

FRANCHISE

Italy



Franchise

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Quick reference guide enabling side-by-side comparison of local insights, including franchise market overview; key considerations when forming and operating a franchise; offer and sale of franchises; franchise contracts and the franchisor/franchisee relationship; and recent trends.

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MARKET OVERVIEW

Franchising in the market

How widespread is franchising in your jurisdiction? In which sectors is franchising common? Are there any economic or regulatory issues in the market that are more or less hospitable to franchising or make it economically viable in your jurisdiction?

Franchising is an important instrument that has, in recent years, increased its importance in Italy with an annual increase of between 1.6 per cent and 2 per cent. This trend has continued during the covid-19 pandemic, in which franchising has proven to be particularly resilient and able to better face hardship. According to numbers published by Assofranchising in 2020 (the 2021 figures are yet to be published), in Italy, almost 1000 franchising networks that can be considered active (ie, with at least three sales points) are present. The majority of them are represented by Italian brands (almost 89 per cent) while the rest can be traced back to foreign franchise networks that operate either through a domestic master franchisor or only through franchisees. Within this spectrum, the food industry plays an important role; the number of restaurants and bars opened under franchise systems in 2018 increased by 20 per cent compared with 2017. Other sectors in which franchising is common are real estate and brokerage activities, education, gyms, beauty services, and sale of general goods to consumers.

Law stated - 03 June 2021

Associations

Are there any national or local franchise associations? What is their role in franchising, including any impact on laws or regulations? Are there any rules of conduct or membership requirements?

There are two franchise associations considered to be the most important in Italy. The first is the Italian franchising association Assofranchising, which was founded in 1971 and, according to own figures, has over 200 franchisor member brands that generate a turnover of over €6 billion through their respective franchise networks. The second is the Italian franchising federation Federfranchising, which belongs to the network of Confesercenti, which is one of the main business associations in the country. Confesercenti represents 350,000 small and medium-sized enterprises in the tourism, trade and services sectors, which are in turn grouped into 70 trade associations (of which Federfranchising is one). Both associations promote franchising in Italy and participate in the legislative process as groups of interest. Important regional and national events are regularly organised by both organisations, such as Assofranchising's annual Salone Franchising event, in which domestic and international franchisors and franchisees, as well as external experts and consultants, meet to discuss topics and trends of franchising.

Law stated - 03 June 2021

BUSINESS OVERVIEW

Types of vehicle

What forms of business entities are relevant to the typical franchisor?

Like most jurisdictions, Italy recognises business entities with limited and unlimited liability. The former is preferred in common commercial practice, particularly among franchise businesses, as it protects shareholders from general business risks and allows for a better allocation of funds.

Depending on the size of the proposed business, the relationship between shareholders and the types of investment, franchisors typically choose between a company limited by shares (SpA) or a limited liability company (Srl).

A SpA is more suitable for major franchise businesses because this type of entity offers more options regarding:

- shareholder agreements;
- the issue of debt notes;
- the allocation of assets for particular corporate purposes; and
- stock listing.

An Srl is more cost-efficient and suitable for small and medium-sized businesses since as this entity permits, among other things:

- greater shareholder control of the company's management;
- a stricter link between shareholders; and
- a more flexible management and shareholders' meeting system.

Law stated - 03 June 2021

Regulation of business formation

What laws and agencies govern the formation of business entities?

Both SpAs and Srls are governed by the Italian Civil Code, which provides all relevant legal provisions for the formation of such business entities. Special rules govern the mandatory registration of companies in the register of undertakings held by the relevant chamber of commerce.

Law stated - 03 June 2021

Requirements for forming a business

Provide an overview of the requirements for forming and maintaining a business entity.

Companies (both SpAs and Srls) are incorporated by means of a deed of incorporation, which also includes the relevant by-laws. With some differences between SpAs and Srls, the deed must contain all relevant information as to:

- the company's name and place of business (municipality only);
- the scope, amount and allocation of share capital;
- the shareholders' meetings; and
- the management rules.

The minimum share capital amounts are €50,000 for a SpA, €10,000 for an ordinary Srl and between €1 and €9,999 for a simplified Srl or an ordinary Srl with reduced share capital.

For the incorporation procedure to be effective and a company to acquire legal status, the deed of incorporation and by-laws must be converted into a public deed by a notary public and be registered with the register of undertakings. It costs approximately €2,500 to form an Srl and €5,000 to form a SpA. Usually, the registration procedure can be completed within five to seven days from the execution of the incorporation deed.

The maintenance of a business entity mainly requires payment of annual fees at the Chamber of Commerce (which

depend on the annual turnover), the preparation of mandatory company books, bookkeeping and filing annual tax declarations.

Law stated - 03 June 2021

Restrictions on foreign investors

What restrictions apply to foreign business entities and foreign investment?

In principle, no significant restrictions apply to foreign business entities and foreign investments. Where a foreign business entity engages in active business in Italy, it may be required or appropriate for it to register as a branch with the Italian register of undertakings, obtain a tax number for doing even the simplest transaction, or both. Some restricted business activities – generally those with a high level of public interest, such as companies in the banking and finance, transportation, energy, and food and drugs sectors – may require special licences from the relevant agencies.

With regard to foreign investment, foreign investors may face difficulties when trying to acquire company participations or merge with Italian companies involved in certain specific core businesses (eg, the automobile, energy or banking industries) given the potentially protective attitude by national or local authorities. Recently, in the context of the covid-19 pandemic, the Italian government has widened the application of the 'golden power' for specific strategic industries including energy, transports, public media, food safety and health etc, which authorises the Italian government to block transactions concerning control of relevant companies or to provide specific provisions.

Law stated - 03 June 2021

Taxation

What aspects of the tax system are relevant to franchisors? How are foreign businesses and individuals taxed?

The Italian tax system provides the following:

- Corporate income tax at a flat rate of 24 per cent.
- Regional tax on business activities, which is a local tax applied to the value of the production generated in each taxable period by persons carrying out business activities in an Italian region. The standard tax rate is set at a minimum of 3.9 per cent. Regions may increase or reduce the standard tax rate by up to 0.92 per cent.
- Value added tax (VAT), generally charged on any supply or service deemed to be made or rendered within Italy. The ordinary VAT rate is 22 per cent.
- Withholding tax (WT) on royalties, at a rate of 30 per cent (section 25(4) of Presidential Decree 600/73).

With regard to the taxation of foreign franchise businesses and individuals, a preliminary investigation into whether the payments qualify as royalties or services rendered within the franchise agreement must be performed, as the relevant tax treatment from an Italian perspective is different from other jurisdictions. This qualification must be assessed on a case-by-case basis, depending on the agreement and the relevant circumstances.

Should the payment be deemed a royalty, all fees paid in connection with a franchising agreement are taxed on the non-resident franchisor in Italy for its Italian source of income.

An Italian entity subject to WT must file a certification of the WT paid on behalf of the recipient, so that the recipient can use such document to obtain tax credits, if available, in its country of residence.

Further, royalties paid by a resident corporate business entity or a commercial public or private entity to a company or a permanent establishment resident in an EU member state other than Italy are tax exempt, provided that certain subjective and participation conditions are met. As to the latter, the exemption applies if:

- the paying company holds at least 25 per cent of the voting rights in the company receiving the payment;
- the recipient company holds at least 25 per cent of the voting rights in the paying company; or
- a third company directly holds at least 25 per cent of the voting rights in both the paying company and the receiving company (section 26quater of Presidential Decree 600/1973).

Conversely, should the initial and service fees be qualified as services rendered outside Italy, such income would not be subject to any tax in Italy, including WT, provided that the recipient does not have a permanent establishment in Italy.

From a VAT perspective, as per sections 7ter and 17 of the VAT Law (Presidential Decree 633/72), even if the franchisor is not an EU-based company, as the service or royalty is related to the Italian activity carried out by (or licensed to) a resident franchisee, the VAT on the relevant payments is due in Italy on the basis of the reverse charge mechanism. Should the non-resident franchisor be an EU-resident entity, the franchise system may be exempted from the application of VAT on the basis of the same mechanism.

Individuals

As a general rule, non-resident individuals are taxed only on income generated in Italy. An individual is considered resident in Italy for tax purposes if for the greater part of the fiscal year (ie, more than 183 days) the individual:

- is registered with the Registry of the Resident Population;
- has a residence in Italy; or
- has a domicile in Italy.

In Italy, individuals are subject to:

- personal income tax (between 23 and 43 per cent);
- an additional regional tax (between 0.9 and 1.4 per cent);
- an additional municipal tax (between 0.1 and 0.8 per cent); and
- a regional tax on business activities (which applies to individuals who have their own VAT position and are resident in Italy).

In the case of individuals with a VAT position, a favourable tax regime was recently implemented, under which a flat personal income tax of 15 per cent applies up to the personal income threshold of €65,000 per year and under the condition that further circumstances are met.

Non-resident individuals are subject to tax on income generated in Italy. According to section 23.2(c) of Ministerial Decree 917/1986, remuneration deriving from the use of intellectual property, processes, formulae, and industrial and commercial information in connection with know-how are deemed as generated in Italy if they are paid by the state, entities resident in the state or permanent establishments of non-resident entities. Such income is subject to a 30 per cent WT under section 25(4) of Presidential Decree 600/73. A tax treaty against double taxation may provide more favourable tax rates.

Law stated - 03 June 2021

Labour and employment

Are there any relevant labour and employment considerations for typical franchisors?

In principle, under a typical franchise structure, the franchisee is an independent entity or individual undertaking and bears its own entrepreneurial risk. Thus, even if the franchisor has its own standards to be applied by the franchisee and its employees, provided that no direct control, advice or subordination on the franchisee's employees is performed by the franchisor, there should be no concerns regarding the franchisor being deemed the employer of the franchisee or its employees. In the case of franchisees incorporated as unlimited liable companies, possible risks should be verified on a case-by-case basis, and be considered accordingly in the franchise agreement and its attachments.

Law stated - 03 June 2021

Intellectual property

How are trademarks and other intellectual property and know-how protected?

Trademarks are protected in Italy by means of registration with the Trademarks and Patents Office or, with regard to EU or international trademarks, through registration with the Office for Harmonisation in the Internal Market and the World Intellectual Property Organization.

Trademarks are regulated by the Industrial Property Code, which was enacted in Italy by Legislative Decree 30/2005.

A duly registered trademark provides the owner with exclusivity rights for 10 years starting from the date of filing the registration request. The owner of a registered trademark has the right to its exclusive use, as well as the right to ban any third parties from using it.

Know-how and trade secrets are expressly recognised in sections 98 and 99 of the Industrial Property Code.

As for protection, the law provides for action where know-how and trade secrets are communicated to third parties, or obtained in an illegal or inappropriate manner. Know-how and trade secrets are generally protected by rules on unfair competition.

To be eligible for protection, know-how must be secret, carry economic value through its secrecy and be kept by the owner in a proper manner to maintain its secrecy.

Law stated - 03 June 2021

Real estate

What are the relevant aspects of the real estate market and real estate law? What is the practice of real estate ownership versus leasing?

Real estate transactions and issues may be crucial to franchisors, particularly where a franchise relationship is connected with a real estate development agreement and real estate finance (this is typical in the hotel and food industry franchise business). This is the case even with smaller and medium-sized franchise businesses, where the franchisee must comply with the franchisor's standards.

In Italy, real estate is expensive compared with other countries. However, prices differ depending on whether it is located in a major city and in a central area or in smaller cities.

Real estate law is governed mainly by the Italian Civil Code with regard to ownership, while lease agreements are regulated by the Italian Civil Code and specific laws (in particular the Commercial Lease Law No. 392/1978). Specific

legislation regulates all relevant administrative town planning issues.

The lease of real estate for commercial purposes must cover a period of at least six to nine years for hotels and similar businesses. Restrictions may apply on automatic renovation after expiration. Renewal cannot be denied upon the first expiration unless the owner can show specific needs as set out in the applicable laws. Commercial lease law provides the possibility for the tenant to withdraw for extraordinary reasons with a six-month notice period. Parties are free to agree on further withdrawal rights. The possibility to rebalance the economic conditions of the lease agreement in case of extraordinary events that impact the business of the tenant (such as, for example, the covid-19 pandemic) must be assessed unless not regulated in the contract, according to the general principles of the Italian Civil Code in relation to force majeure. Further to this, there have been numerous decisions in the Italian courts that have not produced a unanimous opinion on the right of the lessee to rebalance the contract.

It is common practice for landlords that own or manage big commercial infrastructures (such as outlets, airports, train stations, etc) to lease the premises for commercial activities not via an ordinary lease agreement according to commercial lease law (which is more protective of tenants) but with a lease agreement over a business that requires appropriate attention during the relevant negotiations.

Law stated - 03 June 2021

Competition law

What aspects of competition law are relevant to the typical franchisor in your jurisdiction? How is competition law enforced in the franchising sector?

There is no specific competition law regarding franchisees, although the general EU provisions on this must be considered. In brief, the consolidated versions of the Treaty on the European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU) provide for specific rules on competition and, specifically, on vertical agreements and the restraints deriving from the execution of them.

Article 101 TFEU expressly prohibits agreements that may affect trade between EU countries and that prevent, restrict or distort competition. Included among the practices prohibited and referred to under article 101 TFEU is the fixing, either directly or indirectly, of the purchase or selling prices or any other trading conditions, inter alia. Pursuant to article 101, paragraph 2 TFEU, any vertical agreement (prohibited under article 101, paragraph 1 TFEU) is considered automatically void. Despite this, the agreements, which create sufficient benefits to outweigh the anticompetitive effects, are exempt from this prohibition under article 101, paragraph 3 TFEU. With the Commission Regulation No. 2790/1999 of 22 December 1999 (L 336/21) (the Regulation), the European Commission issued new legislation aiming to implement the aforementioned exception for vertical agreements. The Regulation introduced a new principle of balancing the anticompetitive effects of vertical agreements with their benefits, if any. Upon expiration of the Regulation (31 May 2010), on 23 April 2010, the European Commission issued Commission Regulation No. 330/2010 (the New Regulation). The New Regulation, as did the Regulation, concerns the applicability of article 101, paragraph 3 TFEU to vertical agreements.

While no maximum term is provided by the applicable law for the duration of a franchise agreement (which can have an open or a limited term), it must be noted that according to article 3.3 of Act 129/2004 (the Franchising Act), if the agreement is for a limited term, the franchisor must guarantee the franchisee a minimum term related to the period of amortisation of the franchisee's investments. This term must not be less than three years, except in cases of early termination for breach of contract by one of the parties.

The non-compete clause does not represent an essential element of the franchise agreement; therefore, if it is not expressly provided for in the contract, it will not operate between the parties. The non-compete clause is governed by article 2596 of the Italian Civil Code, which provides that such an agreement may have a maximum duration of five

years and must be limited in time or to a specific activity or area. However, according to the prevailing case law, article 2596 of the Civil Code does not apply to agreements between entities operating at different levels of the line (so-called vertical agreements), as is the case for franchises. Consequently, a non-compete clause included in a franchise agreement is not subject to the limits provided for by article 2596 of the Civil Code. Consequently, in principle, the involved parties (and the franchisor) are free to regulate the non-compete clause in the contract if preferred.

Law stated - 03 June 2021

OFFER AND SALE OF FRANCHISES

Legal definition

What is the legal definition of a franchise?

'Franchising' is defined in Act 129/2004 (the Franchising Act) as a particular kind of agreement between two separate entities – one of which is independent from the other both legally and economically – according to which the franchisor, in exchange for payment, grants the franchisee a set of industrial and intellectual property rights (eg, trademarks, commercial trade names, displays, utility models, designs, copyright, know-how, patents, and technical and commercial assistance or consulting). In executing a franchise agreement, the franchisee becomes part of the network of franchisees operating within a determined territory aimed at promoting specific goods or services.

In practice, one of the main purposes of franchising is the creation of a collaborative system and a productive distribution network.

Law stated - 03 June 2021

Laws and agencies

What laws and government agencies regulate the offer and sale of franchises?

Italy enacted a general law on franchising in 2004 and an implementing regulation thereto in 2005. The relevant laws are:

- the Franchising Act, which came into effect on 25 May 2004;
- Ministerial Decree 204/2005 (regulation on commercial franchising – the Franchising Regulation);
- Act 287/1990 (rules on the protection of competition and the market – the Antitrust Law);
- the EU Block Exemption Regulation on Vertical Restraints (330/2010), which is directly applicable in Italy (the previous EU Regulation 2790/1999 having expired); and
- Act 192/1998 (regulation of sub-supply within the production activities) – in particular, section 9 on the abuse of economic dependence (the Anti-Economic Abuse Law).

These laws and regulations provide no agency for the sale or offer of franchises and operate on a general level. No particular exemptions or exclusions are provided.

Law stated - 03 June 2021

Principal requirements

What are the principal requirements governing the offer and sale of franchises under the relevant laws?

The Franchising Act

The Franchising Act provides the most common mandatory rules applicable to franchise agreements, which generally protect prospective franchisees.

According to section 3 of the Franchising Act, a franchise agreement must be executed in written form to become legally valid. The franchisor must have experimented with its own business formula on the market. The minimum duration of the agreement must put the franchisee in the position to have a return on the investment and cannot be less than three years. Further, at least 30 days before the agreement's prospective execution date (cooling-off), the franchisor must provide the prospective franchisee with a copy of the agreement to be signed and any relevant information concerning the franchisor's activity, including:

- basic information relevant to the agreement, such as:
 - the amount of investment and entry fees to be paid by the franchisee before starting its activities;
 - the royalties and fees to be paid to the franchisor;
 - details of territorial exclusivity, if any;
 - the know-how to be transferred to the franchisee;
 - the criteria for the recognition of know-how added by the franchisee;
 - the services and assistance rendered by the franchisor; and
 - the renewal, termination and assignment rules of the agreement;
- the contractual relationships between franchisor and franchisee, including the transfer of trademarks and other intellectual property rights and the pre-contractual obligations that the parties must comply with (for example, reference is made to the disclosure of information and data useful for the stipulation of the contract (sections 4 to 6 of the Franchising Act));
- the possibility to agree, apart from the ordinary jurisdiction clauses or arbitration rules, on a conciliation (alternative dispute resolution) procedure before the chamber of commerce of the territory in which the franchisee is located; and
- circumstances under which the contract may be declared void (section 8 of the Franchising Act).

The Franchising Regulation

The Franchising Regulation applies exclusively to franchisors active outside Italy. It mainly sets out the rules on the pre-disclosure obligations of foreign franchisors towards franchisees.

The Franchising Regulation states that, at least 30 days before the prospective execution date of the agreement, the franchisor must deliver to the prospective franchisee a complete set of all contractual documents and the attachments thereto. Further, within the same 30-day period, the franchisor must deliver a list of franchisees operating in each single state and the number of sales points related thereto. At the request of the prospective franchisee, the franchisor must also deliver the contact details of at least 20 operating franchisees, as well as information on judicial proceedings.

The Antitrust Law

Should a commercial agreement be qualified as an agreement that gives rise to anticompetitive issues from an antitrust perspective (as with certain exclusivity clauses in franchising or distribution agreements), unless such an agreement falls under the EU Block Exemption Regulation on Vertical Restraints, it may be prohibited by the Antitrust Law.

The Anti-Economic Abuse Law

Section 9 of this legislation states that any agreement that is the result of one or more entity's abuse of the existing economic dependence of another undertaking is null and void.

Abuse exists if the dominant entity can take advantage of the other entity, so that the agreement may result in a gross disparity between the parties. The dependence is also evaluated in light of the possibility of the weak entity obtaining alternatives from the market.

The application of the Anti-Economic Abuse Law to franchising has been widely debated. Recent case law has denied that it applies to franchises due to the fact that franchise contracts are per se agreements between a strong and a weak entity, whereby the strong one imposes its business model on the weaker one. Franchise agreements should be upheld under the freedom of contract principle; therefore, the opinion that the Anti-Economic Abuse Law should not apply to a franchise system seems to be correct.

Law stated - 03 June 2021

Franchisor eligibility

Must franchisors satisfy any eligibility requirements in order to offer franchises? Are there any related practical issues or guidelines that franchisors should consider before offering franchises?

Neither the Franchising Act (applicable to franchise contracts governed by Italian law for franchisors that already operate in Italy) nor the Franchising Regulation (applicable exclusively to franchisors that operate only outside Italy where the agreement is subject to Italian law) set any minimum period for having been in business before operating in Italy.

However, the Franchising Act requires franchisors, as part of their pre-contractual information duties, to provide franchisees with a list of affiliated franchisees and changes to affiliated franchisees in the past three years, or at least as of the date of the start of business. This pre-contractual obligation implies that there must be a minimum level of activity and franchisees for a franchisor to start a franchise business in Italy. The exact determination of the business must be examined on a case-by-case basis.

However, the Franchising Regulation sets a more stringent requirement for the pre-contractual information duties of franchisors that have operated exclusively outside Italy. They must provide the prospective franchisee with a list of franchisees divided by country of operation. On the request of the franchisee, the franchisor must provide a list of at least 20 affiliated franchisees or, if the number is below 20, the complete list of franchisees. Therefore, similar to the Franchising Act, the minimum business requirements for foreign franchisors must be evaluated on a case-by-case basis. So, although there is no minimum period to have been in business, the pre-contractual information duties require franchisors to provide information on an existing business to the prospective franchisor, the content of which must be evaluated on a case-by-case basis.

Further, section 3 of the Franchising Act provides that, to create a franchising system, the franchisor must have tested such a commercial system in a relevant market to protect potential franchisees from becoming involved with commercial systems that exist only 'on paper'. In the absence of any provision in the Franchising Act, the Italian Franchising Association Code of Ethics provides for a minimum duration of one year for such market testing.

Alternatively, franchisors may expressly indicate in their franchising agreements that a franchising formula has not yet been tested in the market. Should this be the case, the potential franchisee would be aware of any connected risks when deciding whether to enter into the franchising agreement. If the franchisor does not inform the potential franchisee about a lack of previous testing of its franchising system in the market, the franchisee is entitled to take action to annul the franchising agreement pursuant to sections 1.337 and 1.338 of the Italian Civil Code, and specifically for a violation of the pre-contractual good faith obligation.

Law stated - 03 June 2021

Franchisee and supplier selection

Are there any legal restrictions or requirements relating to the manner in which a franchisor recruits franchisees or selects its or its franchisees' suppliers? What practical considerations are relevant when selecting franchisees and suppliers?

Neither the Franchising Act nor the Franchising Regulation restrict the manner in which a franchisor can recruit franchisees or select its own or its franchisees' suppliers.

Nevertheless, as to the location of the franchised outlets, even if territorial exclusivity is not required as a necessary part of the franchise agreement pursuant to section 3.4(c) of the Franchising Act, franchisees are part of a network of franchisees operating within a determined territory and must be strategically distributed. Thus:

- the franchisor must inform the franchisee of the outlets involved within the network (section 4.1(d) of the Franchising Act) and must inform the franchisee each year of changes concerning the other franchised outlets in the franchised network (section 4.1(e) of the Franchising Act); and
- the franchisee cannot move its franchised outlet if the franchise agreement specifically provides the respective location, except by reason of force majeure, and provided that the franchisor agrees (section 5.1 of the Franchising Act).

Apart from the provisions set out under the Franchising Act and the Franchising Regulation (in the case of a franchisor originally operating outside Italy), any other commercial provisions are left to the contracting parties, franchisor and franchisees.

Law stated - 03 June 2021

Pre-contractual disclosure – procedures and formalities

What procedures and formalities for pre-contractual disclosure are required or advised in your jurisdiction? How often must the disclosures be updated?

Under sections 4 and 6 of the Franchising Act, franchisors must disclose to franchisees a complete set of information, with the exception of that which is actually reserved or whose disclosure may violate third-party rights, at least 30 days before the stipulation of the contract (cooling-off).

Section 4 of the Franchising Act also states that franchisors must make this disclosure to the prospective franchisee within the cooling-off period. The disclosure obligation is therefore limited only to the pre-contractual phase, while the performance of the contract must be carried out by the parties in compliance with the principle of good faith set out in section 1375 of the Civil Code. In light of the above, the Franchising Act imposes no duty on franchisors to update the information disclosed in the pre-contractual phase.

Law stated - 03 June 2021

Pre-contractual disclosure – content

What information is the disclosure document required or advised to contain?

Pursuant to sections 4 and 6 of the Franchise Act, the franchisor must disclose to the franchisee a complete set of information, with the exception of that which is sensitive or whose disclosure may violate third-party rights, at least 30

days before the contract is signed.

Different information must be disclosed by the franchisor depending on whether the franchisor operates within or exclusively outside Italy. A franchisor operating exclusively within Italian territory or both in Italy and abroad must provide the franchisee with a copy of the contract to be signed and the following information:

1. data regarding the franchisor;
2. information concerning the trademarks used in the network;
3. a summary description of the activities and characteristics of the business concept of the franchise network;
4. a list of franchisees operating within the network and the physical locations of the franchisor;
5. an indication of the annual variation of the number of franchisees and their relevant location within the past three years, or from the beginning of the franchise activity if it started less than three years ago; and
6. a summary description of court or arbitration proceedings, or both, involving the franchise network at issue that have been started by franchisees, third parties or public authorities against the franchisor and concluded in the past three years, in compliance with data protection provisions.

According to the Franchise Regulation, a franchisor that operates exclusively outside of Italy must provide the franchisee with the information described in (1), (2) and (3), along with the following:

- a list of franchisees operating within the network, and of the physical locations of the franchisor, sorted country by country (if requested by the franchisee, the franchisor must also supply the franchisee with a list of at least 20 franchisees operating within the network and their relevant locations);
- an indication of the annual variation – sorted country by country – of the number of franchisees and their relevant locations within the past three years or, if it started less than three years ago, from the beginning of the franchise activity; and
- a summary description of any court proceedings concluded with a final judgment within the three years preceding the contract being signed and arbitral proceedings concluded by a final award within the same time frame as described above.

Both the specified court and arbitration proceedings must concern the franchise system. In this regard, the franchisor must provide at least the following information:

- the parties involved;
- the judicial or arbitral authority;
- the claims; and
- the decision or award.

Law stated - 03 June 2021

Pre-sale disclosure to sub-franchisees

In the case of a sub-franchising structure, who must make pre-sale disclosures to sub-franchisees? If the sub-franchisor must provide disclosure, what must be disclosed concerning the franchisor and the contractual or other relationship between the franchisor and the sub-franchisor?

Section 2 of the Franchising Act also applies to sub-franchising. However, it provides no rules as to who must make pre-sale disclosures to the sub-franchisees. That said, given the fact that sub-franchisors are delegated to manage the entire franchise structure in a given territory, such pre-sale disclosure must in practice be made by the sub-franchisor. Given that the pre-sale disclosure rules regarding franchisors apply to sub-franchisors, they must therefore disclose at least what is provided for in section 4 of the Franchising Act.

Sub-franchisors must act with regard to their sub-franchisees according to the principles of good faith, fair dealing and loyalty (section 6 of the Franchising Act) in the pre-sale phase and onwards. With regard to their relationship with the franchisor, sub-franchisors must in principle disclose any further information requested by sub-franchisees that is reasonably relevant to the franchise business, unless such information can be regarded as confidential or its communication would violate third-party rights.

Law stated - 03 June 2021

Due diligence

What due diligence should both the franchisor and the franchisee undertake before entering a franchise relationship?

Before entering into a franchising agreement, franchisors should verify the reliability of the prospective franchisee, especially from a financial standpoint. The prospective franchisee will be requested to pay royalties and other amounts provided by the agreement (eg, an entry fee and advertising contribution). Franchisors should therefore evaluate before the relationship starts whether the prospective franchisee is a reliable subject to work with and whether they will be able to properly manage their activity in order to avoid damaging the franchisor's reputation.

In turn, prospective franchisees should evaluate the type of business that they will run under the franchising agreement. Further, as the prospective franchisee assumes the risk of a new activity, it should verify the solidity of the franchising system and trademark. The prospective franchisee should also verify the costs that it will have to pay (ie, royalties, minimum fees, entry fees, etc).

Both franchisor and franchisees should perform their respective verifications with the impact of covid-19 on the planned business activities of the franchising system taken into account.

Law stated - 03 June 2021

Failure to disclose – enforcement and remedies

What actions may franchisees or any relevant government agencies take in response to a franchisor's failure to make required disclosures? What legal remedies are available? What penalties may apply?

There is no statutory provision on this specific issue; however, sub-franchisors must disclose to sub-franchisees all of the information required under section 4 of the Franchising Act. That said, franchisors are held liable for any disclosure violation to sub-franchisors and sub-franchisees connected to the information required under section 4 of the Franchising Act. Conversely, if the disclosure violation occurs in the process of disclosure by the sub-franchisor and the sub-franchisees or does not consist of false information disclosed by the franchisor, or both, the latter would not be held liable for a disclosure violation. In this case, only the sub-franchisor would be liable.

In principle, individual officers, directors and employees of the franchisor or the sub-franchisor cannot be held personally liable, unless it can be proved that they acted under tort (fraud or negligence) or committed a crime punishable under the Criminal Code.

Failure to disclose – apportionment of liability

In the case of sub-franchising, how is liability for disclosure violations shared between franchisor and sub-franchisor? Are individual officers, directors and employees of the franchisor or the sub-franchisor exposed to liability? If so, what liability?

From a contractual point of view, violation of the disclosure obligations by the franchisor allows the franchisee to claim annulment of the agreement pursuant to section 1439 of the Italian Civil Code, together with compensation for damages, if due, pursuant to section 8 of the Franchising Act.

In the case of sub-franchisees, the master franchisee is responsible for the disclosure of non-compliance or for pre-contractual misrepresentation towards the sub-franchisees, which act in this sense as the franchisor. In any case, the franchisor's duty of control over the master franchisee cannot be excluded. In fact, whenever the franchisor violates his or her duty of control, there could be a non-contractual liability on the franchisor's part towards the franchisee.

Law stated - 03 June 2021

General legal principles and codes of conduct

In addition to any laws or government agencies that specifically regulate offering and selling franchises, what general principles of law affect the offer and sale of franchises? What industry codes of conduct may affect the offer and sale of franchises?

The Franchising Act provides for specific pre-contractual obligations for both franchisors and franchisees. Franchisors must exercise goodwill, fairness and good faith at all times when dealing with a prospective franchisee. Further, the franchisor must provide the prospective franchisee with any information that the franchisee considers necessary or useful for the purposes of the franchise agreement in a timely manner. However, franchisors can withhold information that is reasonably deemed to be confidential or if such a disclosure could infringe third-party rights. At the same time, prospective franchisees must exercise goodwill, fairness and good faith at all times in dealing with the franchisor. Prospective franchisees must provide the franchisor with any information that is necessary or appropriate for the purposes of the franchise agreement, in a timely, correct and comprehensive way.

In light of the foregoing, good faith, fairness and also general principles of loyalty affect the offer and sale of franchises during pre-contractual, contractual and post-contractual phases pursuant to sections 1175, 1337, 1358 and 1375 of the Italian Civil Code.

In addition to the Franchising Act and the Franchising Regulation, private organisations that may have an influence on franchise activity include the Italian franchising association Assofranchising and the Italian franchising federation Federfranchising, which have issued specific codes of conduct with which their members must comply.

Law stated - 03 June 2021

Fraudulent sale

What actions may franchisees take if a franchisor engages in fraudulent or deceptive practices in connection with the offer and sale of franchises?

From a contractual point of view, a franchisor's violation of the disclosure obligations allows the franchisee to claim

annulment of the agreement under section 1439 of the Civil Code, together with compensation for damages, if due, pursuant to section 8 of the Franchising Act.

Conversely, a violation of said obligation has no criminal consequences and requires no involvement of government agencies.

The Franchising Act expressly provides for the annulment of the agreement should any party disclose false information to the other. In any event, such annulment must in principle be requested and declared by a judge or an arbitration panel.

Pursuant to section 1439 of the Italian Civil Code, expressly mentioned by section 8 of the Franchising Act, any agreement may be annulled if false information disclosed by one of the parties led the other to sign the contract.

As to damages, in principle, only the material loss suffered and proved should be recoverable. It is unclear whether loss of profit could be recoverable, as this provision of the Franchising Act has yet to be interpreted by the courts.

Sub-franchisors must disclose to sub-franchisees all of the information required under section 4 of the Franchising Act. That said, franchisors are held liable for any disclosure violation to sub-franchisors and sub-franchisees connected to the information required under section 4 of the Franchising Act. Conversely, if the disclosure violation occurs in the process of disclosure by the sub-franchisor and the sub-franchisees or does not consist of false information disclosed by the franchisor, or both, the franchisor would not be held liable for disclosure violation. In this case, only the sub-franchisor would be liable.

In principle, individual officers, directors and employees of the franchisor or the sub-franchisor cannot be held personally liable, unless it can be proved that they acted under tort (fraud or negligence) or committed a crime punishable under the Criminal Code.

Franchisors may terminate a franchise relationship in the case of default or non-performance of the franchisee's obligations. In general, termination is granted if the breach of the agreement can be considered a serious breach (eg, a default in payment of fees and royalties, a violation of any exclusivity rights on the product or non-compliance with the franchisors' standards). In any case, the agreement should clearly state the cases in which the franchisor can terminate the franchise relationship without a notice period.

Law stated - 03 June 2021

FRANCHISE CONTRACTS AND THE FRANCHISOR/FRANCHISEE RELATIONSHIP

Franchise relationship laws

What laws regulate the ongoing relationship between franchisor and franchisee after the franchise contract comes into effect?

The Franchising Act

Act 129/2004 (the Franchising Act) provides the most common mandatory rules applicable to franchise agreements, which generally protect prospective franchisees.

According to section 3 of the Franchising Act, a franchise agreement must be executed in written form to become legally valid. The franchisor must have experimented with its own business formula on the market. The minimum duration of the agreement must put the franchisee in the position to have a return on the investment and cannot be less than three years. Further, at least 30 days before the agreement's prospective execution date (cooling-off), the franchisor must provide the prospective franchisee with a copy of the agreement to be signed and any relevant information concerning the franchisor's activity, including:

- basic information relevant to the agreement, such as:

- the amount of investment and entry fees to be paid by the franchisee before starting its activities;
 - the royalties and fees to be paid to the franchisor;
 - details of territorial exclusivity, if any;
 - the know-how to be transferred to the franchisee;
 - the criteria for the recognition of know-how added by the franchisee;
 - the services and assistance rendered by the franchisor; and
 - the renewal, termination and assignment rules of the agreement;
- the contractual relationships between franchisor and franchisee, including the transfer of trademarks and other intellectual property rights and the pre-contractual obligations that the parties must comply with (for example, reference is made to the disclosure of information and data useful for the stipulation of the contract (sections 4 to 6 of the Franchising Act));
 - the possibility to agree, apart from the ordinary jurisdiction clauses or arbitration rules, on a conciliation (alternative dispute resolution) procedure before the chamber of commerce of the territory in which the franchisee is located; and
 - circumstances under which the contract may be declared void (section 8 of the Franchising Act).

The Franchising Regulation

Ministerial Decree 204/2005 (regulation on commercial franchising – the Franchising Regulation) applies exclusively to franchisors active outside Italy. It mainly sets out the rules on the pre-disclosure obligations of foreign franchisors towards franchisees.

The Franchising Regulation states that, at least 30 days before the prospective execution date of the agreement, the franchisor must deliver to the prospective franchisee a complete set of all contractual documents and the attachments thereto. Further, within the same 30-day period, the franchisor must deliver a list of franchisees operating in each single state and the number of sales points related thereto. At the request of the prospective franchisee, the franchisor must also deliver the contact details of at least 20 operating franchisees, as well as information on judicial proceedings.

The Antitrust Law

Should a commercial agreement be qualified as an agreement that gives rise to anticompetitive issues from an antitrust perspective (as with certain exclusivity clauses in franchising or distribution agreements), unless such an agreement falls under the EU Block Exemption Regulation on Vertical Restraints (330/2010), it may be prohibited by Act 287/1990 (rules on the protection of competition and the market – the Antitrust Law).

The Anti-Economic Abuse Law

Section 9 of Act 192/1998 (regulation of sub-supply within the production activities the Anti-Economic Abuse Law) states that any agreement that is the result of one or more entity's abuse of the existing economic dependence of another undertaking is null and void.

Abuse exists if the dominant entity can take advantage of the other entity, so that the agreement may result in a gross disparity between the parties. The dependence is also evaluated in light of the possibility of the weak entity obtaining alternatives from the market.

The application of the Anti-Economic Abuse Law to franchising has been widely debated. Recent case law has denied that it applies to franchises due to the fact that franchise contracts are per se agreements between a strong and a weak entity, whereby the strong one imposes its business model on the weaker one. Franchise agreements should be upheld under the freedom of contract principle; therefore, the opinion that the Anti-Economic Abuse Law should not

apply to a franchise system seems to be correct.

Apart from the specific laws indicated above, the general provisions set out in the Italian Civil Code govern the contractual relationship.

Law stated - 03 June 2021

Operational compliance

What mechanisms are commonly incorporated in agreements to ensure operational consistency and adherence to brand standards?

In general, franchisors provide franchisees with operational manuals and detailed instructions so that the franchisees have all the tools to comply with the franchising system.

In order to ensure franchisee compliance with the operational terms and standards of the agreement during the relationship, franchisors may include a specific provision granting them the right to carry out inspections at the franchisee's premises to ascertain franchisee compliance.

Franchisors should ensure, through specific contractual clauses to be implemented in the franchise agreement, that franchisees comply with mandatory applicable guidelines for the performance of the specific activity to be carried out, in particular with respect to health and safety issues (connected, for example, to the covid-19 pandemic) and include in the manuals all the relevant procedures and information.

Law stated - 03 June 2021

Amendment of operational terms

May the franchisor unilaterally change operational terms and standards during the franchise relationship?

Franchisors generally cannot unilaterally change operational terms and standards during an agreement, especially if the changes are material and likely to alter the object of the contractual relationship between the parties. That said, many franchising agreements include clauses providing the right for the franchisor to change unilaterally, for example, the products to be sold by the franchisee. However, such clauses do not allow franchisors to make unlimited changes.

Law stated - 03 June 2021

Policy affecting franchise relations

Do other government or trade association policies affect the franchise relationship?

Neither the government nor any trade association may in principle affect the franchise relationship. However, the Italian Association of Franchising and the Italian Federation of Franchising have issued specific codes of conduct with which all of their members must comply. In principle, such codes may extend the obligations set out by law to further protect the weaker party in the franchise relationship.

Law stated - 03 June 2021

Termination by franchisor

In what circumstances may a franchisor terminate a franchise relationship? What are the specific legal restrictions on a franchisor's ability to terminate a franchise relationship?

Franchisors may terminate a franchise relationship in the case of default or non-performance of the franchisee's obligations. In general, termination is granted if the breach of the agreement can be considered a serious breach (eg, a default in payment of fees and royalties, a violation of any exclusivity rights on the product or non-compliance with the franchisors' standards). In any case, the agreement should clearly state the cases in which the franchisor can terminate the franchise relationship without a notice period.

Law stated - 03 June 2021

Termination by franchisee

In what circumstances may a franchisee terminate a franchise relationship?

Franchisees may terminate the relationship based on a serious breach of the contract terms by the franchisor.

If a franchisee terminates the agreement, it is entitled to reimbursement of the initial fees and costs, damages, or both. In practice, because of the extreme difficulties in proving and quantifying damages, franchise agreements usually grant the franchisee the right to be reimbursed the entrance fee, if any, or an obligation for the franchisor to repurchase the franchisee's stock. However, a typical franchise agreement may include a penalty fee in favour of the franchisor if the franchisee terminates the agreement without reasonable cause.

Law stated - 03 June 2021

Renewal

How are renewals of franchise agreements usually effected? Do formal or substantive requirements apply?

The parties are free to determine the renewal conditions. If they decide to renew the agreement, they are free to change the conditions therein.

Law stated - 03 June 2021

Refusal to renew

May a franchisor refuse to renew the franchise agreement with a franchisee? If yes, in what circumstances may a franchisor refuse to renew?

Under section 3.4(g) of the Franchising Act, renewal conditions must be set out in the agreement, therefore it is crucial to state such conditions clearly. However, in principle, there is no legal obligation for a franchisor to renew the franchise agreement.

Law stated - 03 June 2021

Transfer restrictions

May a franchisor restrict a franchisee's ability to transfer its franchise or restrict transfers of ownership interests in a franchisee entity?

Pursuant to section 3.4(g) of the Franchising Act, the terms for transfer of the contract must be expressly indicated therein. Restrictions are therefore permitted.

Law stated - 03 June 2021

Fees

Are there laws or regulations affecting the nature, amount or payment of fees?

There are no legislative measures on or restricting the nature and amount of fees.

Law stated - 03 June 2021

Usury

Are there restrictions on the amount of interest that can be charged on overdue payments?

The amount of interest on overdue payments can be specified in the contract. However, it cannot exceed the usury rate that is fixed every three months by a ministerial decree. In general, the maximum rate is between 10 and 20 per cent each year, depending on the nature of the relevant business. In the absence of specific contractual provisions, the tax rate is determined by a specific law on overdue payments in commercial transactions and the Italian Civil Code.

Law stated - 03 June 2021

Foreign exchange controls

Are there laws or regulations restricting a franchisee's ability to make payments to a foreign franchisor in the franchisor's domestic currency?

There are no currency restrictions regarding payments by national (local) franchisees of royalties and other payments to non-resident franchisors in their domestic currency. However, certain anti-money laundering requirements may impose specific restrictions. In principle, payments can be made only through an authorised bank or a financial intermediary (eg, bank wire or cheques).

Law stated - 03 June 2021

Confidentiality covenant enforceability

Are confidentiality covenants in franchise agreements enforceable?

Yes, according to the general principles of Italian law on general covenants. Franchise agreements should provide for specific penalties that the party that breaches the covenant must pay to make it easier to quantify the damage suffered by the compliant party.

Law stated - 03 June 2021

Good-faith obligation

Is there a general legal obligation on parties to deal with each other in good faith during the term of the franchise agreement? If so, how does it affect franchise relationships?

Section 6 of the Franchising Act sets out the franchisor's express duty to act under the principles of good faith, fair dealing and loyalty with regard to prospective franchisees during the pre-sale phase.

Under sections 1337 and 1375 of the Civil Code, all parties must deal in good faith during both the pre-sale and the post-sale phase (after the formation of the contract). This principle was reaffirmed by a recent Supreme Court decision stating that a franchise agreement requires a tight and loyal collaboration between the franchisor and the franchisees. Failure to comply with such obligations can be taken into consideration by the courts when evaluating the liability of the parties or calculating the damages, and with respect to termination issues.

Law stated - 03 June 2021

Franchisees as consumers

Does any law treat franchisees as consumers for the purposes of consumer protection or other legislation?

No. A franchisee within a franchise structure is always qualified as a business entity. Therefore, it has a fiscal code, and must generally request a value added tax code and be registered with the competent local register of undertakings.

However, within an atypical franchise structure, the franchisees may be qualified as professionals or semi-professionals, which in principle should exclude them from being treated as consumers (although this is not always the case), or as occasional professionals without any organisation or entrepreneurial risk (eg, in a franchise system that contemplates the door-to-door sale of the franchise's products, where the franchisee does not have to purchase the goods from the franchisor or any of its qualified suppliers within the franchise system).

In such an atypical franchise system, the franchisee may well be treated as a consumer, with all associated consequences, especially regarding the right to withdrawal and other protection rights.

Law stated - 03 June 2021

Language of the agreement

Must disclosure documents and franchise agreements be in the language of your country?

In principle, the Italian language is not mandatory for franchise agreements. However, should a franchisee request an Italian version of the franchise agreement, the franchisor must comply with this request under section 3(1) of the Franchising Regulation. If parties agree on a foreign language, it is advisable that the domestic party declares in the contract that he or she has sufficient knowledge of the foreign language to understand the content of the agreement.

Law stated - 03 June 2021

Restrictions on franchisees

What types of restrictions are commonly placed on the franchisees in franchise contracts?

Under section 3(3) of the Franchising Act, the first term of the franchise cannot be less than three years (except when

terminated for breach of contract).

As to restrictions on purchases or leases of goods or services, they may be considered harsh conditions that, according to section 1341(2) of the Italian Civil Code, must be expressly approved by a second signature.

Parties can choose the law governing the contract and enter into any agreements on arbitration or alternative dispute resolution rules.

Law stated - 03 June 2021

Courts and dispute resolution

Describe the court system. What types of dispute resolution procedures are available relevant to franchising?

Italy has different courts depending on the relevant case matter (ordinary, administrative and tax courts). A typical franchise agreement falls under the ordinary jurisdiction, which is a three-level system: the first-instance court, the Court of Appeal and the Supreme Court. In general, Italian court proceedings can last a long time (up to two or three years for a first-instance judgment). It is therefore advisable to opt for arbitration.

The Code of Civil Procedure contains specific arbitration rules. Parties may choose between a ritual arbitration, an arbitration under the rules of a chamber of commerce (typically Milan) or any other relevant domestic or international organisation (eg, the Rome branch of the International Chamber of Commerce).

Notably, the Italian Federation of Franchising provides for alternative dispute resolution solutions specifically tailored to franchises.

Law stated - 03 June 2021

Governing law

Are there any restrictions on designating a foreign governing law in franchise contracts in your jurisdiction? How does the governing law affect the contract's enforceability?

Parties have, in general, the possibility to select a foreign governing law but mandatory provisions of the Franchise Act always apply (for example, concerning the contract's minimum duration and the pre-contractual disclosure obligations). If a foreign governing law has been chosen, contractual obligations between the parties – with respect to breach of contract, etc – will be decided based on the chosen foreign law that, if brought in front of an Italian court, could lead to a more complicated judicial process. Therefore, if a foreign governing law has been chosen, it is advisable to designate a court of the nominated country that will make a judgment based on its own domestic laws in case of any controversy.

Law stated - 03 June 2021

Arbitration – advantages for franchisors

What are the principal advantages and disadvantages of arbitration for foreign franchisors considering doing business in your jurisdiction? Are any other alternative dispute resolution (ADR) procedures particularly favoured or disfavoured in your jurisdiction?

The advantages of a foreign franchisor choosing arbitration over ordinary court proceedings are:

- speed (even though the arbitration decision may be appealed, which would mean the commencement of ordinary

- proceedings of the usual duration);
- the possibility of choosing the arbitrators;
 - the highest level of efficiency during the procedure, as the arbitration procedure does not fall within the court procedure and is therefore not affected by common delays experienced in court; and
 - confidentiality (possibly the most important advantage).

The fact that the arbitration procedure and decisions are private may represent a significant advantage for parties that wish to keep the results of litigation undisclosed. Further, franchisors may choose the applicable rules governing the procedure, language of the arbitration and seat. Conversely, should the parties to a contract decide on arbitration, the major disadvantages are the high costs of the procedure and the difficulty of finding experienced arbitrators. This is also a problem from another perspective: the parties to an arbitration are more inclined to choose an arbitrator for their impartiality rather than their skills as a judge.

Law stated - 03 June 2021

National treatment

In what respects, if at all, are foreign franchisors treated differently (legally, or as a practical matter) from domestic franchisors?

In principle, the only relevant differences are set out in the Franchising Regulation regarding pre-contractual duties where the franchisor operates outside Italy, provided that the agreement is subject to Italian law. From a practical point of view, foreign franchisors that are internationally unknown, have been in business for a short period and cannot show a consolidated international business model may be treated differently to national franchisors in court.

Law stated - 03 June 2021

UPDATE AND TRENDS

Legal and other current developments

Are there any proposals for new legislation or regulation, or to revise existing legislation and regulation? Are there other current developments or trends to note?

No new legislation or legislative amendments specific to franchising have been announced. In recent years, an electronic invoice system has been introduced in Italy, which applies to all domestic entities.

The covid-19 pandemic has had a considerable impact on all business activities, including franchising, but it has to be pointed out that the franchising system – which is based on a partnership between franchisors and franchisees within a common system – has proven to be particularly resilient. In the first few months of 2021, several Italian franchisors, including in the food sector, announced the opening of new points of sale and an increase in the size of their network, both in Italy and abroad. From a strictly legal point of view, it is advisable to include specific covid-19 clauses in future franchise agreements that ensure compliance with any governmental provisions and restrictions. These clauses should also enable both franchisor and franchisee to implement all activities necessary to safeguard the franchising system and the relevant businesses, based on a fair balance between the parties.

The information contained in this chapter is accurate as at 3 June 2021.

Law stated - 03 June 2021

Jurisdictions

	Australia	Norton Rose Fulbright
	Canada	Lapointe Rosenstein Marchand Melançon LLP
	China	Jones & Co
	Finland	ADVOCARE Law Office
	France	Bersay
	Germany	Taylor Wessing
	India	G&W Legal
	Israel	Gilat Bareket & Co, Reinhold Cohn Group
	Italy	Rödl & Partner
	Japan	Anderson Mōri & Tomotsune
	Malaysia	Wong Jin Nee & Teo
	Mexico	Gonzalez Calvillo SC
	Netherlands	Parker Advocaten
	New Zealand	Stewart Germann Law Office
	Norway	CLP
	South Africa	Spoor & Fisher
	South Korea	Lee & Ko
	Switzerland	Kellerhals Carrard
	Turkey	Özdağıştanlı Ekici Attorney Partnership
	United Kingdom	Ashtons Legal
	USA	Lathrop GPM