.2.3.3 of chapter 4 that it may apply to a franchise relationship. See *State Oil Co v Khan* 118 S Ct 275, 279, 522 US 3 (US Ill, 1997) 10. In this case, the franchisee must plead that the franchisor's concerted action has produced anticompetitive effects within the relevant products and geographic markets, and the franchisor's action is illegal. See *Queen City Pizza Inc v Domino's Pizza Inc* 124 F3d 430 (CA3 (Pa), 1997) 442. In the context of this chapter, the franchisee may bring an antitrust cause of action if the franchisor terminates a franchise contract because the franchisee failed to comply with tying provisions that violate the antitrust laws. See *Osborn v Sinclair Refining Co* 324 F2d 566 (CA Md, 1963) 571. Besides, exclusive dealing, such as exclusive territories, which have been examined in chapter 4, is another example that could lead to violation of antitrust law rules.

332 Subsection 4.4.3.3 in chapter 4 has addressed general requirements for claiming damages for breach of contract under common law. These requirements will also apply in the case of claiming damages in the context of this chapter.

the court concluded that the franchisor's conduct did not constitute a failure to perform and dismissed the franchisee's claim for breach of contract.³³³

Secondly, in sixteen relationship states, an injured franchisee may bring an action for the franchisor's violation of franchise relationship laws to recover damages.³³⁴ Some relationship states may not provide the right to damages for all violations of the law. Taking California as an example, the Franchise Relations Act regulates transfer, non-renewal, and termination of a franchise. However, the law provides the franchisee with the right to damages only in the case of the franchisor's violation of non-renewal and termination rules.³³⁵ In other words, the franchisee cannot resort to a remedy of damages if the franchisor contravenes the rules concerning transfer.³³⁶

As mentioned above, the franchisee's entitlement to statutory damages is primarily based on the franchisee's suffering damage because of the franchisor's contravention of the franchise relationship law rules. In this case, courts may play a significant role in construing the franchise rules to establish the franchisor's contravening conduct. In some cases, the courts' construction may be extensive. For example, in Indiana, the plain language of the franchise statute proscribes any provision in a franchise agreement that provides unilateral termination of a franchise without good cause or bad faith. However, the Supreme Court of Indiana in *Continental Basketball Association* interpreted the rule broadly. According to the court's decision, the franchisor was considered in violation of the Indiana franchise law if the franchisor actually terminated a franchise contract without good cause, irrespective of whether the franchisor did exercise the right to terminate under a franchise contract.³³⁷

333 *Kumon North America Inc v Timban* 2014 WL 2812122 (DNJ, 2014) 6 – 7.

334 Arkansas: AR ST, § 4-72-208(b); California: CA BUS & PROF, § 20035(a); Connecticut: CT ST, § 42-133g(a); Delaware: DE ST TI 6, § 2553(a); Hawaii: HI ST, § 482E-6, in conjunction with § 480-13(a)(1); Illinois: IL ST CH 815, § 705/26; Indiana: IN ST, 23-2-2.7-4; Iowa: IA ST, § 523H.13 and IA ST, § 537A.10(13); Mississippi: MS ST, § 75-24-53, in conjunction with § 75-24-15(1); Missouri: MO ST, 407.410(1); Nebraska: NE ST, § 87-409; New Jersey: NJ ST, 56:10-10; Rhode Island: RI ST, § 6-50-7; Virginia: VA ST, § 13.1-571(a); Washington: WA ST, 19.100.190(2); and Wisconsin: WI ST, 135.06.

335 CA BUS & PROF, § 20035(a).

336 Elizabeth M Weldon and Nicole Liguori Micklich, 'Strange Weather: California's Amended Franchise Relations Act, AB 525' (2016) 35 Franchise Law Journal 577, 590. In this case, the injured franchisee may have recourse to a remedy of damages under other theories, such as a claim for damages for breach of contract. Under the Franchise Relations Act, section 20037 provides that a franchisee is not abrogated the right to sue the franchisor under any other law. Therefore, the franchisee may seek damages in contract instead insofar as the franchisee satisfies the requirements for an award of damages. See eg *JRS Products Inc v Matsushita Electric Corp of America* 8 Cal Rptr 3d 840, 845, 115 Cal App4th 168 (Cal App 3 Dist, 2004) 174; *Mahroom v Best Western International Inc* 2010 WL 11575097 (ND Cal, 2010) 9.

337 *Continental Basketball Ass'n Inc v Ellenstein Enterprises Inc* 669 NE2d 134 (Ind, 1996) 139.

– Principles governing a measure of damages³³⁸

Contract law and statutory damages are compensatory. This statement implies that an injured franchisee generally cannot claim punitive damages under contract law or franchise relationship statutes. There is an exception to the general principle mentioned in the preceding paragraph. An injured franchisee may recover punitive damages under some state franchise relationship statutes. For example, in Washington, an injured franchisee may sue the franchisor for punitive damages.³³⁹ Under the Washington Franchise Investment Protection, the franchisor's violation of the rule on termination constitutes a *per se* unfair or deceptive act or practice. This unlawful conduct is, in turn, actionable under the Washington Consumer Protection Act.³⁴⁰ Under the Washington Consumer Protection Act, courts can award punitive damages. That is, upon the court's discretion, the injured franchisee can recover damages up to an amount not to exceed three times the actual damages sustained, according to section 19.86.090.³⁴¹

Common law and franchise relationship law differ slightly when it comes to measuring damages. In common law, the general principle is that contract law damages are awarded to put the plaintiff into as good a pecuniary position as it would have had if there had been no breach of contract. Conversely, the state franchise relationship laws do not explicitly establish a general measure of damages. In this case, courts are permitted to find a proper standard for calculating damages. In any case, some state franchise relationship statutes choose to specify that certain types of loss or damage are recoverable under the laws. For example, the Delaware statute permits the franchisee to recover damages from the franchisor in the event of the franchisor's unjust termination or non-renewal of a franchise. In calculating damages, the law explicitly provides a non-exhaustive list of recoverable damages. In the list, the recoverable damages include the loss of goodwill and the loss of profits.³⁴²

338 The principles governing a measure of damages have been reviewed in subsection 4.4.3.3 of chapter 4. These principles hold in the context of this chapter.

339 See *eg Saleemi v Doctor's Associates Inc* 292 P3d 108, 115, 176 Wash2d 368 (Wash, 2013) 383; *BBC Group NV LLC v Island Life Restaurant Group LLC* 2020 WL 758070 (WD Wash, 2020) 7.

340 See *eg Nelson v National Fund Raising Consultants Inc* 842 P2d 473, 478, 120 Wash 2d 382 (Wash, 1992) 393; *Doyle v Nutrilawn US Inc* 2010 WL 1980280 (WD Wash, 2010) 7; *Volvo Const Equipment North America LLC v Clyde/West Inc* 2014 WL 5365454 (WD Wash, 2014) 4.

341 When seeking punitive damages, the claimant franchisee needs to show that the franchisor's unfair or deceptive practice occurs in trade or commerce, which has an impact on the public interest. Besides, the franchisee must demonstrate that the franchisor's alleged conduct injures the franchisee's business and property, and there is a causal link between the act and the injury sustained. See *eg Nelson*, *ibid* 393; *Volvo Const Equipment North America*, *ibid* 4; *Noble Roman's Inc v Hattenhauer Distributing Company* 307 F Supp3d 907 (SD Ind, 2018) 926; *Wetzel v CertainTeed Corporation* 2019 WL 3976204 (WD Wash, 2019) 6.

342 DE ST TI 6, § 2553(c)(3).

5.5.3.4 *Cancellation of a contract*

An aggrieved franchisee may put an end to a franchise relationship by cancelling a franchise contract because, for example, the franchisor's refusal to a transfer of a franchise makes it impossible for the franchisee to leave the relationship through a transfer. In this case, the franchisee may cancel a franchise contract by exercising the right to terminate under the terms of the agreement. Without the contractual right to terminate, the franchisee may resort to common law rules to rescind or terminate a franchise agreement. This subsection will examine the franchisee's cancellation of a franchise contract under the terms of a franchise contract, as well as rescission and termination in common law, and explore their effects in the following three italicized headings.

– *Contractual right to terminate*

A franchise contract may include the terms that confer on the franchisee the right to terminate. This conferment may vary from contract to contract. In some cases, a franchise contract may permit a franchisee to terminate a franchise contract without cause. For example, a franchise contract may allow the franchisee to terminate the agreement at will by giving the franchisor prior notice of termination.³⁴³ Nevertheless, a franchisee is typically required to terminate a franchise contract for cause, particularly for the franchisor's breach of the agreement. For example, the ABA's Annotated Franchise Agreement provides that the franchisee may terminate a franchise agreement because of the franchisor's breach of a material provision of the contract. In terminating the contract, the franchisee shall provide the franchisor with a written notice that identifies grounds for the breach and allow the franchisor to cure the breach within 30 days after the receipt of the notice.³⁴⁴

– *Rescission and termination in common law*

In many cases, a franchise agreement may not provide the franchisee with the right to terminate.³⁴⁵ Despite the absence of the right, an aggrieved franchisee may resort to remedies that enable the franchisee to dissolve a franchise relationship under common law.³⁴⁶ In common law, the franchisee

343 Appleby and Rosario (n 227) 223. *See also Sensormatic Sec Corp* (n 186) 715.

344 Appleby and Rosario, *ibid* 222.

345 *Ibid* 223.

346 *See eg Manpower Inc v Mason* 377 F Supp2d 672 (ED Wis, 2005) 679; *Haman Ents Inc v Sharper Impressions Painting Co* 50 NE3d 924, 929, 2015 -Ohio- 4967 (Ohio App 10 Dist, 2015) 929. In contrast to common law, state franchise relationship laws do not allow an aggrieved franchisee to bring an action for rescission in the case of the franchisor's violation of the rules regulating the three exit issues. In some relationship states, such as Indiana, the court

may cancel a franchise contract for an indefinite period by way of termination and terminate a franchise contract for a definite term by way of rescission.

(1) *Franchise contract for a definite period*

An aggrieved franchisee may also resort to common law rules to rescind a franchise agreement with a fixed term.³⁴⁷ In short, the franchisee may seek rescission of a franchise contract only in the case of the franchisor's material breach or repudiation of the agreement. For example, the franchisee may rescind a franchise agreement if the franchisor fails to perform by refusing to renew the term of the contract or by wrongfully terminating the contract. Sometimes, the franchisee may not succeed in seeking an award of rescission if, for example, the franchisee is presumed to waive the right to rescind. Since rescission is an equitable remedy, courts hold discretion in awarding the remedy of rescission. For instance, some courts may determine the adequacy of a remedy at law by ascertaining whether the legal remedy is complete and not uncertain.³⁴⁸

(2) *Franchise contract for an indefinite period*

In the context of indefinite commercial contracts, state courts typically imply the theory of at-will termination if the parties do not specify the process of termination.³⁴⁹ This doctrine could be employed in the franchising context. In brief, the franchisee may terminate an indefinite franchise relationship at any time for any or even for no reason.³⁵⁰ In other words, the franchisee needs not to plead on the franchisor's breach of a contract as a basis for termination. Nevertheless, the franchisee may have to observe a reasonable period requirement before terminating the agreement. Besides, the franchisee may have to provide the franchisor with reasonable notice of termination.³⁵¹

makes clear that the invalidation of a franchise contract is not a remedy under the Franchise Practices Act. See *Gre-Ter Enterprises Inc v Management Recruiters International Inc* 329 F Supp3d 667 (SD Ind, 2018) 679.

347 This chapter has examined the common law rules governing the franchisor's rescission of a contract for a definite term is made in 5.4.3.3. These common law rules are equally be applied in the context of the franchisee's rescission of a franchise agreement.

348 See eg *Powers v Fisher* 272 NW 737, 739, 279 Mich 442 (Mich, 1937) 447; *Steggles v National Discount Corp* 39 NW2d 237, 239, 326 Mich 44 (Mi, 1949) 49.

349 Rachel Arnow-Richman, 'Mainstreaming Employment Contract Law: The Common Law Case for Reasonable Notice of Termination' (2014) 66 Florida Law Review 1513, 1546.

350 Blair and Lafontaine, *The Economics of Franchising* (n 228) 276.

351 This chapter has examined common law rules governing the franchisor's termination of a contract for an indefinite term in 5.4.3.3. Those rules may equally be applied in the context of the franchisee's termination of an indefinite franchise contract.

– *Effects of termination and rescission*

Termination and rescission of a franchise contract similarly put an end to a franchise relationship. However, the remedies of termination and rescission may differ in terms of temporal ramifications.³⁵² In brief, the remedy of termination is the exercise of power to cancel a contract that has a prospective effect. In this case, both parties may sue the other party to enforce any obligation accrued before the termination is effective. Conversely, rescission is an equitable remedy that extinguishes a contract retrospectively as if the agreement never exists. As a result of the successful rescission, the *status quo ante* of the parties will be restored.

5.5.3.5 *Specific remedies*

A franchise contract may protect some properties of the franchisee upon termination of the contract. For example, the ABA's Annotated Franchise Agreement requires the franchisor to purchase from the franchisee all or any portion of the inventory held by the franchisee for the purpose of sale or distribution in a franchised business upon the termination of a franchise agreement.³⁵³ The terms of a franchise contract may not be protective of a franchisee since a franchisor may be permitted to decide if the franchisee's inventory is bought. In this case, some states may protect the franchisee by the rules of law. In America, some relationship states offer a franchisee the following auxiliary remedies under franchise relationship law: the right to repurchase and the right to compensation for goodwill. These two remedies are said to provide a franchisee with greater protection.³⁵⁴ The following three italicized headings will examine these remedies and the events that trigger the right to the remedies.

– *Right to repurchase*

Franchise relationship law of eight relationship states requires the franchisor to repurchase some assets possessed by the franchisee.³⁵⁵ This requirement aims to protect a franchisee from possessing a useless item at the time of

352 An overview of the difference between the effects of termination and rescission has been provided in subsection 4.4.3.4 in chapter 4.

353 Appleby and Rosario (n 227) 226.

354 See eg *American Standard Inc v Miller Engineering Inc* 772 SW2d 344, 347, 299 Ark 347 (Ark, 1989) 351; *Chem-Tek Inc v General Motors Corp* 816 F Supp 123 (D Conn, 1993) 128; *Devore v H&R Block Tax Services LLC* 2016 WL 11520668 (CD Cal, 2016) 2.

355 Arkansas: AR ST, § 4-72-209; California: CA BUS & PROF, § 20022; Connecticut: CT ST, § 42-133f(c); Hawaii: HI ST, § 482E-6(3); Michigan: MI ST, 445.1527(d); Rhode Island: RI ST, § 6-50-5; Washington: WA ST, 19.100.180(i); and Wisconsin: WI ST, 135.045.

termination.³⁵⁶ Under the laws, the items to be repurchased ordinarily include inventory, supplies, equipment, and furnishings.³⁵⁷ In general, these properties must be those the franchisee bought from the franchisor or the approved supplier. In evaluating the value of those assets, a standard for the assessment may vary among the eight states. For instance, under the law of Hawaii and Washington, the franchisor shall compensate the franchisee for the fair market value of the specified items. Likewise, the statute of Rhode Island opts for a similar measure, that is to say, the fair wholesale market value.

– *Right to compensation for goodwill*

Franchise relationship law of four relationship states entitles a franchisee to compensation for the value of goodwill.³⁵⁸ In Hawaii and Washington, the franchise statutes provide that the franchisor must compensate the franchisee for the loss of goodwill.³⁵⁹ In California and Illinois, the laws require the franchisor to compensate the franchisee for the value, or diminution in the value, of the franchised business.³⁶⁰ In the latter jurisdictions, Emerson suggests that the franchisor is required to reimburse for goodwill even though the franchise statutes do not explicitly mention the term ‘goodwill’.³⁶¹

The franchise relationship statute of the four relationship states does not define the term ‘goodwill’. Case law also does not clarify this term. Despite the lack of definition, some legal practitioners offer helpful guidance. For example, Bundy and Einhorn point out that a franchisee may develop what is called ‘sweat equity’ or local and personal goodwill that reflects the going concern value of the franchised business. This local goodwill can be severable from the franchisor’s goodwill that is inherent in the licensed trademarks. In this case, Bundy and Einhorn suggest that courts may adopt the concept of

356 *Chem-Tek* (n 354) 128.

357 It should be noted that the repurchase requirements may vary in detail from state to state. For example, in Arkansas, California, Connecticut, Hawaii, Michigan, and Washington, the franchisor does not have to repurchase the personalized items that have no value to the franchisor. In Rhode Island and Wisconsin, the franchisor is required to repurchase only the inventories with a name, trademark, label, or other marks on the merchandise which identifies the franchisor. Moreover, in California, Hawaii, and Washington, the law explicitly allows the franchisor to offset against the amounts owed to the franchisee any amounts that the franchisee owed to the franchisor.

358 In other relationship states, such as Mississippi, the loss of goodwill may be considered the recoverable loss in light of the franchise statute. *See* MS ST, § 75-24-57. In this case, an injured franchisee may recover the loss of goodwill by seeking an award of statutory damages instead of enforcing the right to compensation for goodwill.

359 Hawaii: HI ST, § 482E-6(3) and Washington: WA ST, 19.100.180(i).

360 California: CA BUS & PROF, § 20035(a) and Illinois: IL ST CH 815, § 705/20.

361 Robert W Emerson, ‘Thanks for the Memories: Compensating Franchisee Goodwill after Franchise Termination’ (2018) 20 University of Pennsylvania Journal of Business Law 286, 294.

sweat equity or local goodwill when it comes to interpreting the term ‘goodwill’ under franchise relationship law.³⁶²

In compensating for the value of goodwill, a question may be raised about how the value of goodwill is evaluated.³⁶³ Answers to this question seem not to be settled. Some franchise relationship statutes offer a measure for evaluating the franchisee’s goodwill. For instance, in California and Washington, the relationship laws adopt the test of the fair market value. In measuring the fair market value, it is claimed that the appropriate measure is the value of the franchised business to disinterested hypothetical buyers and sellers, not to the parties in the litigation.³⁶⁴ Apart from the statutory measurement, some scholars suggest methods for estimating the value of goodwill. For example, Chisum suggests that franchise goodwill can be estimated by referring to the fair market value of the business or capitalizing the earnings of the franchise and then subtracting the value of specific assets of the business.³⁶⁵ Besides, Emerson and Carrington compile the possible standards for quantifying goodwill, including the financial performance model commonly called ‘the capitalization of excess earnings’. This formula suggests that the value of goodwill is calculated mathematically by what the buyer pays the seller minus the value of the net assets.³⁶⁶

– *Triggering events*

At a glance, there is no uniformity concerning the circumstances that would permit the franchisee to exercise the right to repurchase and the right to reimburse for goodwill. Thus, these triggering events may vary from state to state.

In the case of repurchase, the law of Arkansas provides that the franchisor is required to repurchase the franchisee’s materials only in the case of wrongful termination. In other words, the franchisor will be liable only when the termination has been made without good cause.³⁶⁷ Conversely, in Connecticut, Hawaii, Rhode Island, and Wisconsin, the franchisor must repurchase the franchisee’s assets upon the termination of a franchise agreement, regardless

362 Bundy and Einhorn (n 30) 216.

363 Weldon and Micklich, (n 336) 597.

364 Nicole Liguouri Micklich, Michael W Lynch, and Ingrid C Festin, ‘The Continuing Evolution of Franchise Valuation: Expanding Traditional Methods’ (2013) 32 Franchise Law Journal 223, 230-31.

365 Donald S Chisum, ‘State Regulation of Franchising: The Washington Experience’ (1973) 48 Washington Law Review 291, 377.

366 Robert W Emerson and Charlie C Carrington, ‘Devising a royalty structure that fairly compensates a franchisee for its contribution to franchise goodwill’ (2020) 14(2) Virginia Law & Business Review 279, 297-302.

367 *Premier Outdoors El Dorado LLC v Yamaha Motor Corporation USA* 2012 WL 12537468 (WD Ark, 2012) 2.

of whether the termination is made lawfully.³⁶⁸ In California, the franchisor is required to repurchase upon the lawful termination or non-renewal of a franchise.

In the case of compensation for goodwill, the triggering events differ among the states. In California, the franchisor is required to compensate the franchisee for the value of the franchised business in the event of wrongful termination and non-renewal.³⁶⁹ In Hawaii, the franchisor must compensate the franchisee for the loss of goodwill in case the franchisor refuses to renew a franchise for the purpose of converting the franchisee's business to one owned and operated by the franchisor. In contrast, in Washington and Illinois, it will be a violation of the laws if the franchisor refuses to renew a franchise without fairly compensating for the value of goodwill or franchised business of the franchisee.³⁷⁰ Unlike the law of California and Hawaii, there is no requirement concerning the franchisor's unlawful conduct under the law of Washington and Illinois.

5.5.3.6 Conclusions

In the USA, potential private law remedies for an aggrieved franchisee are mainly common contract law remedies. In contract law, an aggrieved franchisee may seek specific performance and injunctions to enforce the franchisor's performance and forbearance, claim damages, and rescind or terminate a franchise contract. However, it is vital for the franchisee to prove that the franchisor has substantially breached a franchise contract when seeking contract law remedies. In the relationship states, the franchisee may bring an action against the franchisor for civil law remedies provided by franchise relationship law. These remedies include specific performance and injunctions, and damages. In seeking statutory remedies, the franchisee has to demonstrate that the franchisor violates the relationship law rules. Additionally, some franchise relationship law establishes auxiliary remedies that permit the franchisee to require the franchisor to repurchase some tangible properties and compensate for the franchisee's local goodwill upon the franchisor's non-renewal and termination of a franchise contract.

³⁶⁸ Bundy and Einhorn (n 30) 213.

³⁶⁹ For example, the franchisor is accountable for the value of the franchised business if it fails to provide the franchisee with written notice of termination required by the California Franchise Relations Act. See *Tikiz Franchising LLC v Piddington* 2017 WL 8780761 (SD Fla, 2017) 8.

³⁷⁰ The statute makes an exception to the compensation of goodwill. That is, the franchisor does not have to make the compensation if the franchisor gives one-year notice of non-renewal to the franchisee, and the franchisor agrees in writing not to enforce any non-compete covenants.

5.5.4 Australia

5.5.4.1 Introduction

An aggrieved franchisee may seek the following private law remedies under common contract law and the Competition and Consumer Act 2010 (CCA): the enforcement of performance, monetary compensation, and cancellation of a franchise contract. This section will examine the common law and specific law rules governing the three remedies in subsections 5.5.4.2, 5.5.4.3, and 5.5.4.4, respectively. A franchise agreement may provide the franchisee with the protection of unsold stocks and the value of goodwill to some extent. The extent to which the terms of a franchise agreement protect the franchisee's properties will be explored in subsection 5.5.4.5. In the end, conclusions about the remedial system under the Australian legal system will be made in subsection 5.5.4.6.

5.5.4.2 Enforcement of performance

– *Specific performance and injunctions in common law*

In common law, an aggrieved franchisee may seek an order of specific performance and injunctions for breach of contract. In this respect, the claimant franchisee must demonstrate the franchisor's non-compliance with an obligation under a franchise agreement. In practice, the court decisions in the case *RPR Maintenance v Marmax Investments* may offer an example in that the franchisee successfully obtains an issuance of specific performance and injunctive relief under common law.³⁷¹ The franchisee alleged that the franchisor breached the terms of a franchise agreement by purporting to terminate the franchise contract. The franchisee also claimed that it had exercised an option to renew the contract term, but the franchisor refused to renew.

In response to the franchisee's claims, the Federal Court of Australia concluded that, first of all, the franchisor did not validly terminate the franchise agreement due to failure to comply with the formality required by the contract. In this case, the franchisor did not give reasons for the termination decision, including the allegation of the franchisee's breach of a contract. Secondly, the court found that the franchise agreement at issue granted the franchisee an option to renew the contract for a further five-year period. Moreover, the franchisee had validly exercised the option to renew. Based on these findings, the court decided to grant a permanent injunction prohibiting the franchisor from taking any step to act upon the purported, invalid termination. The court

³⁷¹ *RPR Maintenance I* (n 42); *RPR Maintenance Pty Ltd v Marmax Investments Pty Ltd* [2014] FCA 514 (*RPR Maintenance II*).

decreed specific performance forcing the franchisor to conclude a franchise contract with the franchisee for a five-year term.³⁷²

Specific performance and injunctions are equitable remedies under common law rules. For example, a court may not order specific performance or issue an injunction if a remedy of damages is considered a suitable remedy.³⁷³ In *W Hoy v WTH*, Barker J dismissed the franchisee's application for injunctive relief, reasoning that to force the parties to stay in a commercial relationship was unwise if damages would provide an adequate remedy for the applicant franchisee.³⁷⁴ Courts may not grant an order of injunctive relief if the plaintiff franchisee also breached a franchise agreement. In common law, a breach by a claimant is a relevant consideration when granting equitable remedies.³⁷⁵

– *Injunctions under the competition and consumer law*

An aggrieved franchisee may seek injunctive relief under section 80 of the CCA to compel the franchisor's action or omission.³⁷⁶ For example, in *Aura Enterprises v Frontline Retail*, the court found that the franchisor could not terminate a franchise agreement because the franchisor did not provide the franchisee with a valid notice of termination for the breach. The court found that the franchisor did not sufficiently specify the obligation claimed to have been breached by the franchisee in the notice. Thus, the court held that an injunction could be awarded to restrain the franchisor from terminating the franchise contract.³⁷⁷

It should be noted that the franchisor's violation of the Franchising Code of Conduct is a basis for an order of injunctions under the CCA.³⁷⁸ In seeking the remedy, the franchisee must prove that the franchisor has engaged in actual or anticipated contravention of the Code.³⁷⁹ Thus, the franchisee may not succeed in claiming the remedy under the CCA if the franchisee fails to show

372 *RPR Maintenance I*, *ibid* [243] – [250], [262] – [263]; *RPR Maintenance II*, *ibid* [24] – [26].

373 *D'Arling One Pty Ltd v Eagle Boys Dial-A-Pizza Pty Ltd* [2009] NSWSC 570 [9].

374 *W Hoy* (n 208) [107].

375 *National Security Training Academy (GC)* (n 207) [33].

376 The injunctive relief sought under section 80 can be mandatory and prohibitory. See Alex Bruce, *Australian Competition Law* (4th edn, LexisNexis 2021) 331.

377 *Aura Enterprises* (n 202) 435. It should be mentioned that only the franchisor's contractually valid termination of a franchise can be considered in contravention of the CCA. In other words, if the franchisor's purported termination is ineffective, there will be no question regarding the contravention of the statute. See *National Security Training Academy (GC)* (n 207) [32].

378 As examined in this chapter, transfer, termination, and non-renewal of a franchise agreement are regulated by provisions of the Code to some extent. See subsections 5.2.4.2, 5.3.4.2, and 5.4.4.2.

379 In requesting an injunction, the claimant franchisee does not have to constitute the link between the franchisor's breaching conduct and loss or damage suffered. See Bruce (n 376) 331.

the franchisor's contravening conduct. For example, the court in *Masterclass Enterprises v Bedshed Franchisors (WA)* held that the franchisee could not prove that the franchisor acted unreasonably in withholding consent to a proposed transfer. Accordingly, the claim for a mandatory injunction compelling the franchisor to approve the transfer failed.³⁸⁰

5.5.4.3 Monetary compensation

An aggrieved franchisee may seek monetary compensation in common law and under the Competition and Consumer Act 2010 (CCA). This subsection will examine the requirements for recovering common law and statutory damages and the principles governing the measure of damages.

– Requirements for recovery of damages

An aggrieved franchisee may seek an award of damages in contract. Thus, the franchisor's breach of contract is a precondition for an award of damages.³⁸¹ In other words, courts will not award damages if the franchisee cannot establish the franchisor's breach of a franchise contract. In practice, the franchisee may plead that the franchisor has engaged in certain breaching conduct, such as wrongful termination of a franchise agreement. For example, in *Bravale v Whistle & Co (1979)*, the franchisee claimed damages, alleging that the franchisor breached a franchise contract by way of repudiation. In this case, the court found that the franchisor's purported termination under the contract was not justified and wrongful because of the lack of the franchisee's substantial breach. Thus, the franchisor's wrongful termination was held to be a repudiation of the contract that entitles the franchisee to recover damages.³⁸²

The franchisee may also claim damages under the CCA. In claiming statutory damages, the franchisee must demonstrate that the franchisor has violated provisions of the Franchising Code of Conduct.³⁸³ In the context of transfer, for example, clause 25(2) of the Code requires a franchisor not to unreasonably withhold consent to transfer of a franchise agreement proposed by its franchisees. In this respect, the transferring franchisee may claim that the franchisor unreasonably withheld its consent to the proposed transfer, although the proposed transferee meets the financial obligations that the

380 *Masterclass Enterprises* (n 46) [2] and [102] – [122].

381 In Australian contract law, breach of contract includes failure to perform and anticipatory breach. See J W Carter, *Contract Law in Australia* (7th edn, LexisNexis Butterworths 2018) 795.

382 *Bravale Pty Ltd v Whistle & Co (1979) Pty Ltd* [2015] QDC 174 [37] – [65] and [74].

383 The CCA, s. 82(1), in conjunction with s. 51 ACB.

transferee would have under the franchise contract.³⁸⁴ No court precedent has been established yet.

In claiming damages, an aggrieved franchisee must prove that it has suffered loss or damage.³⁸⁵ In common law, the loss is recoverable if the loss flows naturally from the breach or should have been contemplated by the parties.³⁸⁶ For example, the franchisee may recover the lost profits caused by the franchisor's breach of a franchise contract.³⁸⁷ Furthermore, the loss recoverable under the CCA must be actual. The loss is actual if the loss is caused by contravening conduct. In other words, the loss is caused by the contravening conduct if the loss would not have been suffered if the relevant conduct had not been engaged in.³⁸⁸ For example, the court in *Bravale v Whistle* concluded that damages for wrongful termination of a franchise contract covered the loss of the business value.³⁸⁹

Additionally, an aggrieved franchisee must show a causal connection between the loss suffered and the franchisor's unlawful conduct. In common law, the issue of causation is a matter of fact. In *March v Stramare*, the court contended that whether the causation was established was to be decided on a common-sense basis. Furthermore, the court mentioned that the 'but for' test was not a sole concept for the determination of the existence of causation.³⁹⁰ This common-sense concept is recognized when it comes to determining the causal link under the CCA too. According to the court in *Wardley Australia v Western Australia*, the common-sense approach will be applied to a claim for damages under section 82 of the CCA unless this notion is supplemented or modified impliedly or expressly by the provisions of the law.³⁹¹

– *Principles governing a measure of damages*

Damages are compensatory; they are principally awarded to compensate for loss or damage suffered by an injured party.³⁹² In this case, courts cannot award exemplary damages for breach of contract to penalize the respondent

384 This withholding could be regarded as unreasonable in light of paragraph (a) of clause 25(3).

385 *Marks v GIO Australia Holdings Ltd* [1998] 196 CLR 494 [9].

386 *Cripps v G & M Dawson Pty Ltd* [2006] NSWCA 81 [35].

387 *Darmody v National Centre Automotive* [2003] FMCA 358 at [c].

388 *Wardley Australia Ltd v Western Australia* (1992) 175 CLR 514, 534.

389 In measuring the value of the business, the court utilized the approach of market value. That is, damages would be measured by reference to the price of the business that will be achieved between a willing seller and a willing buyer in the market. See *Bravale* (n 382) [79].

390 *March v Stramare (E & M H) Pty Ltd* (1991) 171 CLR 506 [17] – [28].

391 *Wardley Australia* (n 388) 525.

392 *Marks* (n 385) [9].

even though the breach is committed willfully or maliciously.³⁹³ Likewise, an award of punitive damages is not available under section 82 of the CCA. In *Musca v Astle Corp.*, the court noted that exemplary damages were not awarded to compensate for losses. Thus, exemplary damages could not be recovered under section 82 of the Trade Practices Act 1974.³⁹⁴ Therefore, a claimant franchisee could only recover a sum that would represent the loss or damage that the franchisee had suffered because of the franchisor's wrongful conduct.³⁹⁵

The rules of common law and the CCA differ when it comes to assessing damages. In common law, the principle governing the assessment of damages for breach of contract has been settled; that is to say, a sum will be awarded to put the injured party in the same position as he or she would have been in had the contract been performed.³⁹⁶ Under this assessment rule, an injured party would recover damages for economic interests, including expectation and reliance losses.³⁹⁷ In *Marks v GIO Australia Holdings*, the judges provided that the recoverable loss in contract law could be signified and covered both the expectation and reliance loss.³⁹⁸

In contrast, section 82 of the CCA does not constitute any standard for assessing damages. It is said that courts may find a proper measure for statutory damages.³⁹⁹ Thus, an approach in measuring damages under the CCA may vary from case to case. For instance, in *Marks v GIO Australia Holdings*, the members of the court concluded that an action for damages section 82 was not confined by analogy with an action in contract law.⁴⁰⁰ In particular, Gaudron J suggested that it was misleading to think of expectation or reliance loss in the context of section 82. Thus, it was concluded that an injured party could recover damages under section 82 insofar as a causal link between loss or

393 *Harris v Digital Pulse Pty Ltd* [2003] NSWCA 10 [294], citing *Gray v Motor Accident Commission* (1998) 196 CLR 1 [13].

394 *Musca v Astle Corp Pty Ltd* (1988) FCA 114 [66]. It should be mentioned that section 82 of the Trade Practices Act 1974 is a predecessor of section 82 of the CCA. Thus, this precedent could be relied upon when it comes to applying section 82 of the CCA.

395 *Manwelland Pty Ltd v Dames & Moore Pty Ltd* [2001] QCA 436 [42].

396 See eg *Darmody* (n 387) 358 [a]; *Roluke Pty Ltd v Lamaro Consultants Pty Ltd* [2008] NSWCA 323 [78].

397 Carter (n 381) 800.

398 *Marks* (n 385) [1] – [26] per Gaudron J, and [27] – [42] per McHugh, Hayne, and Callinan JJ.

399 Arlen Dukes, *Corones' Competition Law in Australia* (7th edn, Thomson Reuters, 2018) at [18.230]. A great deal of case law concerning the causation is limited to the cases of contravention of provisions relating to misleading and deceptive conduct. In any case, it is viewed that those court decisions may provide some useful guidelines in other contravention cases. See Caron Beaton-Wells, 'Private Enforcement of Competition Law in Australia – Inching Forwards' (2016) 39 Melbourne University Law Review 681, 724.

400 *Marks* (n 385) [17] per Gaudron J, and [38] per McHugh, Hayne, and Callinan JJ.

damage and contravening conduct was established.⁴⁰¹ This principle may be applied in the franchising context when it comes to assessing damages for violation of the Franchising Code of Conduct.

5.5.4.4 Cancellation of a contract

Sometimes, a franchisee may attempt to transfer a franchise to exit a franchise relationship with a franchisor.⁴⁰² However, the franchisor may object to the proposed transfer by refusing to consent to the transfer. In this case, the franchisee can do nothing but cancel a franchise contract. In cancelling a franchise contract, the franchisee may have recourse to the terms of a franchise contract and the rules of contract law for the right to terminate the agreement. The franchisee may have to seek rescission of a franchise contract under the CCA.

– Contractual right to terminate

An aggrieved franchisee may discharge a franchise relationship by exercising a contractual right to terminate. In some but few cases, the agreement's termination provisions may explicitly provide the franchisee with the right to terminate the contract. For example, in *Freier v Australian Postal Corporation (No 2)*, the franchisee was entitled to terminate a franchise agreement without cause by giving the franchisor ninety-day prior written notice.⁴⁰³ It should be noted that the franchise agreement at issue was concluded for an indefinite period. Thus, it is common for the parties to terminate the agreement upon notice.

– Common law right to terminate

In most cases, a franchise agreement will not provide the franchisee with the right to terminate.⁴⁰⁴ Despite the absence of the right, an aggrieved franchisee may terminate a franchise contract through common law rules.

⁴⁰¹ Moreover, the court in *HTW Valuers v Astonland* also noted that section 82 permits a wide array of approaches to the assessment of damages insofar as justice is required. See *HTW Valuers (Central Qld) Pty Ltd v Astonland Pty Ltd* 217 CLR 640 [65].

⁴⁰² According to the 2018 Inquiry conducted by the Parliament Joint Committee on Corporations and Financial Services, the franchisee may employ a transfer of a franchise to leave the franchise system. See Parliamentary Joint Committee on Corporations and Financial Services (n 238) at [11.19].

⁴⁰³ *Freier* (n 217) [4].

⁴⁰⁴ For instance, in *Mr Rental Australia v IRD Services*, only the franchisor holds the right to terminate a franchise agreement. See *Mr Rental Australia Pty Ltd v IRD Services Pty Ltd* [2016] NSWSC 700 at Schedule.

(1) *Franchise contract for an indefinite period*

An aggrieved franchisee may terminate a franchise contract for an indefinite period upon reasonable notice. In *Crawford Fitting v Sydney Valve and Fittings*, McHugh JA provided that it could be implied that an indefinite commercial contract was terminable upon reasonable notice.⁴⁰⁵ Since a franchise agreement is a commercial-type contract, the franchisee could argue that an indefinite franchise contract can be terminated by giving the franchisor reasonable notice of termination. According to McHugh JA, it could be implied that a perpetual contract should continue for a reasonable period before the agreement was terminable. In this case, the franchisee may have to allow the franchisor some time to recoup any expenditure incurred before exercising the right to terminate.

(2) *Franchise contract for a definite period*

An aggrieved franchisee may terminate a franchise contract with a fixed term for the following three grounds.⁴⁰⁶ First, the franchisee may terminate the agreement for the franchisor's breach of a condition or an essential term, any breach of which gives rise to the right to terminate without inquiry into any question of loss and the extent of the loss caused by the breach. Second, the franchisee may terminate the agreement for a serious breach of an intermediate term. In this case, courts shall determine the seriousness of a breach; that is to say, the actual and foreseeable results of the breach and the effect of the breach on the contract as a whole.⁴⁰⁷ Third, the franchisee may terminate a franchise agreement in the case of the franchisor's repudiation or renunciation of the contract.⁴⁰⁸

– *Statutory rescission*

From a regulatory standpoint, an aggrieved franchisee may seek a remedial order under section 87(1A), in conjunction with section 87(2)(a), of the CCA

⁴⁰⁵ *Crawford Fitting* (n 215).

⁴⁰⁶ *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] 233 CLR 115 [43] – [45].

⁴⁰⁷ Carter (n 381) 672. See also *VIP Home Services (NSW) Pty Ltd v Swan* [2011] 110 SASR 157 [45] – [47].

⁴⁰⁸ Concerning the third ground for termination, the franchisee needs to establish the franchisor's unwillingness or inability to perform to constitute the franchisor's repudiation. That is, the franchisee must plead that the franchisor's conduct unequivocally conveys to the franchisee that the franchisor evinces its intention no longer to be bound by the franchise agreement as a whole, or fundamental obligations, under the contract. See eg *Bodycorp Repairers Pty Ltd v Maisano (No 8)* [2013] VSC 472 [110] – [114]; *Mr Rental Australia* (n 404) [111]. In practice, the franchisor's purportedly unlawful termination may constitute a renunciation of a franchise contract because the franchisor intends to abandon a franchise relationship and is not going to perform all the outstanding duties under the agreement. See *Otrava Pty Ltd v Mail Boxes Etc (Australia) Pty Ltd* [2004] NSWSC 1066 [103].

to invalidate a franchise contract.⁴⁰⁹ According to paragraph (2) of section 87, a court has authority to order a wide range of orders, including a rescission order that declares the whole or any part of a contract to be void.⁴¹⁰ In seeking the court's declaration, the franchisee has to demonstrate the franchisor's violation of provisions of the Franchising Code of Conduct. For example, the franchisee may plead that the franchisor withheld consent to a transfer in contravention of clause 25(2) of the Code. This violation will, in turn, be considered a violation of section 51ACB of Division 2 of Part IVB of the CCA.

The franchisee also has to demonstrate its actual or anticipated suffering of loss or damage caused by the franchisor's contravening conduct.⁴¹¹ This actual or anticipated loss will provide a ground for issuing a remedial order. According to section 87(1A)(c), the court shall consider that an order concerned will compensate the claimant in whole or in part for the loss or damage or will prevent or reduce the loss or damage. In this case, it is said that the court can only issue orders under section 87 insofar as the orders will compensate, prevent, or reduce the identified or future loss or damage.⁴¹² That consideration equally applies to the issuance of the declaration of avoidance under section 87(2)(a). Therefore, the court can declare the franchise contract to be void in whole or in part only if the declaration will compensate, prevent, or reduce the franchisee's loss or damage.⁴¹³

– *Effects of termination and rescission*

The franchisee's termination and rescission will discharge a franchise relationship. The termination under a franchise contract and common law and the rescission under the CCA differ in terms of retrospective effects. In the case of termination, the parties' duty to perform obligations will be discharged in

409 Alternatively, a franchisee may terminate a franchise agreement in a cooling-off period. According to clause 26(1) of the Code, the franchisee may terminate a franchise contract within 14 days after entering into the contract. In practice, however, the franchisee's right to terminate would expire since transferring a franchise contract may not be proposed within the cooling-off period. In other words, rarely does a franchisee transfer its franchise in the first two weeks after the conclusion of the contract.

410 In avoiding a contract, the court may, if it thinks fit, order that the contract is void *ab initio* or at all times on and after the specific date. See The CCA, s. 87(2)(a).

411 The CCA, s. 87(1).

412 See eg *Deane v Brian Hickey Invention Research Pty Ltd* [1988] ATPR 49,608 [17]; *Rafferty and Another v Madgwicks* [2012] 203 FCR 1 [225].

413 In ordering rescission under section 87, the court may consider some equitable principles as guidelines for the exercise of its discretion. However, it is said that those equities are not necessarily exclusive. For example, in *Munchies Management v Belperio*, the court concluded that the presence or absence of fraudulent conduct may be vital when it comes to ordering rescission at common law. Those matters may not be significant in the exercise of the power to order an appropriate remedy under section 87. See *Munchies Management Pty Ltd v Belperio* [1988] 58 FCR 274.

the future.⁴¹⁴ In this case, an executed obligation will not be affected. Furthermore, some accrued rights, such as the right to damages, will survive the termination and will be enforceable.⁴¹⁵ Conversely, in rescinding a franchise agreement under the CCA, the court may, if it thinks fit, order a franchise contract to be void *ab initio*.⁴¹⁶ In this respect, the status quo ante of the parties will entirely be restored. In other words, the parties will be put into the position that they occupied before the agreement was concluded. As a result of rescission, any performed obligations will be undone.

5.5.4.5 Specific remedies

From a statutory standpoint, an aggrieved franchisee does not have the right to repurchase and the right to compensation for the value of goodwill.⁴¹⁷ Neither the Code nor the CCA provides the franchisee with these additional rights to special relief when a franchise relationship is terminated. Nevertheless, a franchise contract may confer on the franchisee the right to special remedies as follows.

– Option to repurchase

Firstly, a franchise contract may include a so-called ‘buy-back clause’, creating the franchisor’s option to repurchase.⁴¹⁸ For example, a franchise agreement may provide that, upon the termination of the agreement, the franchisor has an exclusive option to purchase from the franchisee machinery owned by the franchisee at a price agreed between the franchisor and the franchisee.⁴¹⁹ Under the contract, a franchisor may have an option to buy back all or some of the equipment and fittings after the termination of a franchise contract.⁴²⁰

414 Carter (n 381) 733; Des Butler and others, *Contract Law Case Book* (3rd edn, Oxford University Press 2018) 491.

415 Furthermore, a franchise contract may supplement the consequences of common law rules. For example, the franchisee must pay all monies, including interest owed to the franchisor, within seven days of the effective date of termination. See *Mr Rental Australia* (n 404) at Schedule: Mr Rental Franchise Agreement.

416 The CCA, s. 87(2)(a).

417 In 2019, the parliamentary joint committee recommended that there should be an examination of whether the Franchising Code of Conduct should be amended to include a requirement for a franchise agreement to set out some end-of-term arrangements for franchisee goodwill. According to the committee, one of these arrangements is the financial consideration to which the franchisee is entitled when a franchise contract expires, and the contract is not renewed. See Parliamentary Joint Committee on Corporations and Financial Services (n 238) at [12.56].

418 As the term suggests, the option to repurchase is ordinarily a matter of the franchisor’s right or discretion. It would imply that the franchisee cannot enforce the repurchase of the items if the franchisor refuses to exercise the option.

419 *Spanline Weatherstrong Building Systems Pty Ltd v Tabellz Pty Ltd* [2013] FCA 1019 [182].

420 *Cafe2U Pty Ltd v Bishambu Pty Ltd* [2013] FCA 191 [60].

Nevertheless, this buy-back clause does not provide the franchisee with the right to compel the franchisor's repurchase. In other words, the franchisee's unsold or unused items can be re-sold to the franchisor, provided that the franchisor has exercised an option to repurchase.

– Compensation for the value of goodwill

Secondly, a franchise contract may also deal with the compensation of the franchisee's goodwill. In practice, a franchise contract may contain terms addressing the franchisee's opportunity to get compensation for goodwill. For instance, in *Blockbuster Australia v Karioi*, the franchise agreement at issue provided that a franchisor had the option to purchase the franchisee's goodwill attached to the franchised operation upon the expiration of a franchise contract.⁴²¹ According to the court, the franchisee could get reimbursement for the value of goodwill only if the franchisor exercised its option. In other words, the franchisor had no obligation under the contract to indemnify for goodwill when the franchise agreement expired.⁴²² In any case, provided that a franchisee agreement entitles the franchisee to compensation for goodwill, two questions arise: what does goodwill mean, and which is the franchisee's goodwill? In general, it could be said that the terms of a franchise agreement can provide the meaning and scope of the franchisee's goodwill. In the absence of the terms, a resort to defining goodwill should be made to case law and legislature.

Concerning the legal meaning of goodwill, Gangemi provided that Australian courts and legislation have not provided the exact meaning of the term 'goodwill'. Despite this ambiguity, Gangemi claimed that the definition of goodwill is associated with the three concepts of goodwill: the custom concept, the privilege concept, and the excess value concept. These three concepts influence defining the term by Australian courts, particularly the High Court of Australia in the influential case *Commissioner of Taxation v Murry*.⁴²³ In *Murry*, the High Court identified goodwill in terms of nature, sources, and value.⁴²⁴ First, goodwill was regarded as property because it was the valuable right or privilege to conduct business in substantially the same manner and by substantially the same means that have attracted custom to it. Second, goodwill might be generated from a variety of sources, including manufacturing and distribution techniques, the efficient use of the assets of a business, superior management practice, and good industrial relations with employees.

421 In this case, the court exemplified that franchisee's goodwill includes staff who have a particularly good reputation or relationship with customers of the business areas. See *Blockbuster Australia Pty Ltd v Karioi Pty Ltd* [2009] NSWSC 1089 [130].

422 Ibid [50] and [94].

423 Nicholas John Joseph Gangemi, 'Is Goodwill Property?' (DPhil thesis, UNSW Business School 2019) 12-14.

424 *Federal Commissioner of Taxation v Murry* [1998] HCA 42; 193 CLR 605.

Third, the value of goodwill was tied to the fortunes of the business, which varied with the profitability of the business and the value of the other identifiable assets.⁴²⁵ According to Gangemi, the High Court placed the privilege concept at the center of the idea of goodwill, putting aside the excess value concept. However, the privilege concept remained to be qualified by the custom concept.⁴²⁶ This High Court's definition has been followed by later cases such as the most recent case *Placer Dome*.⁴²⁷ This definition is also relevant in defining goodwill in the franchising context.⁴²⁸

When it comes to demarcating the ownership of goodwill, Gangemi contended that a franchisee and a franchisor conduct different businesses. Thus, the franchisee might develop its business's value by building up the business's reputation among its customers. In this respect, the franchisee will lose the business's value, amounting to the business's goodwill, if a franchise relationship is terminated.⁴²⁹ If turning to case law, some court decisions mention the franchisee's goodwill. For example, the court in *Karioi* provided that the franchisee's goodwill is said to include staff who has a particularly good reputation or relationship with customers of the business areas.⁴³⁰ This court's viewpoint seems similar to Gangemi's in that the franchisee may own separate goodwill by establishing a good reputation for the business in the customers' eyes.

5.5.4.6 Conclusions

The remedial system in Australia is twofold; common contract law and the CCA are primary legal frameworks enabling an aggrieved franchisee to enforce the franchisor's action and inaction, claim damages, and cancel a franchise contract. Under the remedial regime, the basis for seeking the remedies differs. On the one hand, when seeking the remedies in contract law, the franchisee typically has to prove the franchisor's breach of a franchise contract. On the other hand, the franchisee must demonstrate the franchisor's violation of the provisions of the Franchising Code of Conduct when resorting to the remedies under the CCA. Nevertheless, these two legal frameworks are similar in that they do not provide rules protecting a franchisee's specific properties, such as unsold stocks and goodwill, upon the cessation of a franchise relationship. In this case, the franchisee may have to resort to a franchise agreement for protection. Contracting practices show that the franchise contract's terms may

425 Ibid [23], [25], and [49].

426 Gangemi (n 423) 15.

427 *Commissioner of State Revenue v Placer Dome Inc* [2018] HCA 59.

428 *Gloria Jean's Coffees International Pty Ltd and Another v Chief Commissioner of State Revenue* [2008] 74 ATR 579 [44] – [48].

429 Gangemi (n 423) 222-26.

430 *Blockbuster Australia* (n 421) [130].

confer on the franchisor the right to decide whether to repurchase the franchisee's unused items or compensate for the value of the franchisee's goodwill.

5.5.5 Comparative analysis

5.5.5.1 Introduction

The DCFR, the USA, and Australia have the remedial regimes that permit an aggrieved franchisee to compel the franchisor's performance, claim monetary compensation, and cancel a franchise contract when a franchisor violates the regulation of the three exit issues examined in this chapter. Upon the cessation of a franchise relationship, the chosen legal systems demonstrate that there are some remedial mechanisms that protect the franchisee's tangible and intangible assets. This section will compare, contrast, and discuss the selected legal systems' remedial systems governing the enforcement of performance, monetary compensation, termination of a franchise contract, and other specific remedies in subsection 5.5.5.2. Concluding remarks and key recommendations will be provided in subsection 5.5.5.3.

5.5.5.2 Comparison and discussion

– Enforcement of performance

(1) Similarity

The DCFR, the USA, and Australia are similar in that an aggrieved franchisee may resort to a remedy of enforcement under contract law.⁴³¹ When seeking the enforcement relief in contract under the chosen legal systems, it is common for the franchisee to prove the franchisor's non-compliance with a franchise contract.⁴³² That is, the franchisee needs to plead that the terms of a franchise agreement obligate the franchisor to perform an obligation, and the franchisor fails to perform accordingly. For example, in the renewal context, the franchisee may demonstrate that the terms of a franchise agreement require the franchisor to renew the agreement for another successive term when the agreement's term expires. In this case, the selected legal systems would permit the franchisee to enforce the franchisor's renewal of the term of a franchise agree-

⁴³¹ The phrase 'remedy of enforcement' will be used as a generic term for various types of private law remedies that aim to enforce the performance *in specie* of the debtor or the promisor under the DCFR, and the US and Australian legal systems. Thus, the enforcement remedy intends to cover the right to enforce performance under the DCFR and an equitable remedy of specific performance and injunctions available in the USA and Australia.

⁴³² See subsections 5.5.2.2, 5.5.3.2, and 5.5.4.2.

ment if the franchisor refuses to renew in accordance with the renewal provisions.

(2) *Difference*

The USA and Australia differ from the DCFR in terms of the nature of the remedy of enforcement. In the US and Australian legal systems, the enforcement remedy is a remedy in equity; hence, the issuance of the remedy will depend upon a courts' discretion. A grant of the equitable relief will be constrained by some restrictive rules and principles, such as the inadequacy of damages. In this case, courts will consider whether an award of damages is an adequate remedy under the circumstances of the case. Unlike the USA and Australia, the remedy of enforcement under the DCFR is a matter of right. An aggrieved franchisee is primarily entitled to enforcing the franchisor's performance, regardless of the inadequacy of a remedy of damages. In this case, the franchisor has to prove that the franchisee's right to specific performance is excluded.

The USA and Australia differ from the DCFR in that an aggrieved franchisee may resort to the enforcement of the franchisor's performance and forbearance under specific statutes.⁴³³ In America, the relationship states regulate the transfer, non-renewal, and termination of a franchise contract through franchise relationship laws. In some relationship states, the franchisor's contravention of the franchise relationship law rules provides a basis for an aggrieved franchisee to seek some civil law remedies, including specific performance and injunctive relief. In Australia, the Franchising Code of Conduct regulates some aspects of these three exit issues. Thus, the franchisor's violation of the Code will permit the franchisee to resort to private law remedies under the Competition and Consumer Act 2010. Among other remedies, the franchisee may seek injunctions to compel the franchisor's performance.

(3) *Discussion*

In my view, an enforcement remedy, which includes enforcement of specific performance and injunctions, may be appealing to an aggrieved franchisee in terms of enforcing the franchisor's compliance with the regulation of the three exit issues. In the case of transfer, the franchisor may be required not to withhold consent to a transfer unreasonably. In this case, the enforcement remedy would compel the franchisor to follow the transfer regulation by consenting to the franchisee's proposed transfer. In practice, it is not unusual as some courts allow the franchisee to enforce a transfer if the franchisor withheld consent to the transfer unreasonably.⁴³⁴ The remedy of enforcement would uphold a franchise relationship when a franchisee needs.⁴³⁵ For

⁴³³ See subsections 5.5.3.2 and 5.5.4.2.

⁴³⁴ *VW Credit* (n 17) 341–42.

⁴³⁵ Curtis A Loveland, 'Franchise Regulation: Ohio Considers Legislation to Protect the Franchisee' (1972) 33 *Ohio State Law Journal* 643, 671–72.

example, the termination regulation may prevent the franchisor from wrongfully terminating a franchise contract. In this case, the franchisee may seek a remedy of enforcement to bar the franchisor's potential breach of the rules regulating the termination of a franchise.⁴³⁶

As can be seen from the comparison, the source of the remedy of enforcement is basically twofold.

First, an aggrieved franchisee may seek an order of enforcement of performance in contract law. Under contract law rules, the basis for issuing a remedy of enforcement is ordinarily the non-performance of an obligation. Thus, in seeking the remedy, it is strategically vital that a claimant franchisee establishes the franchisor's non-performance of an obligation under a franchise agreement; that is to say, the franchisor's failure to perform in accordance with the express and implied terms of a franchise contract.⁴³⁷ For example, in the case of the franchisor's withholding consent to a transfer, the franchisee may allege that the franchisor breaches a franchise contract by unreasonably withholding consent to a transfer.⁴³⁸ In this case, the franchisee needs to prove that the franchisor is required by the agreement not to withhold consent to the transfer in an unreasonable manner.

An aggrieved franchisee may face several contractual or legal constraints that would make it unfeasible to compel the franchisor's performance in kind. In contracting practice, a franchisor may hold some corresponding rights or discretion regarding the three exit issues. For instance, the franchisee may not enforce the franchisor to consent to a transfer because the franchisor reserves a right of first refusal under a franchise agreement.⁴³⁹ In this case, the franchisor's exercise of the right would shield the franchisor from any liability, including the contractual liability for failure to effectuate the proposed transfer. To overcome this contractual constraint, the franchisee may have to negotiate for favorable terms so that the franchisee can guarantee that it can resort to a remedy of enforcement under contract law rules. In reality, it might be impracticable for a franchisee to do so if the franchisee has no equal bargaining power at the time of the negotiation with the franchisor.

A claimant franchisee may not succeed in a lawsuit for a remedy of enforcement because of some legal limitations. In common law countries, such as the USA and Australia, the remedy of specific performance and injunctions is a substitutional and equitable remedy, which will be awarded at the court's discretion. In many cases, common law courts are unwilling to issue the

436 See eg *RPR Maintenance I* (n 42) [243] – [250], [262] – [263]; *RPR Maintenance II* (n 371) [24] – [26].

437 Ole Landa, 'Chapter 29: Non-performance (Breach) of Contracts' in Arthur S Hartkamp and others (eds), *Towards a European Civil Code* (Kluwer Law International 2011) 682.

438 *Gray v Toyota Motor Sales USA Inc* 806 F Supp2d 619 (EDNY, 2011) 623.

439 *Crivelli v General Motors Corp* 215 F3d 386 (CA3 (Pa), 2000) 389.

remedies in suits for breach of contract.⁴⁴⁰ For example, some courts would not order specific performance or injunctive relief if the remedy requires the court's ongoing supervision.⁴⁴¹ However, it would be more feasible to demand a remedy of enforcement in countries with civil codes. Taking the DCFR as an example, the right to enforce performance is regarded as an ordinary remedy. Thus, a resort to the enforcement of specific performance is a matter of right. Thus, upon the occurrence of the debtor's non-performance, courts will not have discretion in granting an order of performance for the creditor unless the debtor proves some exceptions under the law.⁴⁴²

Second, an aggrieved franchisee may resort to specific legislation for a statutory remedy of enforcement. However, legal systems may differ concerning legislative sources of the remedy of enforcement. The USA and Australia can be taken as illustrations in this respect. In America, the state franchise relationship statutes provide for a remedy of specific performance and injunctions. Conversely, in Australia, the Franchising Code of Conduct, which is a franchise-specific law, does not offer a remedial system from which an injured franchisee may seek civil law remedies. In this respect, the franchisee needs to resort to the remedies made available under the Competition and Consumer Act 2010. In both cases, the franchisee must demonstrate that the franchisor has violated the rules of franchise relationship law when seeking the court's order of enforcement of performance.

For uniformity's sake, I suggest that comprehensive franchise law contains the remedial regime, ensuring that an aggrieved franchisee can seek a remedy of enforcement in the event of the franchisor's contravention of the rules regulating transfer, non-renewal, and termination of a franchise contract. In this case, it would be crucial for comprehensive franchise law to provide determinative standards to help courts identify the franchisor's contravening conduct. For example, the courts should have clear criteria for determining whether the franchisor's withholding consent is unreasonable or whether the franchisor's purported termination is made wrongfully.⁴⁴³ The determinative criteria would help the courts in granting not only a remedy of enforcement but also other statutory remedies made available under franchise-specific law.

440 E Allan Farnsworth, *Farnsworth on Contracts* (Vol. III, 2nd edn, Aspen Publisher, Inc. 1998) 160; Carter (n 381) 924.

441 Adam Ship, 'Specific Performance of Franchise and Distribution Agreements in Canada' (2012) 39 *Advocates' Quarterly* 407, 410.

442 Bar and Clive (n 9) 829 – 30.

443 Examples of some determinative standards can be found in the proposal concerning the regulation of transfer. For instance, this chapter has proposed that comprehensive franchise law requires the franchisor not to withhold consent to a transfer without reasonable grounds. In this regard, the determinative standards for determining whether the franchisor unreasonably withheld its consent include the unacceptability of a prospective franchisee. See subsection 5.2.5.2.

– *Monetary compensation*

(1) *Similarity*

The DCFR, the USA, and Australia similarly permit an injured franchisee to recover monetary compensation or damages under general contract law rules. Under the chosen legal systems, the preconditions for seeking an award of damages are relatively comparable. That is, the franchisee needs to demonstrate the existence of an obligation under a franchise agreement and the franchisor's non-performance of the obligation. The contract law of the selected legal systems requires the franchisee to prove the loss or damage sustained by the franchisee and a causal connection between the franchisor's non-performance and the loss or damage suffered.

Additionally, under the DCFR, the US, and Australian legal systems, the character of contract law damages is similar. In the chosen legal systems, damages are of a compensatory character; they aim to compensate for the loss or damage sustained by an injured party. In this respect, the selected legal systems seem to accept that an injured franchisee cannot claim punitive damages to punish the franchisor for breach of a franchise contract. Besides, the DCFR, the USA, and Australia adopt an identical standard for assessing contract law damages. In the selected legal systems, a sum is awarded to put an injured party as nearly as possible into the position in which the party would have been had the contract been performed. In this case, the injured franchisee may claim damages for expectation loss, such as the loss of income or profits.

(2) *Difference*

The USA and Australia differ from the DCFR in that an injured franchisee may claim damages against the franchisor under specific legislation. In the USA, franchise relationship states permit the franchisee to seek the remedy under franchise relationship statutes. In Australia, the Competition and Consumer Act 2010 allows the franchisee to seek a remedy of statutory damages. When seeking an award of damages under the specific statutes, the franchisee needs to demonstrate that the franchisor has violated the franchise-specific law rules regulating transfer, non-renewal, or termination of a franchise. The franchisee has to plead that the franchisor's contravention of the statutory rules has caused loss or damage to the franchisee. Moreover, there must be a causal connection between the loss or damage and the franchisor's contravening conduct.

In the USA and Australia, statutory damages are generally compensatory. They aim at redressing the actual loss or damage sustained by the franchisee. The USA markedly differs from Australia in that an injured franchisee may claim punitive damages in some relationship states. For example, in Washington, the court may award treble damages for the franchisor's contravention of the Franchise Investment Protection Act. When it comes to assessing damages, the US and Australian laws do not establish a clear standard for

measuring a sum. Thus, courts can find an appropriate measure to determine actual damages, considering the circumstances of the individual case.

(3) *Discussion*

The franchisor's misconduct in the context of this chapter may inflict pecuniary or economic loss to a franchisee. For example, the franchisee may lose the revenues from a sale of a franchised business because the franchisor unreasonably withholds consent to the franchisee's proposed transfer. The franchisee may lose prospective earnings from the continuation of a franchised relationship because of the franchisor's wrongful refusal to renew an existing franchise contract. The franchisee may lose the potential income and profits because the franchisor wrongfully terminates a franchise agreement. In those instances, it may not be viable, either legally or practically, for the franchisee to enforce the franchisor's performance in kind. In this respect, a remedy of damages would function as a substitute remedy that will redress the franchisee's economic detriment. From the comparison, the legal basis for seeking an award of damages is typically twofold.

First of all, an injured franchisee may seek an award of damages for breach of contract. Resorting to contract law damages would be useful for the franchisee in at least two aspects. Damages are a primary remedy in many legal systems, including the DCFR, the USA, and Australia. In this case, courts may not exercise their discretion in awarding damages to an injured franchisee. Second, the principle of assessment of damages would benefit the claimant franchisee. As can be seen, a general measure of damages in contract law aims to put the injured party as nearly as possible into the position in which the party would have been if the contract had been duly performed. Thus, in the event of the franchisor's non-performance, the franchisee may claim damages for the loss of expectation interests, particularly the lost profits.

Nevertheless, claiming contract law damages may be constrained as a plaintiff franchisee usually has to establish the franchisor's breach of a franchise contract. Similar to the case of enforcement of performance discussed above, the franchisor may manage to avoid contractual liability for damages by incorporating the contractual terms that are self-advantageous. Strictly speaking, the franchisor may introduce a franchise agreement that does not impose an obligation concerning transfer, non-renewal, or termination of a franchise on the franchisor. For example, the franchisor may not be obliged to consent to a proposed transfer by the franchisee. In this case, the franchisor's withholding of its consent cannot be treated as a breach or non-performance of a franchise contract.

Secondly, an aggrieved franchisee may seek an award of damages in the event of the franchisor's violation of franchise relationship law. This statutory remedy would be useful for the injured franchisee when a franchise contract does not provide the franchisee with a basis for claiming damages. Since the franchisor's conduct in connection with the three exit issues is regulated, the

franchisee may claim damages by demonstrating the occurrence of the franchisor's contravening conduct and the loss caused by such conduct. For example, the franchisee may seek an award of damages by proving that the franchisee's unreasonably withholding consent to a transfer causes the loss of gains to the franchisee. In this case, there is no need to resort to a basis for damages under a franchise contract.

Seeking damages under specific legislation may have some flaws. As can be seen, in the USA and Australia, the statutes do not establish a general measure for assessing damages. The lack of the measurement standard would allow courts to identify a proper measure on a case-by-case basis. For example, some Australian courts have discussed and identified the proper measure of damages in the case of contravention of the Trade Practices Act, which is a predecessor of the current competition and consumer law or the CCA. For instance, the High Court of Australia in *Marks v GIO Australia Holdings* concluded that the measure of damages under the statute is not limited by analogy to that in tort, in contract, or in equity. In that case, a distinct measure for calculating damages has not been elaborated. Gummow J. simply stated that the measure of damages is 'the amount of' the loss or damage suffered by an injured person.⁴⁴⁴

For certainty's sake, I suggest that comprehensive franchise law elaborates on the principle regarding the assessment of damages for a violation of the franchise rules. In this respect, several approaches may be adopted by the law. Strictly speaking, the remedial rule may exemplify particular types of loss or damage that are recoverable under the franchise statute. For example, in the USA, some state franchise relationship laws permit the recovery of specific types of loss or damage, including the loss of goodwill and the lost profits.⁴⁴⁵ In my opinion, identifying the recoverable loss or damage is helpful in that courts do not have to zealously theorize on the measurement of damages, which would result in diverged opinions. In the context of this chapter, the potential loss or damage seems to be common; a franchisee typically suffers limited types of loss, such as the loss of value of some assets, the loss of income, and the loss of profits. Thus, it would be practically feasible for comprehensive franchise law to enumerate the list, either exclusive or non-exclusive, of the compensable damage.

The remedial rule should clarify some elements relevant to claiming damages for recoverable loss. For example, if the rule allows the recovery of damages for the loss of the franchisee's goodwill, the rule should define the term 'goodwill'. Without the definition, disputes may unnecessarily be triggered among the parties over the meaning of the compensable goodwill.⁴⁴⁶

444 *Marks* (n 385) [95].

445 See subsection 5.5.3.3.

446 The recovery of the value of the franchisee's goodwill may be dealt with by a different approach. This section will discuss this issue in the heading specific remedies below.

The loss of profits may explicitly be recoverable under franchise relationship statutes. However, courts might find it difficult to assess the amount of the lost profits. In this case, it would be advisable that the comprehensive franchise law establishes a specific measure for assessing the lost profits. For example, in the USA, Delaware's franchise relationship law clarifies that the recoverable loss of profits is presumed to be no less than five times the profit obtained by the franchisee in the most recently completed fiscal year.

– *Termination of a contract*

(1) *Similarity*

The DCFR, the USA, and Australia are similar in that an aggrieved franchisee may cancel a franchise relationship by employing two legal mechanisms. The first common mechanism is exercising the right to terminate under a franchise agreement.⁴⁴⁷ In practice, the termination clause of a franchise contract may provide a franchisee with the right to terminate the agreement. In some cases, the franchisee may terminate the franchise contract without any cause. However, most franchise agreements require the franchisee to terminate a franchise relationship for reasons specified by the agreement. For example, the ICC's Model Contract provides that the franchisee may terminate the agreement for the franchisor's substantial breach of contract. Furthermore, a franchise agreement may provide for specific effects or instructions after the termination of the contract is effective.

Second, an aggrieved franchisee may seek termination of a franchise contract under contract law.⁴⁴⁸ As can be seen, the law of contract of the chosen legal systems usually offers default rules enabling an aggrieved party to unmake a franchise contract. The DCFR and Australian legal system permit the franchisee to terminate a franchise contract. In the USA, the cancellation of a franchise agreement can be made by way of rescission. Under the chosen legal systems, the requirements for termination and rescission of a franchise contract are relatively comparable in the case of terminating a definite franchise agreement. That is, the franchisee may terminate or rescind the contract for the franchisor's material or anticipated breach of contract.

(2) *Difference*

In cancelling a franchise contract under contract law, the USA differs from the DCFR and Australia in terms of the retrospective effect of the rescission of a franchise contract for a definite period in contract law. In America, an order of rescission will bring about a restorative effect. In this case, the parties' position must be restored to *status quo ante*.⁴⁴⁹ In contrast, the termination

⁴⁴⁷ See subsections 5.5.2.4, 5.5.3.4, and 5.5.4.4.

⁴⁴⁸ See subsections 5.5.2.4, 5.5.3.4, and 5.5.4.4.

⁴⁴⁹ See subsections 5.5.3.4.

of a franchise contract under the DCFR and the Australian contract law produces a prospective or future effect.⁴⁵⁰ Upon the termination, the franchisor and franchisee do not have to restore the other party to a pre-contractual position because the termination will discharge the parties from performing outstanding obligations. Thus, the accrued rights or executed duties will not be affected by the termination of the agreement.

Australia markedly differs from the DCFR and the USA in that an aggrieved franchisee may resort to regulatory rescission.⁴⁵¹ In Australia, the Competition and Consumer Act 2010 provides a wide range of private law remedies, including rescission. In the franchising context, the franchisee may seek statutory rescission by alleging that the franchisor violates the Franchising Code of Conduct, thereby resulting in the franchisee's actual or anticipated loss or damage. However, a grant of the remedy of rescission is a matter of the court's discretion. If the court decides to rescind, the court may order a franchise contract to be void *ab initio*. In this case, the pre-contractual status of the franchisor and franchisee will be restored.

(3) Discussion

In many cases, despite the occurrence of the franchisor's misconduct, an aggrieved franchisee may want to uphold a franchising relationship to reap benefits and profits. In this case, the franchisee might have to resort to remedies that would redress actual or anticipated loss or damage, such as the enforcement of performance and damages. Suppose the franchisee is likely to suffer loss or damage caused by the franchisor's wrongful conduct. In that case, the franchisee may decide to compel the franchisor's performance or forbearance to eliminate the potential loss or damage. If the franchisee has suffered loss or damage, the franchisee may choose to claim damages. In these cases, cancelling a contract would seem less desirable for the franchisee.

Nevertheless, the enforcement of performance and damages may not be regarded as adequate remedies from a franchisee's perspective. In some instances, an aggrieved franchisee may want to respond to the franchisor's wrongful conduct by dissolving a franchise relationship. The dissolution of a franchise relationship may enable the franchisee to seek a return of the paid initial fees, monthly fees, and advertising fees.⁴⁵² In this respect, a question arises: what are legal mechanisms that the franchisee may utilize to discharge a franchise relationship? From the comparison, the franchisee may resort to the following three legal mechanisms to cancel a franchise contract.

First of all, the franchisee may exercise a contractual right to terminate. In some exceptional cases, a franchise agreement may allow the franchisee to terminate for specific grounds. For example, the franchise contract may

⁴⁵⁰ See subsections 5.5.2.4 and 5.5.4.4.

⁴⁵¹ See subsection 5.5.4.4.

⁴⁵² *Zeidler v A&W Restaurants Inc* 2001 WL 62571 (ND Ill, 2001) 7.

provide that a franchisee may exercise the right of termination only for the franchisor's material breach. In the Australian case *Swim Loops*, a franchise contract provided that the franchisee might terminate the agreement if the franchisee was in substantial compliance with the agreement and the franchisor breached a material and fundamental term of the agreement.⁴⁵³ However, a franchise contract is typically drafted to protect the franchisor's interests. The franchisor will hold a high degree of discretion in transfer, non-renewal, and termination of a franchise. Thus, it would be unfeasible for the franchisee to have recourse to the termination clause to terminate a franchise contract.

Secondly, an aggrieved franchisee may terminate a franchise contract under contract law. Under the rules of contract law, the franchisee usually has to prove the franchisor's material non-performance or breach of a franchise contract to seek the remedy of unmaking a franchise relationship. This requirement would restrain the franchisee from cancelling a franchise contract under contract law rules. Besides, an aggrieved franchisee should be aware that contract law rules may vary from jurisdiction to jurisdiction. For example, in the USA, a franchisee may terminate a franchise agreement by way of rescission. The effect of rescission is retrospective; hence, the parties must return the other party to the status quo ante. In Australia, a franchisee may terminate a franchise agreement by way of termination. Unlike the USA, the termination of a franchise contract under the Australian legal system will have a future effect. Thus, the parties need not to return the other party to a pre-contractual status.

The third approach is regulatory. An aggrieved franchisee may cancel a franchise agreement through a legal mechanism under specific legislation. For example, in Australia, the Competition and Consumer Act 2010 empowers the court to declare a contract to be void in the case of violation of the Franchising Code of Conduct. Nevertheless, resorting to the remedy of rescission under the CCA may be constrained. Under the CCA, the court may make a declaration if it thinks that the rescission of the contract would compensate the franchisee for the loss or damage sustained or would prevent and reduce the future loss or damage. Thus, it is vital for a claimant franchisee to prove the actual or anticipated loss or damage. Otherwise, the franchisee may not succeed in a claim for rescission.

Nevertheless, it would be wise that comprehensive franchise law provides a mechanism that an aggrieved franchisee can employ to put an end to a franchise relationship to cut loss. In this case, this chapter has discussed and proposed the model termination provisions of comprehensive franchise law.⁴⁵⁴ Those provisions can equally be applied in the case of the franchisee's termination of a franchise contract. In summary, the franchisee may terminate a franchise contract for an indefinite period by giving the franchisor written

⁴⁵³ *H2O Learning* (n 233).

⁴⁵⁴ See subsection 5.4.5.2.

notice of termination after a reasonable period has passed. In this case, the franchisee may terminate the agreement, irrespective of the franchisor's unlawful conduct. Second, the franchisee may terminate a fixed-term franchise contract for the franchisor's substantial non-performance of an obligation. The franchisor's contravention of the regulation of three exit issues proposed in this chapter would permit the franchisee to terminate a franchise contract with a definite term on those grounds.⁴⁵⁵

In terms of a temporal effect, I suggest that the exercise of the right to terminate under comprehensive franchise law should terminate a franchise relationship with a prospective effect. In franchising practice, a franchise relationship is typically a long-term relationship. In most cases, a franchise contract term is five years. In this case, it would be unfeasible and onerous for the parties to return the other party to the status quo ante if the termination is effectuated, for example in the fourth year of the relationship. Thus, the valid termination of a franchise contract should discharge the parties *in futuro*, meaning discharging the parties from unperformed obligations. In other words, the termination of a franchise contract under comprehensive franchise law should not affect the rights that have been accrued under the franchise contract before the termination is effective.

– *Specific remedies*

(1) *Similarity*

The DCFR, the USA, and Australia permit the incorporation of the terms into a franchise contract that provides the franchisee with additional remedial rights when a franchise contract is terminated. This conclusion infers from the fact that no rule under the chosen legal systems prohibits this contractual arrangement. Thus, under the terms of a franchise agreement, the franchisee may be entitled to the right to require the franchisor to repurchase. In practice, a buyback provision may provide that the franchisee is entitled to the repurchase by the franchisor of some remaining assets, such as stocks, supplies, inventory, and equipment, when the contract is terminated. The franchisee may hold the right to indemnity for goodwill. A franchise contract may allow the franchisee to get indemnification for the value of its local goodwill upon the termination of a franchise agreement.

⁴⁵⁵ For example, this chapter has proposed that the franchisor should be obliged by the transfer rule not to withhold its consent to a transfer for unreasonable grounds. Thus, in the case of the franchisor's unreasonably withholding consent to a transfer, the franchisee may provide the franchisor with written notice requiring the franchisor to cure the default by consenting to the transfer. In doing so, the franchisee may fix a reasonable period of not less than 15 days for the cure. If the franchisor failed to fix the default within a specified duration, the franchise contract is automatically terminated.

(2) *Difference*

Unlike Australia, the DCFR and the US legal system recognize the franchisee's legal rights to repurchase and indemnity for goodwill.⁴⁵⁶ Under the DCFR, the franchisee may resort to the rules in Book IV to ask the franchisor to repurchase stock, spare parts, and materials and get compensated for a transfer of goodwill. In the USA, some state relationship statutes provide the franchisee with auxiliary remedies that entitle the franchisee to demand the franchisor to repurchase some properties and compensate for the value of goodwill and franchised business. Nevertheless, the DCFR differs from the USA in that the provisions governing these two entitlements are default rules. In this case, the parties may agree to exclude the application of the provisions or deviate from or vary the effects of the rules through the terms of a franchise contract. In contrast, the US state relationship law rules are mandatory. Thus, it would be impossible for the parties to contract around the application of the statutory provisions by the contract terms.

(3) *Discussion*

From a franchisee's standpoint, some tangible and intangible assets may need greater protection upon the cessation of a franchise contract. In many cases, a franchise contract imposes a non-competition obligation on the franchisee upon the termination of a franchise relationship.⁴⁵⁷ The possible implications of the non-compete obligation are twofold.⁴⁵⁸ First, the terminated franchisee may be restricted from reselling some items, such as unsold stocks and inventory. Second, the franchisee may be prevented from exploiting goodwill that has been developed during a franchise relationship.⁴⁵⁹ These restrictions would cause the franchisee to suffer financial detriment because of the lack of compensation for the value of these assets. Thus, one may question how a franchisee derives the right to repurchase and the right to indemnity for goodwill. From the comparison, the approach to creating these entitlements is twofold.

The first approach is contractual. In franchising practice, the franchisee's right to repurchase and the right to compensation for goodwill may expressly be established by the terms of a franchise agreement. In reality, a franchisor may prevent the franchisee from retaining those contractual rights in several

⁴⁵⁶ See subsections 5.5.2.5 and 5.5.3.5.

⁴⁵⁷ David Gurnick, 'Chapter 6: Typical Contract Terms' in Alexander M Meiklejohn (ed), *Franchising: Cases, Materials, & Problems* (American Bar Association 2013) 280.

⁴⁵⁸ It should be noted that some legal systems may regulate post-contractual non-compete clauses. In Australia, for example, the Franchising Code of Conduct contains clause 23 regulating the effect of a restraint of trade clause if a franchise agreement is not extended. Furthermore, some states, such as New South Wales, have restraints of trade law regulating the validity of a restraint of trade agreement, which would be relevant in the franchising context.

⁴⁵⁹ *Bundy American LLC v Hawkeye Transportation* 2009 WL 10676371 (WD Wash, 2009) 5.

ways.⁴⁶⁰ For example, the franchisor may hold discretion in exercising an option to repurchase items or to compensate for goodwill. The franchise agreement may also affirm that the franchisor has no obligation to refund or compensate a franchisee for some merchandise and goodwill. In this case, the franchisee may get indemnified for the value of those properties, provided that the franchisor has decided to do so. Therefore, the use of a franchise agreement might not be protective of the franchisee in this context.

The second approach is regulatory. A franchisee may seek auxiliary remedies under franchise-specific law rules. From the comparison, the repurchase and goodwill provisions can be categorized into default and mandatory provisions. In this respect, the choice of the character of the rules seems to be imperative in terms of the protection of franchisees. From my perspective, making the statutory provisions default rules, as does the DCFR, would be less protective of a franchisee since the exclusion or variation of the provision is ordinarily allowed. Because of the unequal bargaining power, a superior franchisor will find a way to contract around the rules by introducing the terms of a franchise agreement that are franchisor-friendly. For example, the franchisor may draft a franchise contract containing the term providing that the franchisor is not obliged to repurchase the franchisee's items or to compensate the franchisee for goodwill.

For greater protection of the franchisee, I suggest that comprehensive franchise law contain the repurchase and compensation of goodwill provisions that are made mandatory. A mandatory character of the rules would assure that the terms of a franchise contract will not exclude the franchisee's rights to compensation for the value of particular assets upon the termination of a franchise contract. This regulatory assurance would be helpful for the franchisee in that it would prevent potential abuse by the franchisor and help produce a more balanced and fairer franchise network.⁴⁶¹ This specific remedy would also help the franchisee recoup sunk investment cost, which would hardly be recovered under the law of damages. In this case, the franchisor will always be obliged to repurchase specified items and compensate the franchisee for goodwill and cannot exclude this obligation.

Nevertheless, one may claim that the imposition of the reimbursement obligations would be excessively disadvantageous to the franchisor. In my view, this concern would be slight. In the case of repurchase, it is argued that the franchisor will not be financially burdened because the franchisee usually acquires reasonable quantities of stocks and other items in reliance on the

460 See eg *Fleetwood v Stanley Steamer Intern Inc* 725 F Supp2d 1258 (ED Wash, 2010) 273; *AMC Commercial Cleaning (NSW) Pty Ltd v Coade* [2011] NSWSC 932 [56]. See also DISTRIBUTOR AGREEMENT PREAMBLE, April 14, 2006, CREATIVE ENTERPRISES INTERNATIONAL INC, 10-KSB, EX-10, 10 page(s), 2006 WL 8310792, Westlaw Next.

461 Emerson, 'Thanks for the Memories: Compensating Franchisee Goodwill after Franchise Termination' (n 361) 333 – 34.

continuation of a franchise relationship. Furthermore, the repurchase requirement would even be advantageous to the franchisor in that the franchisor can control the distribution of its trademarks products so that the franchisor's reputation of a franchise system is protected.⁴⁶² In case of compensation for goodwill, it is argued that the franchisor's compensation for the value of goodwill would label a franchisee as an independent contractor, helping the franchisor avoid vicarious liability for the franchisee's conduct. Moreover, the franchisor would avoid potential lawsuits filed by the franchisee when a franchise relationship is terminated.⁴⁶³

The conferral on the franchisee of the right to repurchase and the right to indemnity for goodwill should be qualified, considering the principal purpose of the establishment of the rights. According to Chisum, the apparent purpose of the compensation requirement is to prevent a franchisee from encountering unnecessary financial hardship.⁴⁶⁴ From a practical perspective, that preventive goal is seemingly adopted by some franchise relationship legislation, such as the US franchise relationship laws. Taking the Washington franchise statute as an example, section 19.100.180(i) provides that the franchisor's refusal to renew a franchise will be unlawful if the franchisor does not fairly compensate for the market value, at the time of the expiration of the franchise, of the franchisee's specified assets and goodwill. In the case of goodwill, the franchisor does not have to compensate for the franchisee's goodwill if the franchisor gives the franchisee one year's notice of non-renewal and the franchisor agrees in writing not to enforce any covenant which restrains the franchisee from competing with the franchisor. This rule is claimed to protect franchisees from the loss of capital outlay.⁴⁶⁵

As mentioned elsewhere, the effect of restrictive covenants could restrain the franchisee from operating a competitive business outlet that resells unsold stocks and reimburses for the value of its goodwill. In those cases, the franchisee is likely to suffer financial loss unless the franchisor decides to waive the right to enforce the non-competition clauses. Accordingly, the establishment of the right to repurchase and the right to indemnity for goodwill should reflect the purpose of the protection of the franchisee against potential financial hardship. The franchisor's refusal to enforce non-compete covenants could be taken as an example of the requirement for exercising the right to repurchase and the right to indemnity for goodwill. However, legal systems may introduce other requirements that qualify the exercise of these specific rights.

In designing the substantive provisions regulating the franchisee's rights to repurchase and indemnity for goodwill, the rules of the DCFR and the US

462 Bundy and Einhorn (n 30) 215; Appleby and Rosario (n 227) 228.

463 Emerson and Carrington (n 366) 292.

464 Chisum (n 365) 378.

465 *Jon K Morrison Inc et al v Avis Rent-A-Car Systems Inc* 2003 WL 23119903 (WD Wash, 2003) 4.

state franchise relationship laws could be taken as models. From the comparison, those provisions have the following three features in common.

First, the repurchase and goodwill provisions ordinarily specify events that lead to the franchisor's obligations to repurchase and compensate for goodwill. In general, the dissolution of a franchise contract is the event that will trigger the franchisor's duties. Nevertheless, legal systems differ in detail about how a franchise relationship is dissolved. Taking the DCFR as an illustration, the franchisee will hold the right to repurchase upon the avoidance and termination of a franchise agreement. Conversely, the franchisee may indemnify for a transfer of goodwill based on the mere fact that a franchise relationship is ended, regardless of whether the agreement is terminated or expires. Thus, it would be advisable that the comprehensive franchise law clearly enumerates the situations in which a franchise contract comes to an end.⁴⁶⁶

Second, the rules typically identify the properties or assets, the value of which is reimbursed. In the case of the repurchase requirement, the repurchase rule may enumerate specific properties that will be repurchased by the franchisor. However, the repurchase provisions may vary in terms of the items to be repurchased. Despite the variation, the repurchased assets usually include stock, spare parts, inventory, supplies, equipment, and furnishings. The repurchase rule may require that the items to be repurchased must be those items that were originally bought from the franchisor or the franchisor's approved supplier.⁴⁶⁷ In the case of goodwill, identifying the item seems to be rather impractical. As can be seen, no common definition of goodwill is provided by both the DCFR and the US state franchise relationship statutes. The lack of definition may result from the elusive and variable nature that makes it difficult to formulate a uniform concept of goodwill in the franchising context.⁴⁶⁸ Thus, those legal systems leave the identifying task to courts to decide on a case-by-case basis. In defining goodwill, the precedent laid down by the High Court of Australia in *Commissioner of Taxation v Murry* may be taken as guidance.⁴⁶⁹ The opinions of some legal scholars, such as Gangemi's, may help demarcate the scope of the franchisee's goodwill.⁴⁷⁰

⁴⁶⁶ As can be seen, there has been no uniformity concerning the triggering events. Thus, it might depend on the policy consideration of each legal system when it comes to defining the circumstances that trigger the buyback and compensation for goodwill obligations.

⁴⁶⁷ There is no uniform rule in this case. For example, the DCFR requires the franchisor to repurchase the franchisee's remaining stock, spare parts, and other materials. This repurchase rule could broadly be interpreted to require the franchisor to repurchase all the franchisee's excess items, regardless of whether those items are bought from the franchisor. In any case, comprehensive franchise law should provide clarification on the items to be repurchased by the franchisor so that the parties have prior awareness of what properties are subject to the requirement of repurchase.

⁴⁶⁸ Chisum (n 365) 377.

⁴⁶⁹ See subsection 5.5.4.5.

⁴⁷⁰ See Gangemi (n 423).

Third, the rules frequently provide a measure for assessing the value of the properties to be compensated. From the comparison, there are different approaches to assessing the value of the assets. In some cases, the rules opt for the standard of fairness and reasonableness. For example, under the DCFR, the franchisor is required to repurchase the specified items at a reasonable price. In the USA, the law of Connecticut requires the franchisor to compensate the franchisee for the fair and reasonable value of the specified materials. In other cases, the rules adopt specific measures, such as the fair market value. In America, under the law of Hawaii, the franchisor is required to compensate the franchisee for the fair market value at the time of termination or non-renewal of a franchise contract.⁴⁷¹ The standard of the fair market value is also adopted in other US states, such as California and Washington.⁴⁷²

In my view, the standard of fairness and reasonableness is rather ambiguous and provides no helpful guidance because of its elusiveness. In the commercial context, the measure of the properties should reasonably be predictable. From an accounting viewpoint, there are several tests that can be employed to evaluate the price of the assets. One of those standards is the test of fair market value. However, some people may have concerns over the utilization of the standard of fair market value. For example, Chisum claimed that, concerning the repurchase requirement, the fair market value of second-hand specialized equipment and furnishings is often nominal. In other words, the franchisee would get nothing from the franchisor's buyback.⁴⁷³ I would agree with Chisum that, in some cases, the value of some assets may be insignificant at the time of repurchase or compensation. Nevertheless, it should be reminded that the primary purpose of the repurchase and goodwill rules is to prevent the franchisee from suffering any financial loss. In this case, I am of the opinion that the fair market value offers an acceptable standard that could serve the purpose of compensation for the value of the franchisee's assets.

5.5.5.3 Conclusions

– Concluding remarks

The DCFR, the USA, and Australia offer three private law remedies that could help redress or prevent the franchisee's financial loss or damage in the event of the franchisor's wrongful conduct made in the context of this chapter. First, an aggrieved franchisee may enforce the franchisor's performance and forbearance in accordance with the terms of a franchise contract or the rules of law. Second, the franchisee may claim damages to compensate for the loss or damage caused by the franchisor's violating conduct. Third, the franchisee

⁴⁷¹ HI ST, § 482E-6(3).

⁴⁷² WA ST, 19.100.180(i) and (j).

⁴⁷³ Chisum (n 365) 378.

may cut loss by dissolving a franchise relationship through the termination or rescission of a franchise contract. Besides the three principal remedies, the DCFR and the USA also entitle the franchisee to compensation for the value of some tangible and intangible assets, including unsold items and goodwill. These entitlements are ordinarily provided upon the cessation of a franchise contract.

– *Key recommendations*

(1) *Remedial system*

Comprehensive franchise law should offer a remedial system that provides remedial mechanisms for an aggrieved franchisee to utilize in the event of the franchisor's contravention of the rules regulating the transfer, non-renewal, and termination of a franchise contract. At the very least, these remedial mechanisms should include the enforcement of performance, recovery of monetary compensation, and termination of a franchise contract.

(2) *Enforcement of performance*

The remedial system should offer a remedy that allows the enforcement of performance. This remedy may take the form of specific performance and injunctions. In any case, those remedial mechanisms should enable the franchisee to compel the franchisor to perform some action or forbear from taking some action that is considered in contravention of the rules of comprehensive franchise law.

(3) *Monetary compensation*

The remedial system should provide a remedy that allows the franchisee to seek monetary compensation or damages. In this case, the remedial rule should be clear about the preconditions for an award of damages. In particular, the rule should enumerate specific types of recoverable loss under comprehensive franchise law to establish a precise measure for calculating damages.

(4) *Termination of a contract*

The remedial system should provide a legal mechanism that enables the franchisee to terminate a franchise contract. The requirements for exercising the right to terminate may be distinguished when it comes to terminating an indefinite franchise contract and a definite franchise contract. Besides, the effects of the termination should explicitly be specified under the law. In this case, it is suggested that the valid termination should have a prospective effect that discharges all the parties' outstanding obligations.

(5) *Specific remedies*

Comprehensive franchise law should contain remedial provisions constituting the franchisee's right to repurchase and the right to compensation for goodwill

as distinct remedial rights. The main goal of the formulation of the repurchase and goodwill rules should be to protect the franchisee from encountering any financial detriment or damage. Under the remedial provisions, the following three conditions should, at least, be provided. First, the rules should specify the events that trigger the franchisor's obligations to repurchase and compensate for goodwill. Second, the rules should identify the assets, the value of which is to be indemnified. Third, the rules should provide a clear standard for assessing the value of the properties to be reimbursed.

5.6 CONCLUSIONS

Chapter five has demonstrated that the franchise legal framework of the DCFR, the USA, and Australia generally regulate transfer, non-renewal, and termination of a franchise contract in two aspects. Firstly, from a procedural perspective, the franchisor may be required to get the franchisee sufficiently informed of its intention regarding the exit issues. The franchisor may have to notify the franchisee of whether to consent to the franchisee's proposed transfer. The franchisor may have to inform the franchisee of whether to renew an existing franchise agreement. The franchisor may have to give the franchisee notice of termination. Secondly, from a substantive viewpoint, the franchisor may be required to have justifiable grounds for making decisions. The franchisor may withhold consent to a transfer insofar as the withholding is reasonable. The franchisor may not refuse to renew or terminate a franchise agreement unless the franchisor has legitimate grounds. Nevertheless, the approaches taken to regulating those two aspects may vary among the selected legal systems.

Chapter five has also shown that the franchisor's violation of the regulation usually leads to private law sanctions. In the event of the franchisor's contravention, the DCFR, the USA, and Australia make three principal private law remedies available for an aggrieved franchisee. The franchisee may enforce the franchisor's performance and forbearance. The franchisee may claim monetary compensation to recover the loss or damage sustained. The franchisee may unilaterally terminate a franchise contract. Moreover, the DCFR and the USA offer additional remedies that protect the value of the franchisee's tangible and intangible assets. Under the remedial regimes, the franchisee may require the franchisor to repurchase the remaining items and compensate for the value of goodwill upon the cessation of a franchise relationship. However, the requirements vary among the legal systems.

6 | Conclusion

6.1 INTRODUCTION

Legal systems around the globe encounter franchisor opportunism that occurs in three stages of a franchise life cycle, from a pre-contractual stage to an end of a franchise relationship. These legal systems may cope with this relational problem in different ways. Some legal systems consider franchise regulation through franchise-specific law rules as a panacea for the problem. Suppose these legal systems think the time is right to introduce comprehensive franchise law to regulate franchisor opportunism. In this case, a challenging question arises as to which rules should be developed to regulate the franchisor's opportunistic conduct in the three stages of a franchise life cycle. This question is set to be an overarching research question. This thesis aims to answer this research question with an intention to offer a source of inspiration for legal systems when introducing comprehensive franchise law that contains private law rules regulating franchisor opportunism in the whole life of a franchise relationship, from its birth to its end, as well as remedies for violation of the regulation.

This thesis has conducted doctrinal legal research with a comparative law analysis of the franchise legal framework of the Draft Common Frame of Reference (DCFR), the United States of America (USA), and Australia to answer the main research question to achieve the objective mentioned above. After the examination, this research study has offered the answer that legal systems should introduce comprehensive franchise law that contains two types of private law rules. First, comprehensive franchise law should contain substantive law rules that regulate the franchisor's pre-contractual information duties, the franchisor's ongoing duty not to encroach and duty to assist, and the transfer, renewal, and termination of a franchise contract. Second, comprehensive franchise law should contain remedial rules that provide mechanisms for an aggrieved franchisee to enforce the franchisor's performance, claim damages, and cancel a franchise contract. The remedial rules may confer on the franchisee the right to repurchase and the right to reimburse for goodwill upon the cessation of a franchise relationship.

In formulating the research proposal in the preceding paragraph, this thesis has carried out the comparative law study step-by-step. This thesis has started examining the definition and elements of a franchise under the franchise legal framework of the DCFR, the USA, and Australia in chapter two. Then, chapters

three to five have examined the franchise legal framework of the DCFR, the USA, and Australia to answer the sub-research questions to develop detailed research proposals. Chapter six will recapitulate the research findings and recommendations made in these four chapters in sections 6.2 to 6.5, respectively. Each section will also state caveats regarding the recommendations. In the end, section 6.6 will conclude to end the book and provide a thought for further research.

6.2 DEFINITION OF A FRANCHISE

6.2.1 Research findings

Chapter two has found that the franchise legal framework of the DCFR, the USA, and Australia similarly regulates the following three fundamental elements of a franchise, which is a marketing relationship created by a franchise contract or agreement between a franchisor and a franchisee. First, the franchisor must agree to grant the franchisee the right to conduct a franchised business. Second, the franchisor must agree to grant the franchisee the right to use the franchisor's marks in the operation of a franchised business. Third, the franchisee must agree to pay the franchisor monetary consideration in exchange for the grant of the rights. Without these three essential elements, a marketing relationship will not be regarded as a franchise in light of the chosen legal systems' franchise legal framework.

Chapter two has discovered that the DCFR, the USA, and Australia differ in three detailed requirements for establishing a franchise. The marked difference is that the DCFR's franchise-specific law does not mention a formality in concluding a franchise contract. Conversely, the franchise legislation of the USA and Australia explicitly regulates the format of a franchise agreement. Despite the divergence, the latter two legal systems generally allow a franchise contract to be made in oral and written form. The other two differences are connected to the explicit acceptance of specific components of a franchise. First, unlike the USA and Australia, the DCFR expressly includes an independence concept into the definition of a franchise contract. However, it could be said that the US and Australian legal systems tacitly adopt this independent idea. Second, some US franchise regulating states adopt a so-called 'community of interest' element in a franchise definition. This component focuses on shared financial interests between a franchisor and franchisee, which cannot be observed in a definition of a franchise in other legal systems.

6.2.2 Recommendation

This research study has suggested that comprehensive franchise law defines a franchise to open the door to regulating a franchise relationship. In defining a franchise, comprehensive franchise law should establish the essential elements of a franchise comparable to those adopted by the franchise legal framework of the DCFR, the USA, and Australia. In other words, the term 'franchise' should be defined as a legally enforceable contract between a franchisor and franchisee with the following three fundamental components.

First, the franchisor must agree to grant the franchisee the right to conduct a franchise business, which is a business of offering, dispensing, or distributing the franchisor's goods or services onto the market. In this element, the law should assert the franchisor's control over the franchisee's business or marketing plan or method. The law should ensure the franchisee's independence in operating a franchised business.

Second, the franchisor must agree to grant the franchisee the right to use the franchisor's marks in a franchised business operation. In this case, the law should define the franchisor's marks to include the franchisor's intellectual property rights and other commercial names or symbols, which are not regarded as IP rights *per se*.

Third, the franchisee must pay or agree to pay the franchisor monetary considerations to obtain the right to operate a franchise business and the right to use the franchisor's marks. These monetary considerations may take several forms. In any case, the law should ensure that the franchisee pays or agrees to pay these sums of money to reciprocate the franchisor for the grant of the rights.

In addition to the essential elements of a franchise contract, this research study has also advised that comprehensive franchise law regulates a formality of a franchise contract. This thesis suggests that a franchise contract should be required to be evidenced in writing. Failure to comply with this formal requirement should merely render the franchise contract unenforceable. In other words, an oral franchise agreement can be valid, but it cannot be enforced in courts.

6.2.3 Limitation

This thesis has proposed the essential elements of a franchise contract and its format in comprehensive franchise law with one limitation. This research study has merely discussed and suggested a big picture of a franchise. In other words, this research has not analyzed all elements that should be considered when defining a franchise under the legislation. For example, this research study has not discussed if comprehensive franchise law should adopt the American notion of 'community of interest' as one component of a franchise.

Nor does the research discuss what the challenges would be if the law inserts this element in the definition of a franchise. In this respect, therefore, legal systems may tailor detailed requirements for constituting a franchise under comprehensive franchise law to align with their societal, economic, or political policies.

6.3 REGULATION OF PRE-CONTRACTUAL INFORMATION OBLIGATIONS OF THE FRANCHISOR

6.3.1 Duty of pre-contractual disclosure

6.3.1.1 *Research findings*

Chapter three has found that the franchise legal framework of the DCFR, the USA, and Australia similarly establishes the franchisor's pre-contractual disclosure duty. Generally speaking, the franchise legal framework of the selected legal systems requires a franchisor to provide a prospective franchisee with essential information about the franchisor, the franchise system, the franchise business, and the terms of a franchise agreement for a certain period before the conclusion of a franchise contract. In requiring the franchisor to disclose pre-sale information, however, the franchise legal framework of the DCFR, the USA, and Australia does not regulate a means for delivering the information. In this case, the chosen legal systems seem to accept that the franchisor may disclose the required pre-sale information electronically.

Chapter three has also discovered two notable differences as follows.

First, the DCFR markedly differs from the US and Australian legal systems in formatting the disclosure of pre-sale information and fixing the disclosure period. The DCFR does not require a franchisor to provide a prospective franchisee with a disclosure document, as the US and Australian legal systems require. Besides, unlike the USA and Australia, the DCFR does not obligate a franchisor to provide a prospective franchisee with pre-contractual information within 14 days before concluding a franchise contract.

Second, the USA differs from the DCFR and Australia in that the franchise legal framework permits the disclosure of pre-sale information to be performed by the franchisor's representative, agent, employee, and broker in certain circumstances. In addition, the disclosure of pre-sale information can be performed towards an agent, representative, and employee of an actual franchisee.

6.3.1.2 *Recommendation*

This research study has proposed that comprehensive franchise law contains disclosure provisions imposing a pre-contractual disclosure obligation on a

franchisor towards a prospective franchisee. This thesis has proposed that comprehensive franchise law defines the term 'prospective franchisee' to mean a person who approaches or is approached by a franchisor for the right to conduct a franchise business. In determining the existence of the status of a prospective franchisee, this research study has suggested that the law should establish a clear benchmark. For example, the law may deem a person who expresses its intention to negotiate for the right to conduct a franchise business to be a prospective franchisee in light of the disclosure rules.

Under the disclosure rules, a franchisor should be required to provide a prospective franchisee with material information that sufficiently provides insights into the franchisor, the franchise system, the franchise business, and the fundamental rights and obligations under a franchise contract. The franchisor should be required to disclose such information within at least one month before the conclusion of a franchise contract or the franchisee's prepayment of monetary considerations, depending upon which event is triggered first. Besides, the franchisor should be required to provide the prospective franchisee with pre-contractual information in the form of a simplified and streamlined disclosure document. In this case, the franchisor may deliver the disclosure document by any means, including electronic transmission. Nevertheless, the disclosure rules should regulate the franchisor's electronic disclosure in the following three aspects: the durability of the digital document, prospective franchisee's consent, and prior consultation by a franchisor.

6.3.1.3 Limitation

This thesis has proposed the establishment of the franchisor's pre-contractual duty of disclosure under comprehensive franchise law with the following three limitations.

First, this research study has suggested the underlying principle that the contents of pre-sale information should address the franchisor, the franchise system, the franchise business, and the fundamental rights and obligations under a franchise contract. Nevertheless, this research has not discussed and recommended specific informational items listed in comprehensive franchise law's disclosure provisions. In this case, legal systems will be free to decide on making a list of the required information to be disclosed, either exhaustive or non-exhaustive list. Despite this decisional freedom, it should be mentioned that this thesis has advised that comprehensive franchise law requires a franchisor to disclose a reasonable number of informational items so that a prospective franchisee can comprehend the disclosure items at marginal cost.

Second, this research study has proposed that the franchisor's disclosure is performed by providing a prospective franchisee with a simplified and streamlined disclosure document. However, this thesis has not suggested the form and order of the disclosure document under comprehensive franchise law. In this case, legal systems have the freedom to format a disclosure docu-

ment, which should be readable and well-organized. Nevertheless, legal systems should ensure that the format of a disclosure document is not extensive and focuses on delivering important pre-contractual information to a prospective franchisee. In other words, legal systems should not require a disclosure document to include irrelevant statements or information.

Third, this research study has not discussed how public law rules play a significant role in facilitating the franchisee's acquisition of pre-contractual information about a franchisor and a franchise system. This thesis has focused on formulating private law rules establishing the franchisor's pre-contractual information duties. Thus, it has not touched on the issue of whether and to what extent legislation requires the franchisor to make certain items of information available as public records so that prospective franchisees can acquire the information free of charge to conduct due diligence.

6.3.2 Duty to provide complete, current and accurate information

6.3.2.1 *Research findings*

Chapter three has discovered that the franchise legal framework of the DCFR, the USA, and Australia does not constitute the franchisor's pre-contractual duty to provide complete, current and accurate information as a duty distinct from the pre-contractual duty of disclosure. Nevertheless, this chapter has found that the chosen legal systems regard disclosing current and accurate pre-sale information as a manner in which a franchisor has to engage when performing the pre-contractual disclosure obligation. In this respect, the franchisor's failure to provide a prospective franchisee with current and accurate information would be considered breach of a pre-contractual disclosure duty under the selected legal systems. Besides, the DCFR and Australia adopt the concept of good faith that could be utilized to require the franchisor to ensure the accuracy and currentness of disclosure items.

The third chapter has found that the DCFR markedly differs from the USA and Australia in the following two aspects. First, the DCFR does not contain provisions requiring a franchisor to update pre-contractual information annually to reflect changes to the disclosure items. Second, the DCFR does not contain anti-fraud provisions preventing the dissemination of misleading pre-contractual information by a franchisor. The possible explanation for the disparity is that the DCFR's franchise-specific law is not primarily designed to perform industry-specific regulation as same as franchise legislation of the USA and Australia. In other words, the DCFR's franchise-specific law principally intends to offer specific contract law rules governing rights, duties, and liabilities of the parties to a franchise contract. In this respect, the level of franchise regulation may not be as high as the US and Australian franchise laws.

6.3.2.2 *Recommendation*

This research study has proposed that comprehensive franchise law contains disclosure provisions constituting the franchisor's duty to provide complete, current and accurate information as a distinct pre-contractual duty. The law rules should obligate a franchisor to provide a prospective franchisee with pre-contractual information with a certain degree of care; the rules should require the franchisor to provide the franchisee with pre-contractual information, which is current, complete, and accurate at the date of the provision of the information. This research study has also suggested that comprehensive franchise law may, if legal systems so choose, contain provisions establishing reinforcing mechanisms that would strengthen the delivery of current and candid disclosure items. For instance, comprehensive franchise law may constitute an obligation to act in good faith and fair dealing that would require a franchisor to ensure the trustworthiness and truthfulness of pre-sale information. Furthermore, comprehensive franchise law may prohibit particular fraudulent conduct of the franchisor in a pre-contractual stage, including intentionally making an untrue statement of material facts.

6.3.2.3 *Limitation*

There is a word of caution concerning the recommendation mentioned in the preceding paragraph. This thesis has suggested that comprehensive franchise law ensures the currentness, completeness, and accuracy of pre-contractual information to be provided. Nevertheless, this research study has not gone into details about how to determine if the information is current, complete, and accurate at the time of dissemination. In this respect, legal systems may leave the issue for a regulator or court to decide on a case-by-case basis. Alternatively, legal systems may elaborate on requirements for disclosing particular pre-sale informational items to set a benchmark for determining the integrity and truthfulness of the information. Suppose the disclosure rules require a franchisor to provide a prospective franchisee with information about litigation history. In this case, the rules may, among other things, provide that the franchisor has to disclose if the franchisor has pending civil actions against the franchisor regarding a franchise and if the franchisor was liable in a civil action regarding a franchise back in ten years. This requirement would ensure that the provision of the franchisor's litigation history is current and complete.

6.3.3 Private law remedies

6.3.3.1 *Research findings*

Chapter three has found that the franchise legal framework of the DCFR, the USA, and Australia similarly permits an aggrieved franchisee to seek monetary compensation. Under the selected legal systems, the franchisee may claim compensatory damages for the loss caused by the franchisor's failure to comply with the franchise disclosure rules. In this case, the franchisee may seek damages to recover reliance or out-of-pocket loss. However, the chosen legal systems seem not to allow the recovery of the lost chance. Additionally, the third chapter has discovered that the franchise legal framework of the DCFR, the USA, and Australia have certain legal mechanisms that can be utilized to cancel a franchise relationship in the event of the franchisor's contravention of the disclosure rules. In summary, an aggrieved franchisee may avoid a franchise contract in light of contract law rules on mistake and fraud under the DCFR. In the US and Australian legal systems, the franchisee may rescind a franchise contract based on the theory of misrepresentation.

The third chapter has detected a marked difference in terms of enforcing the franchisor's performance of pre-contractual information duties. Chapter three has found that the franchise legal framework of the DCFR and Australia permits a prospective franchisee to compel the franchisor's performance of the pre-contractual obligations. However, the legal mechanism that allows the franchisee to enforce the franchisor's performance differs between these two legal systems. Under the DCFR, the franchisee has to resort to contract law rules on enforcing specific performance of an obligation. Conversely, in Australia, the franchisee needs to seek statutory injunctions under the CCA and the ACL to compel the franchisor's performance of the obligations. While the right to enforce specific performance is a matter of right under the DCFR, in Australia, a court will have discretion to grant an injunction compelling the franchisor to perform specific duties. In the USA, it is not certain if a remedial provision offering catch-all relief under the state franchise sale statute of some jurisdictions can be utilized to enforce the franchisor's disclosure under the laws.

6.3.3.2 *Recommendation*

For the sake of protecting the franchisee's rights, this research study has proposed that comprehensive franchise law establishes a remedial system that enables an aggrieved franchisee to seek the following three private law remedies: (1) enforcement of the franchisor's performance of pre-contractual information duties, (2) recovery of damages, and (3) cancellation of a franchise contract. First, the law should facilitate the acquisition and utilization of the pre-contractual information by enabling a prospective franchisee to enforce the franchisor's disclosure of current and candid pre-sale information. Second,

the law should allow a prospective franchisee to redress the loss or damage caused by the franchisor's non-performance of the pre-contractual information obligations. Third, the law should construct a legal mechanism that allows the franchisee to rescind or avoid a franchise contract with a retrospective effect. In this case, the law may require that the franchisor's non-performance of the pre-contractual information duties materially affects the franchisee's decision to enter into a franchise contract.

6.3.3.3 *Limitation*

There are the following two limitations concerning the recommendation mentioned above.

First, this research study has proposed the principle that comprehensive franchise law introduces remedial mechanisms that enable an aggrieved franchisee to seek the three private law remedies. Nevertheless, this research study has not thoroughly discussed the establishment of each mechanism. For example, this research study has not elaborated on detailed mechanisms in which an aggrieved franchisee may rescind or avoid a franchise contract. Strictly speaking, this thesis has relinquished discussing if comprehensive franchise law should regard rescission or avoidance of a franchise contract as a matter of the franchisee's right or should confer the power to rescind or avoid a franchise contract on courts upon the franchisee's request. In this respect, legal systems are free to decide on the approach that suits their systems.

Second, this research study has not discussed the internal element of the franchisor's liability. That is, this thesis has not discussed if comprehensive franchise law should insert a fault element requiring a claimant franchisee to prove that a franchisor fails to perform the pre-contractual duties intentionally or recklessly. In other words, this research study has left the nature of the franchisor's liability for legal systems to decide on based on their legal policy. For example, legal systems may require proof of franchisor's scienter in the case of liability for damages and cancellation of a franchise contract while disregarding this internal element when it comes to enforcing the franchisor's performance. Other legal systems may disregard the fault element altogether so that the franchisor's liability to the franchisee is of a strict character.

6.4 REGULATION OF THE FRANCHISOR'S ONGOING OBLIGATIONS

6.4.1 Duty not to encroach

6.4.1.1 *Research findings*

Chapter four has found that the DCFR, the USA, and Australia are similar in the following aspect. That is, the chosen legal systems, except for the five US relationship states, do not introduce franchise-specific law rules regulating encroachment by a franchisor. Thus, a franchise contract will primarily regulate the franchisor's duty not to encroach. In practice, a franchise contract may include an exclusivity clause that establishes the franchisee's exclusive territory and prevent the franchisor from encroaching upon that geographic location, such as placing a new franchised store within the vicinity of the franchisee's location. Despite the absence of this express agreement, the selected legal systems seem to permit courts to imply terms into a franchise contract prohibiting the franchisor's encroachment.

As mentioned above, the fourth chapter has discovered that the five US relationship states – Hawaii, Indiana, Iowa, Minnesota, and Washington – differ in that they regulate the franchisor's encroachment through franchise relationship law rules. These rules mainly aim to prevent the franchisor from geographically encroaching upon the existing franchisee's business. Nevertheless, there is one divergence between the five states. That is, unlike the other three jurisdictions, Iowa and Indiana's franchise relationship law rules bar the franchisor from engaging in territorial encroachment, regardless of whether the franchisor grants the franchisee an exclusive territory under a franchise contract. In other words, the anti-unfair competition rules of Hawaii, Minnesota, and Washington will apply to prevent the franchisor's geographic encroachment only if the franchisee is granted an exclusive area of business.

6.4.1.2 *Recommendation*

This research study has proposed that comprehensive franchise law contain a mandatory, anti-encroachment provision regulating two forms of the franchisor's encroachment upon the franchisee's business. Nevertheless, this research study does not intend an anti-encroachment rule to prohibit the franchisor's encroaching conduct. Instead, this research study suggests that the rule requires the franchisor to remedy any financial detriment suffered by the franchisee. Thus, the franchisor should be required to satisfy the following two preconditions before engaging in traditional and non-traditional conduct. The first condition is that the franchisor may encroach upon the existing franchisee's reasonable area provided that the franchisor has offered the franchisee the right to operate a new franchise outlet in a reasonable area of the franchisee's business. Second, the franchisor may encroach upon the existing franchisee's

reasonable area provided that the franchisor has offered reasonable compensation or other remedial forms to offset the franchisee's lost profits caused by the franchisor's encroachment.

6.4.1.3 *Limitation*

There are two limitations concerning the above-mentioned recommendation as follows.

First, this research study has suggested the franchise regulation of the franchisor's non-traditional encroachment conducted in the franchisee's protected marketing area. In this case, this research study has focused on discussing the franchisor's encroaching upon the franchisee's location by online sales. In other words, this thesis has not discussed other forms of franchisor's non-traditional encroachment that should be regulated in light of the thesis's recommendation. For example, this research study has not analyzed if sister brand encroachment, signifying the franchisor's acquisition of a competing brand that markets similar products in the franchisee's protected area, is considered another form of franchisor encroachment that the proposed anti-encroachment rule regulates.

Second, this research study has advised that the franchisor should be required to offer reasonable compensation or other remedial forms to offset the franchisee's lost profits before engaging in encroaching conduct. Nevertheless, this thesis has not discussed and exemplified the latter type of remedy. In this respect, legal systems may strive to elaborate on remedial forms, apart from monetary compensation, for the purpose of applying the proposed anti-encroachment rule. For example, legal systems may provide that an income-sharing or profit-sharing arrangement between the franchisor and the existing franchisee is a remedial form in light of the anti-encroachment rule. Legal systems may provide that the franchisor may offer to reduce royalties as a remedial means in light of the rule.

6.4.2 *Duty to assist*

6.4.2.1 *Research findings*

Chapter four has found that the DCFR, the USA, and Australia are similar in that a franchise contract is a primary source of the franchisor's duty to assist. A franchise contract's terms may obligate a franchisor to provide a franchisee with initial assistance, such as setting pre-opening training programs. The contract terms may require the franchisor to provide the franchisee with ongoing assistance, such as providing technical and operational advice and manuals. Nevertheless, this chapter has observed one marked difference among the selected legal systems; that is to say, the DCFR contains a default provision

that establishes the franchisor's duty to assist in the absence of an express agreement. In contrast, in the USA and Australia, the franchisor's duty to assist must be constituted by express terms of a franchise contract. In other words, these two legal systems do not provide a gap-filling mechanism similar to that of the DCFR.

6.4.2.2 Recommendation

This research study has proposed that comprehensive franchise law contains a mandatory provision establishing the franchisor's duty to assist. This provision should require the franchisor to provide the franchisee with three forms of assistance as follows. First, the franchisor should be required to provide the franchisee with initial assistance that adequately assists the franchisee in opening a franchised business. Second, the franchisor should be required to give the franchisee ongoing assistance that adequately and periodically supports the franchisee's business operation. The third form is that the franchisor should be required to respond to the franchisee's reasonable request for specific assistance or support. Additionally, this research study has suggested that the proposed provision of comprehensive franchise law specifies a person who bears the costs of rendering the required assistance or support. In this respect, the rule should provide that the franchisor must be responsible for the costs of providing initial and ongoing assistance. In contrast, the franchisee must bear the expense of providing special assistance.

6.4.2.3 Limitation

There is one limitation on formulating the recommendation mentioned above. As can be seen, this thesis has proposed the establishment of three types of franchisor assistance. In particular, this thesis has suggested the imposition of mandatory initial and ongoing assistance by a franchisor. Nevertheless, this research study has not gone into detail about forms of the required support since they can vary from business to business. Thus, this thesis has advised that the contracting parties clarify the forms of assistance under a franchise agreement. Despite this suggestion, legal systems may set a minimum requirement for rendering the required support by enumerating or exemplifying forms of the franchisor's initial and ongoing assistance common to all franchise businesses. For instance, legal systems may require the franchisor to provide the franchisee with initial support in the form of training and advertising. Legal systems may obligate the franchisor to give technical and operational advice during a franchise relationship. These listed assistance forms will establish minimum requirements that the franchisor must provide to the franchisee.

6.4.3 Private law remedies

6.4.3.1 *Research findings*

This research study has found that general contract law rules provide legal mechanisms that permit an aggrieved franchisee to enforce the franchisor's performance of the ongoing obligations, claim damages, and cancel a franchise contract. In this case, it is common that the franchisee needs to establish that a franchise contract imposes the duty not to encroach and the duty to assist on the franchisor and the franchisor fails to perform these obligations. In other words, if a franchise contract does not obligate the franchisor to refrain from encroaching upon the franchisee's business or assist the franchisee in the operation of a franchised business. The franchisee will not be able to resort to the three contract law remedies in the first place.

The fourth chapter has also discovered that the USA and Australia differ from the DCFR in the case of franchisor encroachment. That is, an aggrieved franchisee may enforce the franchisor's performance, claim damages, and cancel a franchise contract under statutes because the franchisor's encroachment is regulated statutorily. Nevertheless, the USA differs from Australia in that an aggrieved franchisee may seek statutory remedies under franchise relationship law. In this case, the franchisee usually needs to plead that the franchisor's encroaching conduct violates anti-encroachment or anti-unfair competition rules under relationship law. Conversely, in Australia, the franchisee has to seek statutory remedies under the competition and consumer legislation. In seeking the remedies, the franchisee has to prove that the franchisor's encroaching conduct is regarded as unconscionable conduct prohibited by the legislation.

6.4.3.2 *Recommendation*

As mentioned earlier, this research study has proposed the regulation of the franchisor's duty not to encroach and the duty to assist under comprehensive franchise law. Based on this proposal, this research study has also suggested that comprehensive franchise law establish a remedial regime providing legal mechanisms for an aggrieved franchisee to employ in the event of the franchisor's contravention of the regulation. Under the remedial system, an aggrieved franchisee should be permitted to seek the enforcement of the franchisor's performance, recovery of damages, and cancellation of a franchise contract. The first remedy should confer on the franchisee the right to compel the franchisor to do or not to do something that the rules of comprehensive franchise law require. The remedy of damages should allow the franchisee to recover money for the loss sustained. The third remedy should provide a mechanism that enables the franchisee to discharge a franchise relationship.

6.4.3.3 *Limitation*

This research study has proposed the establishment of the three remedial mechanisms with the limitations mentioned in subsection 6.3.3.3. There is another limitation in this chapter. This thesis has yet to discuss the possibility of including rules on alternative dispute resolution in comprehensive franchise law. This research study acknowledges that many franchisees may be prevented from seeking remedies under the law against a franchisor because they cannot pay the prohibitive cost of litigation. Moreover, a franchisor may manage to prevent franchisees from joining class-action lawsuits against the franchisor to seek remedies. In this respect, making remedies available for franchisees may be in vain; hence, the law may need to think of other forms of settling a dispute between the franchisor and the franchisees. However, providing dispute resolution options for a franchisee is an important issue that deserves more space to discuss. Thus, the discussion has not been made in this research study.

6.5 REGULATION OF TRANSFER, NON-RENEWAL, AND TERMINATION OF A FRANCHISE CONTRACT

6.5.1 Transfer of a franchise contract

6.5.1.1 *Research findings*

Under the franchise legal framework of the DCFR, the USA, and Australia, chapter five has discovered two approaches to regulating the franchisor's unreasonable consent to a transfer of a franchise contract.

First, under the DCFR and most US jurisdictions, a franchise contract's terms will primarily regulate the requirement of the franchisor's consent to the transfer. Under the contract terms, the franchisor usually retains the right to withhold consent to the transfer. In this case, however, courts may concretize the principle of good faith and fair dealing in order to control the franchisor's withholding consent by requiring the franchisor not to withhold its consent unless the franchisor has legitimate grounds for doing so.

The second approach is utilized by the US transfer states and Australia. These jurisdictions introduce transfer rules of franchise relationship law regulating the franchisor's consent to a transfer by a franchisee. Under the regulation, the franchisor cannot refuse to consent to the transfer unless the franchisor has grounds for withholding its consent, such as the unacceptability or unqualification of the proposed transferee and good cause.

6.5.1.2 Recommendation

This research study has proposed that comprehensive franchise law contains transfer provisions regulating a transfer of a franchise contract by a franchisee, which should be effectuated by the franchisor's consent. In this case, the transfer rules should play the two roles as follows.

First, the rules should regulate the procedure for obtaining the franchisor's consent to a transfer of a franchise contract. That is, the rules should require a transferring franchisee to give a franchisor written notice of transfer. The written notice should contain material information about the proposed transferee, including the transferee's name and address, statement of financial qualification, and business experience during a previous 5 year. Upon receipt of the notice, the franchisor should be required to notify the franchisee of its decision in writing within 30 calendar days. In this case, the franchisor should be taken to have consented to the transfer if the franchisor fails to notify the franchisee of its decision.

The second role of the transfer rules is to restrict the franchisor's ability to withhold consent to a transfer. The franchisor should be required to have reasonable grounds for withholding consent to a transfer. The grounds for withholding consent should include the commercial unacceptability of the prospective transferee. The determinants of the unacceptability of the transferee should include three facts as follows. First, the prospective transferee is a competitor of the franchisor. Second, the transferee does not meet the franchisor's financial criteria for franchisees. Third, the transferee lacks sufficient business experience to operate a franchised business. Nevertheless, the grounds for withholding consent mentioned earlier are not complete. The rules should allow a franchisor to withhold its consent to a transfer based on other commercial grounds.

Besides the transfer rules, this research study has suggested that comprehensive franchise law contains a provision that constitutes the requirement of good faith. This requirement should obligate both parties to act in good faith in the course of a franchise relationship. In the context of a franchise transfer, the franchisor should be required by good faith and fair dealing not to withhold consent to a proposed transfer capriciously. For example, the franchisor cannot withhold consent to a transfer discriminatorily, except the franchisor has legitimate grounds for the discrimination. Thus, this requirement of good faith and dealing would ensure that the franchisor's withholding consent to a transfer is not abusive to a transferring franchisee.

6.5.1.3 Limitation

There is one limitation concerning the recommendation. This research study has suggested that the franchisor cannot withhold its consent to the franchisee's proposed transfer of a franchise contract unless the franchisor bases its decision

on the commercial unacceptability of a prospective transferee. This ground for withholding consent is not exclusive. The franchisor may argue that it refuses to consent to the transfer for other commercially reasonable grounds. However, this thesis has not thoroughly discussed other possible reasonable grounds for withholding consent. In this case, legal systems may introduce and enumerate reasonable grounds for withholding consent to a transfer, apart from what this research study has proposed, in transfer provisions of comprehensive franchisee law. For example, the franchisor may withhold consent to a transfer of a franchise contract if the franchisee fails to pay outstanding debts or redress defaults triggered before the transfer.

6.5.2 Non-renewal of a franchise contract

6.5.2.1 *Research findings*

Under the franchise legal framework of the DCFR, the USA, and Australia, the fifth chapter has explored two approaches to regulating the franchisor's refusal to renew a fixed-term franchise contract that is about to expire.

The first approach is adopted by the DCFR and the majority of the US states. In these legal systems, general contract law rules will apply to non-renewal of a franchise contract by a franchisor. In general, contract law rules will not prevent the franchisor from refusing to renew a franchise agreement. In exceptional cases, courts may employ the principle of good faith to require the franchisor not to refuse to renew the term of a franchise contract in bad faith. In other words, the requirement of good faith and fair dealing may obligate the franchisor to have legitimate grounds for refusing to renew a franchise agreement.

Second, the seventeen US states and Australia adopt a statutory approach; that is to say, these legal systems regulate the franchisor's non-renewal of a franchise contract through the rules of franchise relationship law. However, the US legal system differs from Australia in that the rules of franchise relationship law explicitly require a franchisor to have legitimate grounds, such as good cause and good faith, for refusing to renew a franchise contract. In contrast, the Australian franchise legislation merely regulates the franchisor's notification of non-renewal of a franchise agreement. In other words, the law does not obligate the franchisor to have any reasonable ground for the non-renewal of a franchise agreement.

6.5.2.2 *Recommendation*

This research study has proposed that comprehensive franchise law contains a renewal provision providing that a franchise contract for a definite period expires on the expiration date. In this case, a franchisor should generally have

freedom not to renew an expiring franchise agreement. Nevertheless, the renewal rule should protect the franchisee's expectations by establishing the procedure for renewing a franchise contract. Under the rule, the franchisee may propose to renew the term of a franchise contract before the current term expires. In proposing to renew, the franchisee should be required to give the franchisor written notice of renewal at least 90 calendar days before the expiration date. Upon receipt of the franchisee's notice, the franchisor should be obliged to inform the franchisee of its decision in writing within 30 calendar days. Suppose the franchisor does not notify the franchisee within 30 calendar days. In this case, the renewal rule should deem the term of an incumbent franchise contract to have been renewed for an indefinite period.

This research study has also suggested that the franchisor's decision not to renew a franchise contract is constrained by the requirement of good faith. As mentioned in subsection 6.5.1.2, this thesis proposes that comprehensive franchise law contains a provision constituting the general duty to act in good faith and fair dealing. This duty will require the franchisor not to refuse to renew a franchise contract for a capricious or opportunistic purpose. For example, the franchisor may be prevented from refusing to renew a franchise agreement with an intention to forfeit the franchisee's local goodwill unfairly. In any case, it should be noted that whether a franchisor refuses to renew a franchise contract in bad faith will be decided on a case-by-case basis.

6.5.2.3 Limitation

There is one limitation regarding the recommendation mentioned above. This research study has suggested that a franchisor cannot refuse to renew the term of a definite franchise contract contrary to the requirement of good faith. In this case, this thesis has exemplified that the principle of good faith and fair dealing may require a franchisor to have reasonable grounds for the non-renewal of a franchise agreement in some exceptional cases. Nevertheless, this research study has not discussed possible situations that the franchisor is required by good faith to give the franchisee reasonable grounds for refusing to renew the agreement. In this respect, legal systems may further elaborate on cases where a franchisor has to provide grounds on the basis of good faith and fair dealing for the non-renewal of a franchise contract. Alternatively, legal systems may leave this issue for courts to develop precedents in the future.

6.5.3 Termination of a franchise contract

6.5.3.1 Research findings

Chapter five has found that the franchisor's termination of a franchise contract with an indefinite term falls within the ambit of general contract law of the

DCFR, the non-termination US states, and Australia. Under contract law regimes, it is common that an indeterminate franchise agreement can be terminated at will or without cause. In other words, the chosen legal systems' contract law rules do not require a franchisor to terminate a franchise contract for justifiable grounds unless the contract provides otherwise. That is, a franchise contract may incorporate terms that require a franchisor to terminate an indefinite franchise contract for the franchisee's breach of contract or in the occurrence of certain circumstances listed under the contract. Nevertheless, the selected legal systems' contract law rules similarly require the franchisor to provide the franchisee with reasonable notice of termination. In this case, the franchisee will be protected in that the franchisor cannot terminate a franchise contract immediately.

The fifth chapter has discovered that the US termination states employ the rules of franchise relationship law to regulate the franchisor's termination of a franchise contract with a definite term. In terminating a franchise contract, the termination rules require the franchisor to follow the procedural requirements for terminating the contract. Furthermore, the rules require the franchisor to have legitimate grounds for the termination of a fixed term franchise contract. Chapter five has explored that the Australian franchise legislation also regulates the franchisor's termination of a fixed-term franchise agreement. However, the Australian legal system differs from the US in that franchise relationship law does not require the franchisor to terminate the agreement for justifiable causes. Instead, the law merely contains provisions regulating the procedure for terminating a franchise agreement.

6.5.3.2 *Recommendation*

This research study has proposed that comprehensive franchise law contains provisions regulating termination of a franchise agreement by the parties, including a franchisor. However, the law should provide termination rules regulating termination of a franchise contract for an indefinite period, which are different from those regulating termination of a franchise contract for a definite period. In the former case, the termination rules should permit the parties to terminate an indefinite franchise agreement for any reason or even for no reason. Nevertheless, the rules should allow a terminating party to terminate a franchise contract only after the contract has lasted for a reasonable period. In terminating a franchise contract, the terminating party should be required to give the other party written notice of termination for a reasonable period before the termination is effectuated. Conversely, in the latter case, the termination rules should not permit the parties to terminate a franchise contract with a fixed term before it expires unless the parties have legitimate grounds for terminating the contract. The grounds for termination should be divided into material non-performance of an obligation and other commercial reasons.

In terminating a franchise contract for material non-performance, the terminating party should be required to allow the other party to cure the alleged material non-performance by giving written notice specifying a reasonable manner by which the non-performance is cured and a reasonable period of not less than 15 calendar days for the correction. In this case, the franchise contract should be terminated automatically if the notified party fails to cure the non-performance within the specified period. However, if the alleged material non-performance is incurable, the terminating party may terminate a franchise contract, by giving the other party written notice of termination with immediate effect.

In terminating a franchise contract for other commercial reasons, the termination rules should require the parties to terminate the contract only for reasons that are of commercial significance. An example of significant commercial reasons is that a franchisor may terminate a franchise contract if the franchisor intends to withdraw from the market entirely. When intending to terminate the contract, the terminating party should give the other party written notice of termination for a reasonable period before the termination is effective. In the notice, the terminating party should provide the other party with the reasons on which the proposed termination is based for the evidence's sake.

Besides the proposed termination rules, this research study has advised that the terminating party should also be required to act in accordance with the requirement of good faith when intending to terminate a franchise contract. Since this thesis has proposed the establishment of a general duty to act in good faith and fair dealing, this obligation would require the parties to a franchise contract not to terminate the contract capriciously, which should be determined on a case-by-case basis. For example, the principle of good faith and fair dealing may prevent the franchisor from engaging in discriminatory termination of a franchise agreement.

6.5.3.3 Limitation

There is one caveat with regard to the recommendation mentioned above. This research study has proposed that the parties are permitted to terminate a franchise contract for commercially significant reasons by giving reasonable notice. As can be seen, the standard of commercial significance seems to be elusive. This thesis has exemplified only one case, namely the franchisor's termination of a franchise contract for an entire market withdrawal reason. In this respect, there may be more cases of the parties' termination for other commercially significant reasons. Nevertheless, this research study has not had space to discuss those examples. Thus, legal systems may elaborate on the circumstances under which the parties can terminate a franchise contract for commercially significant reasons or allow courts to decide on a case-by-case basis. Alternatively, a franchisor and a franchisee may strive to enumerate

the events in which a franchise contract can be terminated based on this standard.

6.5.4 Private law remedies

6.5.4.1 *Research findings*

Chapter five has discovered that the DCFR, the USA, and Australia allow an aggrieved franchisee to enforce the franchisor's performance, claim damages, and cancel a franchise agreement through general contract law mechanisms. In these cases, the franchisee needs to establish that the terms of a franchise agreement constitute the franchisor's obligations regarding transfer, non-renewal, and termination of a franchise contract, and the franchisor fails to perform these obligations. The selected legal systems may differ in terms of detailed rules and principles governing each remedy. In addition, the fifth chapter has found that the USA and Australia markedly differ from the DCFR in that those former two legal systems permit an aggrieved franchisee to seek the enforcement of the franchisor's performance and the recovery of damages under specific statutes. Besides, Australia allows the franchisee to request statutory rescission to cancel a franchise agreement. In any case, however, the franchisee needs to prove that there are franchise-specific law rules regulating the franchisor's conduct relating to transfer, non-renewal, and termination of a franchise contract, and the franchisor violates those rules.

Chapter five has also discovered that the DCFR, the USA, and Australia are similar in that an aggrieved franchisee can reimburse for the value of tangible and intangible assets upon the cessation of a franchise relationship, provided that the terms of a franchise contract confer on the franchisee the right to do so. In this case, the terms of a franchise contract may entitle the franchisee to seek the franchisor's repurchase of the remaining stocks, supplies, inventory, and equipment upon the termination of a franchise contract. Furthermore, the terms of a franchise agreement may entitle the franchisee to indemnify for the value of its local goodwill when a franchise relationship is ended. Additionally, the fifth chapter has explored that the DCFR and the USA have franchise-specific law rules that constitute the franchisee's right to seek these two special remedies. Nevertheless, the DCFR differs from the USA in that the rules are made by default; hence, the parties may agree to exclude or deviate from the effect of the rules.

6.5.4.2 *Recommendation*

As mentioned earlier in subsections 6.3.3.2 and 6.4.3.2, this research study has proposed that comprehensive franchise law establishes a remedial system that enables an aggrieved franchisee to seek the following three private law

remedies: (1) enforcement of the franchisor's performance of pre-contractual information duties, (2) recovery of damages, and (3) cancellation of a franchise contract. Thus, chapter five comes up with the same recommendation. Nevertheless, in the context of the cessation of a franchise relationship, this research study has suggested that comprehensive franchise law may contain remedial provisions constituting the franchisee's right to repurchase and the right to compensation for goodwill as distinct remedial rights. This thesis has also advised that the remedial provisions establish, at least, the following three elements. First, the rules should specify the events that trigger the franchisor's obligations to repurchase and compensate for the value of goodwill. Second, the rules should identify the assets, the value of which is to be indemnified. Third, the rules should provide a clear standard for assessing the value of the properties to be reimbursed.

6.5.4.3 *Limitation*

There is a caveat concerning the recommendation of the establishment of the franchisee's specific remedial rights mentioned above. As can be seen, this research study has suggested that legal systems may decide to include remedial provisions constituting the franchisee's right to repurchase and the right to compensation for goodwill in comprehensive franchise law's remedial system. If legal systems choose so, this thesis has advised the legal systems to be explicit as regards the three components: the triggering events, the franchisee's assets whose value will be reimbursed, and the assessment standard. Nevertheless, this thesis has not discussed each element in detail. In other words, this research study has left the task of deciding on legal systems to elaborate on the detailed requirements of all components. For example, concerning the first element, legal systems may provide that the franchisor's duty to repurchase is triggered when a franchise contract is prematurely terminated. Conversely, the franchisor's duty to reimburse for goodwill is triggered upon the cessation of a franchise contract, regardless of whether the contract is ended by termination. In any event, legal systems may vary in these cases.

6.6 CONCLUSIONS AND EPILOGUE

The regulation of franchisor opportunism will not be complete and uniform if legal systems do not introduce franchise-specific law that contains rules regulating the whole life of a franchise life cycle. In other words, franchise-specific law should be comprehensive in that it regulates the franchisor's opportunistic conduct in the three stages of a franchise relationship: a pre-contractual franchise relationship, an ongoing franchise relationship, and an end of a franchise relationship. This thesis has conducted a comparative law study of the franchise legal framework of the DCFR, the USA, and Australia

to assist legal systems in introducing comprehensive franchise law regulating franchise opportunism in the course of a franchise relationship to protect a weaker franchisee. In order to provide legal systems with practical examples, this thesis will, in the following paragraphs, translate the recommendations on the proposed franchise rules made in the preceding sections into a list of fourteen model provisions of comprehensive franchise law.

MODEL PROVISIONS OF COMPREHENSIVE FRANCHISE LAW

Article 1 (Definitions)

For the purpose of this comprehensive franchise law:

Franchise means a legal relationship established by a franchise contract.

Franchise contract means a contract in which:

- (1) The franchisor grants the franchisee (a) the right to conduct a franchise business independently, following the franchisor's business method, and (b) the right to use the franchisor's marks, including trademarks and trade names, in the operation of a franchised business for a definite or an indefinite period.
- (2) The franchisee pays or agrees to pay the franchisor monetary considerations in exchange for granting the rights mentioned in (1)(a)(b).

Franchisor means a person who enters into a franchise contract as the franchisor.

Franchisee means a person who enters into a franchise contract as the franchisee.

Prospective franchisee means a person who approaches, or is approached by, the franchisor for a franchise.

Article 2 (Form of a franchise contract)

- (1) A franchise contract must be made in writing.
- (2) A franchise contract that does not comply with the requirement imposed by (1) is unenforceable.

Article 3 (Duty to act in accordance with good faith)

- (1) The parties to a franchise contract must act towards the other party in accordance with good faith in performing an obligation or in exercising a right under a franchise contract and the rules of comprehensive franchise law.
- (2) The duty to act in accordance with good faith imposed by (1) also applies to the performance of an obligation or the exercise of a right in a pre-contractual stage.
- (3) The duty to act in accordance with good faith in (1) and (2) cannot be excluded or limited by agreement.

Article 4 (Duty of disclosure)

- (1) The franchisor must provide the prospective franchisee with a disclosure document, which is reasonably accessible by the prospective franchisee, at least one month

before (a) the conclusion of a franchise contract or (b) the payment to the franchisor by the prospective franchisee of monetary considerations.

- (2) A disclosure document must contain information that sufficiently provides insights into the franchisor's identity, the franchise system, the franchise business, and the fundamental rights and obligations under a franchise contract.
- (3) The franchisor may provide the prospective franchisee with an electronic disclosure document on the condition that the franchisor (a) creates an electronic disclosure document in a durable format, (b) asks for the prospective franchisee's prior consent to the provision of an electronic disclosure document and (c) consults the prospective franchisee of relevant preconditions for reviewing an electronic disclosure document.

Article 5 (Duty to provide complete, current and accurate information)

The franchisor must ensure that the information required to provide by Article 4(2) is current, complete, and accurate at the date of the disclosure.

Article 6 (Encroachment)

The franchisor may (a) operate or authorize other franchisees to operate a franchised business within a reasonable area of the existing franchisee's business or (b) engage in any conduct that triggers or is likely to trigger competition between the franchisor and the franchisee within a reasonable area of the existing franchisee's business provided that the franchisor has offered the existing franchisee the right to operate the new outlet within a reasonable area of the franchisee's business or the franchisor has offered reasonable compensation or other forms of consideration to offset, in whole or in part, lost profits to be caused by the conduct in (a) or (b).

Article 7 (Assistance and support)

- (1) The franchisor must provide the franchisee with (a) initial assistance that is necessary for the opening of the franchised business and (b) ongoing assistance that is necessary for the operation of the franchised business. In this case, the franchisor must bear the costs associated with the provision of the initial and ongoing assistance.
- (2) The franchisor must be responsive to the franchisee's reasonable request for special assistance. In this case, the franchisee must bear the costs associated with the provision of the special assistance.

Article 8 (Transfer of a franchise)

- (1) A transfer of a franchise must be effectuated by the franchisor's consent. For the purpose of this Article, a transfer of a franchise includes a situation in which the franchisee's rights and obligations under a franchise contract are transferred to the proposed transferee during the term of the contract.
- (2) The franchisee may request consent to a transfer by giving the franchisor written notice of an intention to transfer. The notice of transfer must include, but is not limited to, information about the name and address of the proposed transferee,

statement of financial qualification, and business experience during the previous 5 years. Upon receipt of the franchisee's notice, the franchisor may require more relevant information about the proposed transferee.

- (3) Within 30 calendar days after receipt of the notice, the franchisor must give written notice to the franchisee, informing the franchisee whether the franchisor consents to the proposed transfer. The franchisor is deemed to have consented if the franchisor fails to notify the franchisee in writing within a specified period.
- (4) The franchisor must have reasonable grounds for withholding consent to a transfer. The reasonable grounds for withholding consent include, but are not limited to, the commercial unacceptability of the proposed transferee.
- (5) The commercial unacceptability of the proposed transferee may be determined by the fact that the proposed transferee is a competitor of the franchisor; the proposed transferee faces financial difficulties, and the proposed transferee lacks sufficient business experience.

Article 9 (Renewal of a franchise contract)

- (1) A franchise contract with a definite term is extinguished at the end of the agreed period. Nevertheless, the term of the contract may be renewed by virtue of paragraph (2).
- (2) The franchisee may give the franchisor written notice of its wish to renew at least 90 calendar days before the date of the expiry of the contract. Upon receipt of the franchisee's notice, the franchisor must notify the franchisee of its intention in writing within 30 calendar days. If the franchisor fails to notify the franchisee of its intention within a specified period, the term of the contract is deemed to have been renewed for an indefinite period.

Article 10 (Termination of a franchise contract with an indefinite term)

- (1) A party to a franchise contract with an indefinite term may terminate the contract by giving the other party written notice under the conditions set out in paragraph (2).
- (2) A party may terminate a franchise contract with an indefinite term only after an existing franchise relationship has existed for a reasonable period. When intending to terminate the contract, the terminating party shall give notice to the other party a reasonable period before the termination is effective.

Article 11 (Termination of a franchise contract with a definite term)

- (1) A party may terminate a franchise contract with a definite term for the other party's material non-performance of an obligation.
- (2) When intending to terminate the contract in (1), the terminating party must allow the other party to cure an alleged non-performance. In this case, the terminating party must give the other party written notice of termination. In the notice, the terminating party must specify a reasonable manner in which the other party may cure the alleged non-performance. Besides, the terminating party must fix a reasonable period of not less than 15 calendar days after receipt of the notice for the cure.

If the other party fails to cure the alleged non-performance within a specified period, the contract is automatically terminated.

- (3) The terminating party may not allow the other party to cure by virtue of (2) if the alleged non-performance is incurable, considering the circumstances of the case. In this case, the terminating party may terminate a franchise contract by giving the other party written notice of termination with immediate effect.
- (4) A party may terminate a franchise contract with a definite term for reasons other than material non-performance of an obligation of the other party insofar as the reasons for termination are of commercial significance.
- (5) When intending to terminate the contract, the terminating party must give the other party a written notice of termination for a reasonable period before the termination is effective. In the notice, the terminating party must include the reasons on which the proposed termination is based.

Article 12 (Remedy of enforcement)

- (1) If the franchisor fails to comply with the rules of comprehensive franchise law, the franchisee may enforce the franchisor's performance, which conforms to the rules.
- (2) The enforcement of the franchisor's performance in (1) is not permitted if enforcing the franchisor's performance would be unlawful or unreasonably burdensome.

Article 13 (Remedy of damages)

- (1) If the franchisor fails to comply with the rules of comprehensive franchise law, the franchisee may claim damages for recoverable loss caused by the franchisor's non-compliance with the rules.
- (2) The recoverable loss means financial or economic loss, such as expenses or burdens incurred, loss of incomes or profits, and a reduction of the value of assets.

Article 14 (Remedy of repurchase and compensation of goodwill)

- (1) Upon the cessation of a franchise, the franchisee is entitled to (a) the repurchase of the remaining stock, spare parts, inventory, supplies, equipment, and furnishings bought from the franchisor or the franchisor's approved supplier and (b) compensation for the value of the franchisee's goodwill on the condition that the franchisee is restricted by a non-compete agreement.
- (2) The franchisor must repurchase the items specified in (a) or compensate for the franchisee's goodwill in (b) at the fair market value.

In the end, this doctoral thesis is not a complete picture of how franchisor opportunism is to be regulated by law rules. In other words, this thesis has left much room for future research on several issues. As can be seen, this research study has focused on proposing substantive private law rules regulating franchisor opportunism. In this case, there are opportunities for researching public law mechanisms, which could reinforce the rules of comprehensive

franchise law. For instance, this research study has proposed the imposition of the franchisor's duty to disclose pre-contractual information, which is current and accurate, to a prospective franchisee. One may conduct research on how public law rules set up mechanisms that enable the franchisee to check the currentness and veracity of the information. Furthermore, this doctoral thesis is genuinely law literature; it has contributed literature on the regulation of franchisor opportunism in a franchise relationship from a legal perspective. Hopefully, this thesis's proposals can seed empirical legal research that tests the thesis's proposal through quantitative or qualitative legal analysis. Strictly speaking, one may be interested in researching whether and the extent to which the proposed model provisions under comprehensive franchise law protect a weaker franchisee against franchisor opportunism from socio-legal and economic viewpoints. Future research studies on these issues would add pieces of jigsaw to build a comprehensive picture of the regulation of franchisor opportunism in a franchise relationship.

Summary

Chapter 1: Introduction

Chapter one sets the framework of this PhD dissertation. This chapter first identifies that a franchise is a contractual relationship created by a franchise contract between a franchisor and a franchisee to distribute the franchisor's goods or services to the market through the franchised business operation. Although a franchisor and a franchisee are business persons, a franchise relationship is ordinarily asymmetrical because the franchisor holds greater informational and bargaining power than the franchisee. This asymmetrical relationship increases the likelihood of franchisor opportunism. A franchisor may unfairly treat a franchisee in the three stages of a franchise life cycle, from a pre-contractual stage of a franchise relationship to the end of the relationship. The franchisor's unfair or opportunistic conduct would cause the franchisee economic loss or damage.

Based on that assumption, chapter one develops an overarching research question:

Which franchise-specific law rules should be formulated to regulate the franchisor's opportunistic conduct?

In answering the research question, the first chapter indicates that this dissertation utilizes legal-dogmatic research with a comparative law method as a research methodology. This dissertation examines and juxtaposes the franchise legal framework of the European Draft Common Frame of Reference (DCFR), the United States of America (USA), and Australia to extract legal approaches to the problem. This dissertation discusses the extracted solutions to propose guidelines for formulating private law rules under comprehensive franchise legislation regulating franchisor opportunism in the three stages of a franchise relationship to protect franchisees.

Chapter 2: Definition and essential elements of a franchise

Chapter two explores the definition of a franchise. Defining a franchise will demarcate a franchise relationship from other legal relationships for the purpose of regulation. The second chapter proposes that the conclusion of a franchise contract by the franchisor and the franchisee establishes a franchise

relationship under comprehensive franchise law. Comprehensive franchise law should understand a franchise contract as a marketing contract with the following three fundamental elements: (1) the franchisor's grant of the right to conduct a franchise business, (2) the franchisor's license to use the franchisor's marks, and (3) the franchisee's payment of franchise fees. Chapter two also suggests that comprehensive franchise law regulates the formality of making a franchise contract. A franchise contract should be made in writing; otherwise, the contract is unenforceable.

Chapter 3: Regulation of pre-contractual information obligations of the franchisor

Chapter three examines the regulation of the franchisor's pre-contractual information duties. In the pre-contractual stage, a franchisor may opportunistically withhold or distort essential information about a franchisor and a franchise system; hence, a franchisee needs legal protection in this phase. The third chapter proposes that comprehensive franchise law establishes the franchisor's disclosure obligation. Comprehensive franchise law should require the franchisor to provide the prospective franchisee with a disclosure document, which is reasonably accessible by the franchisee, at least one month before (1) the conclusion of a franchise contract or (2) the franchisee's payment of monetary considerations. Comprehensive franchise law should prescribe that a disclosure document contains essential information about the franchisor, the franchise system, the franchise business, and the fundamental rights and obligations under a franchise contract.

Chapter three also proposes that comprehensive franchise law imposes the duty to provide complete, current and accurate information on the franchisor. The law should require the franchisor to ensure that the information included in a disclosure document is current, complete, and accurate at the date of the disclosure. In the end, the third chapter suggests that comprehensive franchise law constitutes a remedial regime. Under the remedial system, the franchisor's failure to perform these pre-contractual duties provides the franchisee with a legal ground for enforcing the franchisor's performance, claiming monetary compensation for loss or damage, and canceling a franchise contract.

Chapter 4: Regulation of the franchisor's ongoing obligations

Chapter four examines the regulation of franchisor encroachment and the franchisor's provision of assistance. During an ongoing relationship, a franchisor may cannibalize franchisees' franchised business by engaging in territorial encroachment in traditional or non-traditional forms. A franchisor may open a new company-own franchised outlet or license other new franchisees to operate a franchised store in close proximity to an existing franchisee's business. A franchisor may also distribute its goods or services through alternative

distribution channels, such as online sales, which compete with the franchisee's business. The fourth chapter proposes that comprehensive franchise law regulates the franchisor's encroaching conduct to protect franchisees. The franchisor may engage in those encroaching practices provided that the franchisor has offered the franchisee the right of first offer or reasonable compensation or other remedial forms to offset the franchisee's potential lost profits caused by the franchisor's encroachment.

A franchisor may not appropriately assist and support franchisees in opening and operating franchised businesses. In this case, chapter four proposes that comprehensive franchise law establishes the franchisor's duty to assist. The law should require the franchisor to provide the franchisee with initial and ongoing assistance, which is vital for launching and running a franchised business. The franchisor should be obliged to respond to the franchisee's reasonable request for support during the operation of a franchised business. Comprehensive franchise law should also designate a person who bears the costs of rendering the assistance. The franchisor should bear the costs of providing the franchisee with initial and ongoing assistance. The franchisee should reimburse the franchisor for expenses spent in providing tailor-made support. In the end, chapter four advises that the remedial system provides an aggrieved franchisee with mechanisms to compel the franchisor's performance of the duties, claim damages for the franchisor's non-performance, and cancel a franchise agreement.

Chapter 5: Regulation of transfer, non-renewal, and termination of a franchise contract

Chapter five explores the regulation of franchisor opportunism related to a franchise transfer by a franchisee and a franchisor's non-renewal and termination of a franchise contract.

First, a franchisor may abuse a franchisee by withholding consent to the proposed transfer of a franchise. To protect a franchisee, chapter five proposes that comprehensive franchise law regulates the procedure for transferring a franchise by a franchisee. Furthermore, the law should constrain the franchisor's consent to a transfer. The law should require the franchisor to have reasonable grounds for withholding consent to a transfer and to withhold its consent in accordance with good faith.

Second, a franchisor may not renew an expiring franchise contract to the detriment of a franchisee's legitimate interests. The fifth chapter proposes that comprehensive franchise law sets the notice procedure that permits a franchisee to request the renewal of the term of a franchise agreement. The law should also require the franchisor to act in good faith when refusing to renew the agreement.

Third, a franchisor may terminate a franchise contract, inflicting a financial loss on a franchisee's business. Chapter five proposes that comprehensive franchise law regulates termination of a franchise contract through termination

rules. These rules apply to termination of the contract by both parties. The rules should require a party to a franchise contract with an indefinite term to terminate the contract by giving the other party written notice of termination for a reasonable period before the termination is effectuated. The rules should require a party to a franchise contract with a definite term to prematurely terminate the contract only for legitimate grounds, including the other party's material non-performance of an obligation and other compelling commercial reasons.

The fifth chapter also advises that the remedial system of comprehensive franchise law establishes the franchisee's right to repurchase and the right to compensation for goodwill as the remedial rights distinct from other private law remedies suggested in this dissertation. Upon the cessation of a franchise relationship, the franchisee should be entitled to ask the franchisor to repurchase the remaining stock, spare parts, inventory, supplies, equipment, and furnishings bought from the franchisor or the franchisor's approved supplier. The franchisee should also be entitled to compensation for the value of the franchisee's goodwill, provided that the franchisee is restricted by a non-compete agreement.

Chapter 6: Conclusion

Chapter six concludes the PhD dissertation by recapitulating research findings in each chapter, summarizing recommendations for formulating private law rules under comprehensive franchise law, and pointing out caveats with regard to the findings and recommendations in this research study. The sixth chapter also offers a list of the model provisions of comprehensive franchise law to exemplify the dissertation's proposals for the benefit of utilization by legal systems. Chapter six ends the dissertation with issues for future research.

Samenvatting (Dutch summary)

EEN JURIDISCH KADER VOOR FRANCHISING

Een vergelijkende studie van het Europese Draft Common Frame of Reference (DCFR), het Amerikaanse recht en het Australische recht inzake franchiseovereenkomsten

Hoofdstuk 1: Inleiding

Hoofdstuk 1 schetst het kader van dit proefschrift. Allereerst wordt vastgesteld dat franchise een contractuele relatie is tussen een franchisegever en een franchisenemer om goederen of diensten van de franchisegever via de door de franchisenemer geëxploiteerde franchiseformule te distribueren. Hoewel franchisegever en franchisenemer allebei ondernemers zijn, is een franchise-relatie gewoonlijk asymmetrisch; de franchisegever beschikt immers over meer informatie en onderhandelingsmacht dan de franchisenemer. Deze asymmetrische relatie vergroot de kans op opportunistisch gedrag van de franchisegever. De kans bestaat dat een franchisegever een franchisenemer oneerlijk behandelt, in de drie fasen van een franchiseovereenkomst: van de precontractuele fase tot het einde van de relatie. Oneerlijk of opportunistisch gedrag van de franchisegever kan de franchisenemer economisch verlies of schade berokkenen.

Op basis van deze veronderstelling wordt in hoofdstuk 1 een overkoepelende onderzoeksvraag ontwikkeld:

Welke specifiek voor de franchiseovereenkomst geldende rechtsregels zouden moeten worden geformuleerd om opportunistisch gedrag van de franchisegever te reguleren?

Deze vraag wordt beantwoord op grond van juridisch-dogmatisch en rechtsvergelijkend onderzoek. In dit proefschrift worden de juridische kaders van het Europese Draft Common Frame of Reference (DCFR), de Verenigde Staten van Amerika (VS) en Australië onderzocht en vergeleken, met het doel diverse benaderingen van de problematiek in kaart te brengen. De gevonden oplossingen worden onderzocht om richtlijnen te kunnen aandragen voor het opstellen van privaatrechtelijke, specifiek op franchise gerichte, wetgeving in de drie fasen van een franchiserelatie, ter bescherming van de franchisenemer tegen opportunisme van de franchisegever.

Hoofdstuk 2: Definitie en essentiële elementen van een franchise

Hoofdstuk 2 onderzoekt de definitie van franchise. Het definiëren van franchise zorgt ervoor dat de franchiseovereenkomst, met het oog op regelgeving, kan worden afgebakend van andere rechtsverhoudingen. Een franchiseovereenkomst wordt omschreven als een overeenkomst met de volgende drie fundamentele elementen: (1) de verlening door de franchisegever van het recht om een franchisevestiging te exploiteren, (2) de licentie van de franchisegever om de kenmerken van de franchisegever te gebruiken, en (3) de betaling door de franchisenemer van franchisevergoedingen. Voorgesteld wordt om in de franchisewetgeving te bepalen dat een franchiseovereenkomst een formeel contract is; een franchiseovereenkomst moet schriftelijk worden gesloten en is anders niet afdwingbaar.

Hoofdstuk 3: Regulering van de precontractuele informatieverplichtingen van de franchisegever

Hoofdstuk 3 gaat in op het reguleren van de precontractuele informatieverplichtingen van de franchisegever. In de precontractuele fase kan een franchisegever essentiële informatie over zichzelf en over het franchisesysteem achterhouden of verdraaien. Om de franchisenemer hiertegen te beschermen, wordt voorgesteld om een informatieplicht van de franchisegever neer te leggen in wetgeving. Daarin dient te staan dat de franchisegever de aspirant-franchisenemer informatie moet verstrekken, vastgelegd in een document dat voor de franchisenemer redelijkerwijs toegankelijk is; dit document moet hem worden verstrekt ten minste één maand vóór (1) de sluiting van een franchiseovereenkomst of (2) de betaling van een geldelijke vergoeding door de franchisenemer. Ook moet de wet voorschrijven dat dit informatiedocument essentiële informatie bevat over de franchisegever, de franchiseformule, de franchiseonderneming en de voornaamste rechten en verplichtingen die voortvloeien uit de franchiseovereenkomst.

Bovendien dient de wet de franchisegever een verplichting op te leggen er zorg voor te dragen dat de precontractuele informatie actueel, volledig en nauwkeurig is op de datum waarop zij wordt verschaft. Tot slot wordt in dit hoofdstuk voorgesteld om sancties voor de schending van de informatieplichten in de wet op te nemen. Het niet-nakomen door de franchisegever van zijn precontractuele verplichtingen levert voor de franchisenemer een rechtsgrond op om nakoming te vorderen, een geldelijke vergoeding voor verlies of schade te eisen of de franchiseovereenkomst te beëindigen.

Hoofdstuk 4: Regulering van de verplichtingen van de franchisegever gedurende de looptijd van de overeenkomst

Hoofdstuk 4 gaat in op het reguleren van concurrentie door de franchisegever en het verlenen van bijstand door de franchisegever. De franchisegever kan, op traditionele of niet-traditionele wijze, de franchisenemer concurrentie aandoen in diens verzorgingsgebied en daardoor de activiteiten van de franchisenemer kannibaliseren. Een franchisegever kan een nieuwe eigen franchisevestiging openen of andere nieuwe franchisenemers het recht verlenen om een franchisevestiging te exploiteren in de nabijheid van de vestiging van een bestaande franchisenemer. Een franchisegever kan zijn goederen of diensten ook distribueren via alternatieve distributiekkanalen, zoals onlineverkoop, die concurreren met het bedrijf van de franchisenemer. De franchisewetgeving dient dergelijk inbreukmakend gedrag van de franchisegever te normeren ter bescherming van de franchisenemer. De franchisegever mag de franchisenemer weliswaar concurrentie aandoen, maar hij dient de franchisenemer compensatie aan te bieden voor diens potentiële winstderving. Hij kan bijvoorbeeld de franchisenemer het recht geven om als eerste een franchisevestiging in een bepaald verzorgingsgebied over te nemen, of hem een financiële compensatie aanbieden.

Het komt voor dat een franchisegever de franchisenemer niet op passende wijze bijstaat en ondersteunt bij het openen en exploiteren van de franchiseonderneming. Daarom wordt voorgesteld om de verplichting om bijstand te verlenen wettelijk te verankeren. De wet dient de franchisegever te verplichten de franchisenemer initiële en permanente bijstand te verlenen, welke bijstand van vitaal belang is voor het opstarten en exploiteren van een franchiseonderneming. De franchisegever wordt verplicht te reageren op een redelijk verzoek om ondersteuning van de franchisenemer tijdens de exploitatie van diens onderneming. De wet dient ook te bepalen wie de kosten van het verlenen van de bijstand draagt. De franchisegever dient de kosten van de initiële en permanente bijstand aan de franchisenemer te dragen, terwijl de franchisenemer aan de franchisegever de kosten voor ondersteuning op maat dient te vergoeden. Tot slot wordt in hoofdstuk 4 geadviseerd dat het stelsel van rechtsmiddelen een benadeelde franchisenemer mechanismen biedt om de nakoming van de verplichtingen door de franchisegever af te dwingen, schadevergoeding te vorderen wegens niet-nakoming door de franchisegever, en een franchiseovereenkomst te beëindigen.

Hoofdstuk 5: Regulering van overdracht, niet-verlenging en beëindiging van een franchiseovereenkomst

Hoofdstuk 5 verkent hoe wetgeving de franchisenemer kan beschermen tegen opportunistisch gedrag van de franchisegever bij de overdracht door de

franchisenemer van diens onderneming en bij de niet-verlenging en beëindiging van een franchiseovereenkomst door de franchisegever.

In de eerste plaats kan de franchisegever de belangen van de franchisenemer schaden door geen toestemming te geven voor de voorgestelde overdracht van de door hem geëxploiteerde franchisevestiging. Ter bescherming van de franchisenemer dient de procedure voor de overdracht wettelijk te worden geregeld. Bovendien moet de wet het vereisen van toestemming van de franchisegever voor een overdracht aan banden leggen. De franchisegever dient redelijke gronden te hebben om zijn toestemming voor een overdracht te weigeren en hij kan deze toestemming alleen te goeder trouw weigeren.

Ten tweede kan de franchisegever de belangen van de franchisenemer schaden door een aflopende franchiseovereenkomst niet te vernieuwen. In de wet dient een procedure te worden opgenomen op grond waarvan een franchisenemer om verlenging van de looptijd van een franchiseovereenkomst kan verzoeken. Ook dient te worden bepaald dat de franchisegever verplicht is om bij zijn beslissing over dit verzoek te goeder trouw te handelen.

Ten derde kan de franchisegever de franchiseovereenkomst opzeggen, waardoor de franchisenemer financieel verlies lijdt. Voorgesteld wordt daarom dat in de wet opzeggingsregels worden opgenomen, die van toepassing zijn op de opzegging van het contract door beide partijen. Opzegging van een franchiseovereenkomst voor onbepaalde duur dient schriftelijk te geschieden en met inachtneming van een redelijke opzegtermijn. Een franchiseovereenkomst voor bepaalde tijd kan alleen tussentijds opgezegd worden wegens gegronde redenen, waaronder een wezenlijke tekortkoming in de nakoming en andere dwingende commerciële redenen.

In dit hoofdstuk wordt ook geadviseerd dat de franchisewetgeving aan de franchisenemer twee specifieke remedies toekent: het recht op terugkoop en het recht op een compensatie voor goodwill. Bij de beëindiging van een franchiserelatie moet de franchisenemer het recht hebben de franchisegever te verzoeken de resterende voorraad, reserveonderdelen, inventaris, voorraden, uitrusting en meubelen die hij van de franchisegever of diens erkende leverancier heeft gekocht, terug te kopen. Wanneer de franchisenemer door een niet-concurrentiebeding wordt beperkt, moet hij jegens de franchisegever ook recht hebben op een compensatie voor de goodwill van zijn onderneming.

Hoofdstuk 6: Conclusie

Hoofdstuk 6 sluit het proefschrift af met een samenvatting van de onderzoeksbevindingen van elk hoofdstuk. Daarbij wordt een samenvatting gegeven van de aanbevelingen voor het formuleren van privaatrechtelijke regels in specifieke franchisewetgeving en wordt ook aangegeven welke voorbehouden gelden ten aanzien van de bevindingen en aanbevelingen in dit onderzoek. In dit hoofdstuk zijn tevens modelbepalingen van franchisewetgeving opgenomen, die kunnen dienen als illustratie van de voorstellen die in dit proefschrift zijn

gedaan ten behoeve van het gebruik in rechtsstelsels die behoefte hebben aan regulering van de franchiseovereenkomst. Het proefschrift wordt afgesloten met suggesties voor toekomstig onderzoek.

Selected bibliography

BOOKS

- Abell M, *The Law and Regulation of Franchising in the EU* (Edward Elgar Publishing 2013)
- Abell M (ed), *The Franchise Law Review* (2nd edn, Law Business Research Ltd 2015)
- Armstrong G, Kotler P, and Oliver Opresnik M, *Marketing: An Introduction* (7th global edn, Pearson Education Limited 2023)
- Baez III HB, *Tort Law in the United States* (3rd edn, Kluwer Law International 2020)
- Bar CV and Clive E, *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.1, Oxford University Press 2010)
- *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.2, Oxford University Press 2010)
- *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.3, Oxford University Press 2010)
- *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR): Full Edition* (Vol.4, Oxford University Press 2010)
- Barkoff RM and others (eds), *Fundamentals of Franchising* (4th edn, American Bar Association 2016)
- Beale H and others, *Cases, Materials and Text on Contract Law* (3rd edn, Hart Publishing 2019)
- Bender M, and Courmadias N, *Marketing and the Law* (5th edn, LexisNexis 2015)
- Blair RD and Lafontaine F, *The Economics of Franchising* (2nd edn, Cambridge University Press 2010)
- Boele-Woelki K and Grosheide W (eds), *The Future of European Contract Law* (Kluwer Law International 2007)
- Bruce A, *Australian Competition Law* (4th edn, LexisNexis 2021)
- Bryan MW, Vann VJ, and Thomas SB, *Equity and Trusts in Australia* (2nd edn, Cambridge University Press 2017)
- Buberis P, *Australian Franchising Code of Conduct: A Critical Analysis with Current Case law* (Emerald Publishing 2020)
- Buchan J, *Franchisees as Consumers: Benchmarks, Perspectives and Consequences* (Springer 2013)
- Carter JW, *Contract Law in Australia* (7th edn, LexisNexis 2018)
- Butler D and others, *Contract Law Case Book* (3rd edn, Oxford University Press 2018)
- Castle TD, Steggall Z, and Terry A, *Destruction and Appropriation of Goodwill: The Problem of Non-renewal* (Competitive Foods Australia Limited 2007)
- Chatterjee DK (ed), *Encyclopedia of Global Justice* (Springer 2011)

- Chirelstein MA, *Concepts and Case Analysis in the Law of Contracts* (7th edn, Foundation Press 2013)
- Clarke P and Clarke J, *Contract Law: Commentaries, Cases, and Perspectives* (3rd edn, Oxford University Press 2016)
- Costello KR (ed), *Collateral Issues in Franchising: Beyond Registration and Disclosure* (American Bar Association 2015)
- Davis R, *Tritton on Intellectual Property in Europe* (5th edn, Thomson Reuters 2020)
- Davison MJ, Monotti AL, and Wisman L, *Australian Intellectual Property Law* (3rd edn, Cambridge University Press 2016)
- Díaz OB, *Franchising in European Contract Law: A comparison between the main obligations of the contracting parties in the Principles of European Law on Commercial Agency, Franchise and Distribution Contracts (PEL CAFDC), French and Spanish law* (sellier. european law publisher 2008)
- Dukes A, *Corones' Competition Law in Australia* (7th edn, Thomson Reuters 2018)
- Epstein RA, *Torts* (Aspen Law & Business 1999)
- Farnsworth EA, *Farnsworth on Contracts* (Vol. III, 2nd edn, Aspen Publisher, Inc. 1998)
- *United States Contract Law* (rev edn, Juris Publishing 1999)
- *Contracts* (4th edn, Aspen Publishers 2004)
- Garner BA (ed), *Black's Law Dictionary* (11th edn, Thomson West (US) 2019)
- Garner WM (ed), *Franchise Desk Book: Selected State Laws, Commentary and Annotations* (Vol 1, 3rd edn, American Bar Association 2019)
- Gestel RV, Micklitz HW, and Rubin EL (eds), *Rethinking Legal Scholarship: A Transatlantic Dialogue* (Cambridge University Press 2017)
- Giles S, *Annotated Franchising Code of Conduct* (2nd edn, LexisNexis Butterworths 2021)
- Greene N, Newton D, and Olson K (eds), *The Annotated Franchise Agreement* (2nd edn, American Bar Association 2021)
- Grueneberg S and Hurwitz A (eds), *The FTC Franchise Rule* (3rd edn, American Bar Association 2019)
- Hartkamp AS, *Contract Law in the Netherlands* (2nd edn, Kluwer Law International 2015)
- and others (eds), *Towards a European Civil Code* (4th edn, Kluwer Law International, 2011)
- Hay P, *The Law of the United States: An Introduction* (Routledge 2017)
- Hoy F, Perrigot R, and Terry A (eds), *Handbook of Research on Franchising* (Edward Elgar Publishing 2017)
- Husa J, *A New Introduction to Comparative Law* (Hart Publishing 2015)
- International Chamber of Commerce, *ICC Model International Franchising Contract* (ICC Publications 2011)
- International Institute for the Unification of Private Law, *UNIDROIT Principles of International Commercial Contracts 2016* (International Institute for the Unification of Private Law 2016)
- Jansen N and Zimmermann R (eds), *Commentaries on European Contract Laws* (Oxford University Press 2018)
- Klass G, *Contract Law in the United States* (2nd edn, Kluwer Law International 2012)
- Kötz H, *European Contract Law* (Gill Mertens and Tony Weir trs., 2nd edn, Oxford University Press 2017)

- Kyriakakis J and others, *Contemporary Australian Tort Law* (Cambridge University Press 2020)
- Lea D and Bradbery J, *Oxford Advanced Learner's Dictionary* (10th edn, Oxford University Press 2020)
- Loewinger AP and Lindsey MK (eds), *International Franchise Sale Laws* (2nd edn, American Bar Association 2016)
- Mehren ATV and Murray PL, *Law in the United States* (2nd edn, Cambridge University Press 2007)
- Miller AR and Davis MH, *Intellectual Property: Patents, Trademarks, and Copyright in a Nutshell* (6th edn, St. Paul Minn 2018)
- Miller L, *The Emergence of EU Contract Law: Exploring Europeanization* (Oxford University Press 2011)
- Mills J and Birks M, *Qualitative Methodology: A Practical Guide* (SAGE Publications 2014)
- Meiklejohn AM (ed), *Franchising: Cases, Materials, & Problems* (American Bar Association 2013)
- Monateri PG (ed), *Comparative Contract Law* (Edward Elgar Publishing 2017)
- Morrison AB (ed), *Fundamentals of American Law* (Oxford University Press 1996)
- Nickels WG, McHugh JM and McHugh SM, *Understanding Business* (12th edn, The McGraw-Hill Companies 2018)
- Omar PJ and Gant JLL (eds), *Research Handbook on Corporate Restructuring* (Edward Elgar 2021)
- Oosterhuis J, *Specific Performance in German, French and Dutch Law in the Nineteenth Century: Remedies in an Age of Fundamental Rights and Industrialisation* (Martinus Nijhoff Publishers 2011)
- Rose V and Bailey D (eds), *Bellamy & Child European Union Law of Competition* (8th edn, Oxford University Press 2018)
- Sagaert V, Storme M and Terryn E (eds), *The Draft Common Frame of Reference: national and comparative perspectives* (Intersentia 2012)
- Sappideen C and Vines P (eds), *Fleming's The Law of Torts* (10th edn, Thomson Reuters 2011)
- Schaper MT and Lee C (eds), *Competition Law, Regulation & SMEs in the Asia-Pacific: Understanding the Small Business Perspective* (ISEAS-Yusof Ishak Institute 2016)
- Schwartz VE, Kelly K, and Partlett DF, *Prosser, Wade and Schwartz's Torts* (14th edn, Foundation Press 2020)
- Siems M, *Comparative Law* (3rd edn, Cambridge University Press 2022)
- Smits JM, *Contract Law: A Comparative Introduction* (3rd edn, Edward Elgar 2021)
- (ed), *Elgar Encyclopedia of Comparative Law* (2nd edn, Edward Elgar 2012)
- Spencer EC, *The Regulation of Franchising in the New Global Economy* (Edward Elgar Publishing Limited 2010)
- Tight M, *Documentary Research in the Social Sciences* (SAGE Publications Ltd 2019)
- Webber R, *An Introduction to Franchising* (Palgrave Macmillan 2013)
- Windsperger J and others, *Economics and Management of Franchising Networks* (Physica-Verlag 2004)
- Woods WK (ed), *Fundamentals of International Franchising* (2nd edn, American Bar Association 2013)

THESES

- Atwell C, 'Early withdrawal rights in franchise contracts: A comparative study of their role and effectiveness in Australia, England and France' (DPhil thesis, UNSW Business School 2018)
- Gangemi NJJ, 'Is Goodwill Property?' (DPhil thesis, UNSW Business School 2019)

ARTICLES

- Abell M, 'The regulation of franchising in EU Member States' (2012) 10(2) *International Journal of Franchising Law* 17
- Aloisio TD, 'Franchising in Australia' (1989) 58 *Antitrust Law Journal* 949
- Anderson E, Lodish LM and Weitz BA, 'Resource Allocation Behavior in Conventional Channels' (1987) 24(1) *Journal of Marketing Research* 85
- Arnow-Richman R, 'Mainstreaming Employment Contract Law: The Common Law Case for Reasonable Notice of Termination' (2014) 66 *Florida Law Review* 1513
- Atwell C and Buchan J, 'The Franchise Fulcrum: The Legal System's Contributions to Research about Power and Control in Business Format Franchising' (2014) 21 *Journal of Marketing Channels* 180
- Baer JRF and Mills PJ, 'Renewals: Questions and Pitfalls for Franchisors and Some Distributors' (1990) 10 *Franchise Law Journal* 1
- Barthélemy J, 'Agency and institutional influences on franchising decisions' (2011) 26(1) *Journal of Business Venturing* 93
- Beaton-Wells C, 'Private Enforcement of Competition Law in Australia – Inching Forwards' (2016) 39 *Melbourne University Law Review* 681
- Benoliel U, 'Criticizing the Economic Analysis of Franchise Encroachment Law' (2011) 75(1) *Albany Law Review* 205
- and Buchan J, 'Franchisees' Optimism Bias and the Inefficiency of the FTC Franchise Rule' (2015) 13 *DePaul Business & Commercial Law Journal* 411
- , Buchan J, and Gutentag T, 'Revisiting the Rationality Assumption of Disclosure Laws: An Empirical Analysis' (2017) 46 *Hofstra Law Review* 469
- Blair RD and Lafontaine F, 'Understanding the Economics of Franchising and the Laws That Regulate' (2006) 26 *Franchise Law Journal* 55
- Boyle L, 'An Australian August Corpus: Why There Is Only One Common Law in Australia' (2015) 27 *Bond Law Review* 27
- Bridges EI, 'Keep Off My (Virtual) Lawn: Encroachment in the Age of the Internet' (2017) 36 *Franchise Law Journal* 415
- Buchan J, 'Challenges that franchisees of insolvent franchisors pose for liquidator' (2008) 16 *Insolvency Law Journal* 26
- 'Ex ante information and ex post reality for franchisees: The case of franchisor failure' (2008) 36 *Australian Business Law Review* 407
- 'Consumer Protection for Franchisees of Failed Franchisors: Is There a Need for Statutory Intervention?' (2009) 9(2) *Queensland University of Technology Law and Justice Journal* 232
- 'Deconstructing the Franchise as a Legal Entity: Practice and Research in International Franchise Law' (2014) 21 *Journal of Marketing Channels* 143

- 'Franchising: A Honey Pot in a Bear Trap' (2014) 34 *Adelaide Law Review* 283
- 'Australia's Franchising Code of Conduct Review – A Continuation Down the Path of Jamming a Square Peg into a Round Hole?' (2019) 47 *Australian Business Law Review* 393
- 'The 2018 Review of the Franchising Code of Conduct: Epicentre of a Year of Scrutiny for Australian Franchising' (2019) 47 *Australian Business Law Review* 101
- and Nicholls R, 'The Challenges of Navigating the COVID-19 Pandemic for Australia's Franchise Sector' (2020) *Australian Business Law Review* 126
- Chetwin M, 'Relational and Discrete Contracts and Remedies Requiring Supervision: Same Principle?' (2014) 38(1) *University of Western Australia Law Review* 80
- Chisum DS, 'State Regulation of Franchising: The Washington Experience' (1973) 48 *Washington Law Review* 291
- Chow L and Frazer L, 'Servicing customers directly: Mobile franchising arrangements in Australia' (2003) 37(3/4) *European Journal of Marketing*, 594
- Cise JGV, 'A Franchise Contract' (1969) 14 *Antitrust Bulletin* 325
- Curtin B, 'Recent developments in termination for convenience clauses: the role of good faith' (2010) 24(3) *Commercial Law Quarterly* 23
- Dant RP and Kaufmann P, 'Structural and strategic dynamics in franchising' (2003) 79 *Journal of Retailing* 63
- Dietrich J, 'Giving Content to General Concepts' (2005) 29 *Melbourne University Law Review* 218
- Dixon H and Quinn B, 'Franchising and the Internet: an exploratory study of franchisor Web sites' (2004) 14(4) *Internet Research* 311
- Dnes AW, 'A Case-Study Analysis of Franchise Contracts' (1993) 22 *Journal of Legal Studies* 367
- 'Franchise Contracts, Opportunism and the Quality of Law' (2009) 3 *Entrepreneurial Business Law Journal* 257
- Doellinger CJ, 'Incurable Breaches: A Fresh Look at an Old Problem' (2013) 32 *Franchise Law Journal* 119
- Doherty AM, Chen X, Alexander N, 'The franchise relationship in China: agency and institutional theory perspectives' (2014) 48 *European Journal of Marketing* 1664
- Dunn TM, 'The Franchisor's Control over the Transfer of a Franchise' (2008) 27 *Franchise Law Journal* 233
- Emerson RW, 'Franchise Contract Clauses and the Franchisor's Duty of Care toward Its Franchisees' (1994) 72(4) *North Carolina Law Review* 905
- 'Franchise Encroachment' (2010) 47(2) *American Business Law Journal* 191, 234
- 'Directing the Disjointed: A Call to Harmonize EU Franchise Law' (2014) 12 *International Journal of Franchising Law* 41
- 'Franchising Constructive Termination: Quirk, Quagmire or a French Solution' (2015) 18 *University of Pennsylvania Journal of Business Law* 163
- 'Franchise Terminations: Good Cause Decoded' (2016) 51 *Wake Forest Law Review* 103
- 'Thanks for the Memories: Compensating Franchisee Goodwill after Franchise Termination' (2018) 20 *University of Pennsylvania Journal of Business Law* 286
- and Benoliel U, 'Are Franchisees Well-Informed: Revisiting the Debate over Franchise Relationship Laws' (2012) 76 *Albany Law Review* 193

- and Benoliel U, 'Can Franchisee Associations Serve as a Substitute for Franchisee Protection Laws' (2013) 118 Penn State Law Review 99
- and Carrington CC, 'Devising a royalty structure that fairly compensates a franchisee for its contribution to franchise goodwill' (2020) 14(2) Virginia Law & Business Review 279
- Epstein RA, 'Unconscionability: A Critical Reappraisal' (1975) 18 Journal of Law & Economics 293
- Falbe CM and Dandridge TC, 'Franchising as a Strategic Partnership: Issues of Cooperation and Conflict in a Global Market' (1992) 10(3) International Small Business Journal, 40
- Farnsworth EA, 'Legal Remedies for Breach of Contract' (1970) 70(7) Colum Law Review 1145
- Fern MD and Klein PI, 'Restrictions on Termination and Nonrenewal of Franchises: A Policy Analysis' (1981) 36 The Business lawyer 1041
- Fichter CB, Malzahn AM, and Matheson A, 'Don't Tread on Me: A Defense of State Franchise Regulation' (2018) 38 Franchise Law Journal 23
- Fittante, Jr JJ, "'Community of Interest': Clarity or Confusion?' (2003) 22 Franchise Law Journal 160
- Fontenot G, Keaty A, and Srivastava R, 'Selling on the Internet into the Franchisee's Territory' (2006) 13(3) Journal of Marketing Channels 79
- Frazer L and others, 'Pre-contractual Due Diligence by Franchisees and Independent Small Business Buyers' (2018) 46 Australian Business Law Review 157
- Frignani A and Pratt JH, 'Termination and Non-Renewal of Franchise Agreements in the European Union: Italian Law in a Comparative Perspective with Other European Civil Law Systems and England and Wales' (2017) 37 Franchise Law Journal 15
- Fuller LL, 'Consideration and Form' (1941) 41 Columbia Law Review 799
- Gant JLL and Buchan J, 'Moral Hazard, Path Dependency and Failing Franchisors: Mitigating Franchisee Risk Through Participation' (2019) 47(2) Federal Law Review 261
- Frignani A, 'Italian Case Law after Three Years since the Enactment of Law, 6 May, 2004, No. 129' (2007) 5 International Journal of Franchising Law 17
- Garner WM, 'Editor's Column' (1991) 11 Franchise Law Journal 2
- 'The Implied Covenant of Good Faith in Franchising: A Model for Discretion' (1995) 20(2) Oklahoma City University Law Review 305
- Goldberg JCP, 'Pragmatism and Private Law' (2012) 125 Harvard Law Review 1640
- Golder T and Fuller A, 'The risks of 'e-tailoring' a franchise system' (2006) 9(4) Internet Law Bulletin 41
- Grimes WS, 'When Do Franchisors Have Market Power – Antitrust Remedies for Franchisor Opportunism' (1996) 65(1) Antitrust Law Journal 105
- Grub PD, 'Multinational Franchising: A New Trend in Global Expansion' (1972) 7(1) Journal of International Law and Economics 21
- Grueneberg S, 'Entering the U.S. Franchise Market: A Summary of Legal Considerations' (2013) 11(3) International Journal of Franchising Law 43
- Grünhagen M, Zheng X, and Wang JJ, 'When the Music Stops Playing: Post-litigation Relationship Dissolution in Franchising' (2017) 2 Journal of Retailing 138

- Gurnick D and Steve Vieux S, 'Case History of the American Business Franchise' (1999) 24 Oklahoma City University Law Review 37
- Hadfield GK, 'Problematic Relations: Franchising and the Law of Incomplete Contracts' (1990) 42(4) Stanford Law Review 927
- Harman KL, 'The Good Faith Gamble in Franchising Agreements: Does Your Implied Covenant Trump My Express Term?' (1997-1998) 28 Cumberland Law Review 473
- Hartlief T and Baeck J, 'Goodwill Compensation after Termination of a Franchise Contract: Comparative Perspective on Cour de Cassation 23 October 2012 (No. 11-21.978)' (2014) 22(6) European Review of Private Law 955
- Hill A, 'Good Faith: Enforcement in Australia' (2013) 11 International Journal of Franchising Law 29
- Kariyawasam K and Samarkovski L, 'Legal Issues in Franchising in Australia: Is the Current Regulatory Environment for the Franchise Sectoradequate' (2012) 9 Macquarie Journal of Business Law 179
- Karp EH and Stern AN, 'A Proposal for a Mandatory Summary Franchise Disclosure Document' (2016) 35 Franchise Law Journal 541
- Klein B, 'Transaction Cost Determinants of "Unfair" Contractual Arrangements' (1980) 70(2) The American Economic Review 356
- 'The economics of franchise contracts' (1995) 2 Journal of Corporate Finance 9
- Knoll DD, 'Assessing commercial losses in private trade practices litigation' (2002) 10 Competition & Consumer Law Journal 1
- Kronman AT, 'Mistake, Disclosure, Information, and the Law of Contracts' (1978) 7(1) The Journal of Legal Studies 1
- Kumar N, Scheer LK, and Steenkamp JEM, 'The Effects of Supplier Fairness on Vulnerable Resellers' (1995) 32 Journal of Marketing Research 54
- Lagarias PC and Kushell E, 'Fair Franchise Agreements from the Franchise Perspective' (2013) 33 Franchise Law Journal 3
- Leeming M, 'Theories and Principles Underlying the Development of the Common Law – The Statutory Elephant in the Room' (2013) 36 University of New South Wales Law Journal 1002
- Lindblom A and Tikkanen H, 'Knowledge creation and business format franchising' (2010) 48 Management Decision 179
- Loveland CA, 'Franchise Regulation: Ohio Considers Legislation to Protect the Franchisee' (1972) 33 Ohio State Law Journal 643
- Loverranes R, 'Termination for Convenience Clause' (2012) 14 University of Notre Dame Australia Law Review 103
- McLaughlin M and Rubinstein JH, 'Addressing the Threat of Punitive Damages Claims in Franchise and Dealer Litigation' (1995) 15(1) Franchise Law Journal 11
- Michael SC, 'First mover advantage through franchising' (2003) 18 Journal of Business Venturing 61
- Micklich NL, Lynch MW, and Festin IC, 'The Continuing Evolution of Franchise Valuation: Expanding Traditional Methods' (2013) 32 Franchise Law Journal 223
- Miravalls JM, 'Spanish Legal System on Disclosure in Franchise Networks: Problem and Proposals for an Improved Regulation' (2014) 25 European Business Law Review 943

- Modell C, 'Drafting Exclusive Territory Provisions in Franchise Agreements' (1996) 16(2) *Franchise Law Journal* 74
- Modell CS and Beck GA, 'Franchise Renewals – You Want Me to Do What' (2002) 22 *Franchise Law Journal* 4
- O'Sullivan J, 'Rescission as a Self-Help Remedy: A Critical Analysis' (2000) 59 *Cambridge Law Journal* 509
- Posner RA, 'The Concept of Corrective Justice in Recent Theories of Tort Law' (1981) 10 *The Journal of Legal Studies* 187
- Potter S, 'Why some people don't respond to warnings: writing effective short warning messages' (2021) 36 *Australian Journal of Emergency Management* 29, 30.
- Pratt J, 'Franchising in the United Kingdom' (2012) 32 *Franchise Law Journal* 95
- Preble JF and Hoffman RC, 'Competitive Advantage through Specialty Franchising' (1994) 8(2) *Journal of Services Marketing* 5
- Price S, 'Performance of Fast-food Franchises in Britain' (1993) 5(3) *International Journal of Contemporary Hospitality Management* 10
- Rubin P, 'The Theory of the Firm and the Structure of the Franchise Contract' (1978) 21(1) *The Journal of Law and Economics* 223
- Rudnick LG, 'Structuring a Franchise Relationship' (1980) 1 *Journal of the Forum Committee on Franchising* 9
- Saunders DW, 'Franchisee Sales of Existing Franchises' (1991) 11 *Franchise Law Journal* 31
- Schagen EV, 'The Draft Common Frame of Reference and Multilevel Governance' (2010) 1 *Edinburgh Student Law Review* 74
- Schaper MT, 'Franchising Regulation in Australia: Recent Trends and Current Issues' (2013) 11(1) *International Journal of Franchising Law* 3
- Schwartz A, 'The Case for Specific Performance' (1979) 89(2) *Yale Law Journal* 271
- Sears N, 'Australia's Updated Franchise Code of Conduct: Does an Express Obligation of Good Faith Benefit the Franchisor and Franchisee' (2014) 20 *Law and Business Review of the Americas* 121
- Shaikh A, 'Conceptualizing fairness in franchisor-franchisee relationship: Dimensions, definitions and preliminary construction of scale' (2016) 28 *Journal of Retailing and Consumer Services* 28
- Ship A, 'Specific Performance of Franchise and Distribution Agreements in Canada' (2012) 39 *Advocates' Quarterly* 407
- Ship A and Sohail M, 'Franchise Renewal and Transfers in Canada Common Law Provinces' (2015) 35 *Franchise Law Journal* 237
- Sotos J, 'Recent Trends in Franchise Relationship Laws' (2012) 10(1) *International Journal of Franchising Law* 3
- Steinberg P and Lescatre G, 'Beguiling Heresy: Regulating the Franchise Relationship' (2004) 109(1) *Penn State Law Review* 105
- Stover JJ, 'No Cure, No Problem: State Franchise Laws and Termination for Incurable Defaults' (2004) 23 *Franchise Law Journal* 217
- Svantesson D, 'Codifying Australia's Contract Law – Time for a Stocktake in the Common Law Factory' (2008) 20(2) *Bond Law Review* 1
- Tajti T, 'Franchise and Contract Asymmetry: A Common Trans-Atlantic Agenda' (2015) 37 *Loyola of Los Angeles International and Comparative Law Review* 245

- Terry A and Giugni PD, 'Freedom of Contract, Business Format Franchising and the Problem of Goodwill' (1995) 23(4) Australian Business Law Review 242
- and Lernia CD, 'Franchising and the Quest for the Holy Grail: Good Faith or Good Intentions' (2009) 33(2) Melbourne University Law Review 542
- Tractenberg C, Turgeon JP, and Destremes S, 'The Franchisor's Duty to Police the Franchise System' (2016) 36 Franchise Law Journal 87
- Turitto FR and others, 'Anatomy of a Franchise Dispute: Lessons for Transactional Lawyers Drafting Franchising Agreements' (2016) 14(5) International Journal of Franchising Law 3
- Velentzas J and Broni G, 'The Business Franchise Contract As A Distribution Marketing System: Free Competition And Consumer's Protection' (2013) 5 Procedia Economics and Finance 763
- Vincent WS, 'Encroachment: Legal Restrictions on Retail Franchise Expansion' (1998) 13 Journal of Business Venturing 29
- Wathne KH and Heide JB, 'Opportunism in Interfirm Relationships: Forms, Outcomes, and Solutions' (2000) 64 Journal of Marketing 36
- Watson A and others, 'Retail franchising: an intellectual capital perspective' (2005) 12 Journal of Retailing and Consumer Services 25
- Weinrib EJ, 'Corrective Justice' (1992) 77 Iowa Law Review 403
- Weldon EM and Micklich NL, 'Strange Weather: California's Amended Franchise Relations Act, AB 525' (2016) 35 Franchise Law Journal 577
- Williamson OE, 'The Economics of Organization: The Transaction Cost Approach' (1981) 87 American Journal of Sociology 548
- Wites MA, 'The Franchisor as Predator: Encroachment and the Implied Covenant of Good Faith' (1996) 7 University of Florida Journal of Law and Public Policy 305
- Withered JL, 'The No-Assignment-without-Consent Clause in Franchise Agreements' (1984) 4 Franchise Law Journal 1
- Woker T, 'Franchising – The Need for legislation' (2005) 17 South African Mercantile Law Journal 49
- Zellweger NS, 'Enforceability of Oral Franchise Agreement' (2009) 28 Franchise Law Journal 136
- Zines L, 'The Common Law in Australia: Its Nature and Constitutional Significance' (2004) 32 Federal Law Review 337

OTHER SECONDARY SOURCES

- Fair Work Ombudsman, *A Report of the Fair Work Ombudsman's Inquiry into 7-Eleven* (Commonwealth of Australia 2016)
- Franchise Council of Australia, *Submission by the Franchise Council of Australia to the Treasury Department in relation to the possible extension of unfair contract term protections to small business* (2014)
- Parliamentary Joint Committee on Corporations and Financial Services, *Fairness in Franchising* (Senate Printing Service 2019)
- Wein A, *Review of the Franchising Code of Conduct* (2013)

Curriculum vitae

Chalermwut Sriporm (Udon Thani, Thailand 1986) obtained his bachelor's degree in law with second class honours and master's degree in private law from the faculty of law of Thammasat University, Thailand, in 2009 and 2013, respectively. Subsequently, he was admitted to Leiden Law School, the Netherlands, and received his master's degree in advanced studies in international civil and commercial law in 2016. From 2017 to 2022, Chalermwut was registered as a contract PhD candidate doing a dissertation under the supervision of Prof. dr. Jac. Hijma and Dr. I.S.J. Houben at the Institute of Private Law of Leiden Law School of Leiden University. His PhD thesis focused on comparing the franchise legal framework of the DCFR, the USA, and Australia with a focus upon franchise contracts. Currently, Chalermwut is an assistant professor in private law at the faculty of law, Thammasat University (Lampang campus), Thailand. His areas of interest are contract law, tort law, and comparative private law.

In the range of books published by the Meijers Research Institute and Graduate School of Leiden Law School, Leiden University, the following titles were published in 2021, 2022 and 2023

- MI-365 M.P.A. Spanjers, *Belastingbudget. Onderzoek betekenis budgettaire impact belastingen bij parlementaire vaststelling belastingwetgeving* (diss. Leiden), Den Haag: Flosvier 2021, ISBN 978 90 8216 072 7
- MI-366 J. Zhang, *The Rationale of Publicity in the Law of Corporeal Movables and Claims. Meeting the Requirement of Publicity by Registration?* (diss. Leiden), Den Haag: Boom juridisch 2021
- MI-367 B.C.M. van Hazebroek, *Understanding delinquent development from childhood into early adulthood in early onset offenders* (diss. Leiden), Amsterdam: Ipskamp Printing 2021, ISBN 978 94 6421 2723
- MI-368 M.R. Manse, *Promise, Pretence and Pragmatism – Governance and Taxation in Colonial Indonesia, 1870-1940* (diss. Leiden), Amsterdam: Ipskamp Printing 2021
- MI-369 M.E. Stewart, *Freedom of Overflight: – A Study of Coastal State Jurisdiction in International Airspace* (diss. Leiden), Amsterdam: Ipskamp Printing 2021
- MI-370 M.T. Beumers, *De bescherming van immateriële contractuele belangen in het schadevergoedingsrecht* (diss. Leiden), Den Haag: Boom juridisch 2021, ISBN 978 94 6290 962 5
- MI-371 C.M. Sandelowsky-Bosman, T. Liefwaard, S.E. Rap & F.A.N.J. Goudappel, *De rechten van ongedocumenteerde kinderen in Curaçao – een gezamenlijke verantwoordelijkheid*, Den Haag: Boom juridisch 2021, ISBN 978-94-6290-965-6
- MI-372 G.J.A. Geertjes, *Staatsrecht en conventie in Nederland en het Verenigd Koninkrijk*, (diss. Leiden), Zutphen, Uitgeverij Paris bv 2021, ISBN 978 94 6251 270 2
- MI-373 L. Noyon, *Strafrecht en publieke opinie. Een onderzoek naar de relatie tussen de strafrechtspleging en het publiek, met bijzondere aandacht voor het Openbaar Ministerie*, (diss. Leiden), Den Haag: Boom juridisch 2021, ISBN 978 94 6290 978 6
- MI-374 F. Behre, *A European Ministry of Finance? Charting and Testing the National Constitutional Limits to EU Fiscal Integration*, (diss. Leiden), Amsterdam: Ipskamp Printing 2021
- MI-375 R. Spence, *Collateral transactions and shadow banking* (diss. Leiden), Amsterdam: Ipskamp Printing 2021
- MI-376 B.H.M. Custers, F. Dechesne & S. van der Hof (red.), *Meesterlijk. Liber amicorum ter gelegenheid van het emeritaat van prof. dr. Jaap van den Herik*, Amsterdam: Ipskamp Printing 2021
- MI-377 E. Campfens, *Cross-border claims to cultural objects. Property or heritage?*, (diss. Leiden), The Hague: Eleven 2021, ISBN 978 94 6236 250 5
- MI-378 S.R. Bakker, *Uitzonderlijke excepties in het strafrecht. Een zoektocht naar systematiek bij de beslissingen omtrent uitsluiting van strafrechtelijke aansprakelijkheid in bijzondere contexten*, (diss. Rotterdam), Den Haag: Boom juridisch 2021, ISBN 978 94 6290 998 4, ISBN 978 90 5189 194 2 (e-book)
- MI-379 M. Gkliati, *Systemic Accountability of the European Border and Coast Guard. The legal responsibility of Frontex for human rights violations*, (diss. Leiden), Alblasterdam: Ridderprint 2021
- MI-380 C.-I. Grigorieff, *The Regime for International Air Carrier Liability. To what Extent has the Envisaged Uniformity of the 1999 Montreal Convention been Achieved?*, (diss. Leiden), Amsterdam: Ipskamp Printing 2021
- MI-381 M. Stam, *Essays on Welfare Benefits, Employment, and Crime*, (diss. Leiden)
- MI-382 C.M.F. Mommers, *Voluntary return and the limits of individual responsibility in the EU Returns Directive*, (diss. Leiden), Amsterdam: Ipskamp Printing 2022, ISBN 978 94 6421 583 0
- MI-383 M.E. Franke, *Over de grens van de onrechtmatige daad. Een onderzoek naar de plaats van de rechtvaardiging in het buitencontractuele aansprakelijkheidsrecht*, (diss. Leiden), Den Haag: Boom juridisch 2022, ISBN 978 94 6290 152 0
- MI-384 B.L. Terpstra, *Instrumental and normative pathways to compliance. Results from field research on moped drivers*, (diss. Leiden), Amsterdam: Ipskamp Printing 2022

- MI-385 Q. Mauer, *Application, Adaptation and Rejection. The strategies of Roman jurists in responsa concerning Greek documents*, (diss. Leiden), Den Haag: Boom juridisch 2022, ISBN 978 94 6236 291 8, ISBN (e-book) 978 90 5189 952 8
- MI-386 F. Tan, *The Duty to Investigate in Situations of Armed Conflict. An examination under international humanitarian law, international human rights law, and their interplay*, (diss. Leiden), Amsterdam: Ipskamp Printing 2022
- MI-387 G.G. Lodder, *Recht doen of Recht hebben. Een analyse van de rechten van de migrant op bescherming door de staat tegen arbeidsuitbuiting*, (diss. Leiden), Amsterdam: Ipskamp Printing 2022, ISBN 978 94 6421 679 0
- MI-388 M. Mannan, *The Emergence of Democratic Firms in the Platform Economy: Drivers, Obstacles and the Path Ahead*, (diss. Leiden), Amsterdam: Ipskamp Printing 2022
- MI-389 A.M. Bouland, *'Please Give Me My Divorce'. An Ethnography of Muslim Women and the Law in Senegal*, (diss. Leiden), Amsterdam: Ipskamp Printing 2022
- MI-390 B.J. Braak, *Overcoming ruptures: Zande identity, governance, and tradition during cycles of war and displacement in South Sudan and Uganda (2014-9)*, (diss. Leiden), Amsterdam: Ipskamp Printing 2022
- MI-391 S.R. Varadan, *Article 5 of the UIN Convention on the Rights of the Child. Parental guidance and the evolving capacities of the child*, (diss. Leiden), Amsterdam: Ipskamp Printing 2022, ISBN 978 94 6421 700 1
- MI-392 J.M.W. Pool, *De rol van de curator bij de aanpak van onregelmatigheden. Een empirisch-juridisch onderzoek naar de rol van de curator in de praktijk bij de aanpak van onregelmatigheden voor en tijdens faillissement*, (diss. Leiden), Amsterdam: Ipskamp Printing 2022, ISBN 978 94 6421 827 5
- MI-393 D.S. Verkroost, *'Met zachte drang'. Uitgangspunten voor jeugdhulpverlening op het snijvlak van vrijwilligheid en dwang*, (diss. Leiden), Den Haag: Boom juridisch 2022, ISBN 978 94 6212 735 7, ISBN 978 94 0011 197 4 (e-book)
- MI-394 D. Măndrescu, *The application of EU antitrust law to (dominant) online platforms*, (diss. Leiden), Amsterdam: Ipskamp Printing 2022
- MI-395 A.H.A. Mohammad, *De normering van academisch ondernemerschap. Perspectieven vanuit het onderwijs(bekostigings)recht, het Europees staatssteunrecht en de academische vrijheid & wetenschappelijke integriteit*, (diss. Leiden), Amsterdam: Ipskamp Printing 2023
- MI-396 T.L. Masson-Zwaan, *Widening the Horizons of Outer Space Law*, (diss. Leiden), Amsterdam: Ipskamp Printing 2023, ISBN 978 94 6421 977 7
- MI-397 W. Zhang, *Achieving decent work in China. A case study of decent working time*, (diss. Leiden), Amsterdam: Ipskamp Printing 2023
- MI-398 T.M. Vergouwen, *The effect of directives within the area of direct taxation on the interpretation and application of tax treaties*, (diss. Leiden), Amsterdam: Ipskamp Printing 2023
- MI-399 R. de Massol de Rebetz, *Beyond the Dichotomy between Migrant Smuggling and Human Trafficking. A Belgian Case Study on the Governance of Migrants in Transit*, (diss. Leiden), Amsterdam: Ipskamp Printing 2023
- MI-400 W. Ruijs, *Pandbelening*, (diss. Leiden), Den Haag: Boom juridisch 2023, ISBN 978 94 0011 288 9 (e-book)
- MI-401 C. Sriporm, *Franchising Legal Frameworks. A Comparative Study of the DCFR, US Law and Australian Law Regarding Franchise Contracts*, (diss. Leiden), Amsterdam: Ipskamp Printing 2023, ISBN 978 94 6473 088 3