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Philip F Zeidman
DLA Piper LLP (US)

Franchise M&A
Andrae J Marrocco
Dickinson Wright LLP

Australia
Alicia Hill and Raynia Theodore
MST Lawyers

Brazil
Paulo Shiguero Yamaguchi, Marco Mello Cunha and Victor Goulart Lazarini
Tess Advogados

Canada
Bruno Floriani and Marissa Carnevale
Lapointe Rosenstein Marchand Melançon LLP

Chile
Cristóbal Porzio
Porzio Rios Garcia

China
Claudio d’Agostino
DLA Piper UK LLP (Shanghai)
Paula Cao
DLA Piper UK LLP (Beijing)

Denmark
Mikkel Friis Rossa and Dan Bjerg Geary
Bech-Bruun

Finland
Patrick Lindgren
Advocare Law Office

France
Emmanuel Schulte
Bersay & Associés

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Advaya Legal

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Anderson Mōri & Tomotsune

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Lee & Ko

Malaysia
Jin Nee Wong
Wong Jin Nee & Teo

Mexico
Jorge Mondragón
González Calvillo SC

New Zealand
Stewart Germann
Stewart Germann Law Office

Norway
Kjetil Vågen and Eline Thorsrud
Advokatfirmaet CLP DA

Russia
Vladimir Biriulin and Sergey Medvedev
Gorodissky & Partners

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Meyerlustenberger Lachenal

Thailand
Chanvithaya Suvarnapunya and Pattama Jarupunphol
DLA Piper (Thailand) Limited

Turkey
Hikmet Koyuncuoğlu
Koyuncuoğlu & Köksal Law Firm

United Kingdom
David Bond, Gordon Drakes and Vicky Reinhardt
Fieldfisher

United States
Richard Greenstein and Philip F Zeidman
DLA Piper LLP (US)
Overview

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

In general, as with most jurisdictions, Italy has businesses that have limited and unlimited liability. The former is clearly preferred in common commercial practice, particularly in franchise businesses, as limited liability protects shareholders from general business risks and allows better allocation of funds.

Depending on the size of the proposed business, the relationship among shareholders and the types of investments, franchisors typically choose between a company limited by shares (SpA) or a limited liability company (Srl). The first entity offers more options regarding agreements among shareholders, the issue of debt notes, the allocation of assets for particular corporate purposes and stock listing. It is therefore more suitable for major franchise businesses that entail larger investments. The second option permits, inter alia, greater shareholder control of the company’s management, a stricter link between shareholders, and a more flexible management and shareholders’ meeting system. It is more cost-efficient and is more suitable for small and medium-sized franchise businesses.

The relevant corporate rules have been extensively amended in recent years. In particular, the SpA can also be organised with the ‘dual structure’ similar to the German system, where the management is appointed by a supervisory board (also exercising the control function) rather than by the shareholders. The Srl can be managed with a board of directors (the traditional system) or as a single-director management. For further information about these kinds of business entities, see question 3. In addition, there is also a simplified Srl that enjoys the same main features as a regular Srl (in particular limited liability of the shareholders), but the requirements for its incorporation are fewer and simplified, provided that a set of prerequisites are met.

Other forms of business entities rather less relevant to the typical franchisor are the sole proprietorship, the general partnership, the simplified, provided that a set of prerequisites are met. For further information about these kinds of business entities, see question 3. In addition, there is also a simplified Srl that enjoys the same main features as a regular Srl (in particular limited liability of the shareholders), but the requirements for its incorporation are fewer and simplified, provided that a set of prerequisites are met.

2 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 into the register of undertakings held by the relevant chamber of commerce.

3 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 the SpA and Srl, said documents must contain all relevant information as to the company’s name, the place of business (municipality only), the scope, the amount and allocation of share capital, the shareholders’ meeting and the management rules, etc.

Minimum share capital amounts to €30,000 for an SpA, €10,000 for an ordinary Srl and from €1 to €9,999 for the simplified Srl or for the ordinary Srl with reduced share capital. When the deed of incorporation is executed, at least 25 per cent of the relevant share capital must be paid in before or upon incorporation. However, for simplified Srl and for the Srl with reduced share capital, the share capital must be fully paid in upon incorporation.

For the incorporation procedure to be effective and for the company to acquire its legal status, the deed of incorporation and the by-laws must be formed by a notary public as a public deed and be registered with the register of undertakings. It costs about €2,500 to form an Srl and about €5,000 to form an SpA.

4 What restrictions apply to foreign business entities and foreign investment?

In principle, there are no significant restrictions applicable 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 degree of public interest, such as companies in the banking and finance, transportation, energy, and food and drugs sectors – may require special licences issued by the relevant agencies.

With regard to foreign investments, some difficulties may be faced by foreign investors trying to acquire company participations or merge with Italian companies involved in certain specific core businesses, such as the automobile industry, energy or banking, given the possible protective attitude by national or local authorities.

5 Briefly describe the aspects of the tax system relevant to franchisors. How are foreign businesses and individuals taxed?

The Italian tax system, as relevant to franchise business entities, provides the following taxes:

- corporate income tax (RES), at a flat rate of 24 per cent;
- regional tax on business activities (IRAP), which is a local tax applied on the value of the production generated in each taxable period by persons carrying out business activities in a given 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 0.9 per cent;
- VAT, generally charged on any supply or service deemed to be made or rendered within Italian territory. The ordinary VAT rate is set at 22 per cent; and
- withholding taxes (WT) on royalties, at a rate of 30 per cent according to article 254(4) of Presidential Decree No. 600/73 (unless a specific treaty against the double taxation with Italy providing a lower WT rate applies, as, for example, the Organisation for Economic Cooperation and Development model treaty, which is the one generally adopted).

With regard to the taxation of foreign franchise businesses and individuals, a preliminary investigation has to be made of whether the payments qualify as royalties (the exploitation or revenue arising from the licensing of intellectual property rights, know-how, trademarks, etc) or as services rendered within the franchise agreement, as the relevant tax treatment from an Italian perspective is different. This qualification...
is to 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. According to article 23.2(c) of Ministerial Decree 917/1986, remuneration deriving from the utilisation of intellectual property, trademarks, processes, formulae, and industrial and commercial information in connection with know-how, are deemed as being produced in Italy if they are paid by the state, by entities resident in the state or by permanent establishments of non-resident entities. Taxes are levied by the application of a 30 per cent WT that is applied to 100 per cent of the gross amount of the payment (on a cash basis). However, any relevant tax treaty regarding the double taxation may provide for more favourable tax rates, which in such a case will prevail over the domestic taxation regime described above.

The Italian entity subject to WT must file a certification related to the WT paid on behalf of the recipient, so that the recipient will be able to use such document in order to obtain tax credits, if available, in its country of residence.

Moreover, royalties paid by a resident corporate business entity (SpA or Srl) 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 both in the paying company and in the receiving company (article 26-quater of Presidential Decree 600/1973). A similar regime also applies to business entities tax resident in Switzerland.

On the other hand, should the initial and the service fees be qualified as services rendered outside of Italy, such income would not be subject to any taxation in Italy, nor to WT, provided that the recipient does not have a permanent establishment in Italy.

From a VAT perspective, as per section 7-ter of the Italian VAT Law (Presidential Decree No. 653/72) and section 17 of the same law, even if the franchisor is not an EU-based company, as the service or the 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 franchising may be exempted from the application of VAT on the basis of a reverse charge 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, for more than 183 days) one of the following conditions is met:

- the individual is registered with the Registry of the Resident Population;
- the individual has a residence (habitual abode) in Italian territory;
- the individual has a domicile (principal centre of business, economic and social interests) in Italian territory.

In Italy, individuals are subject to personal income tax (from 23 to 43 per cent), additional regional tax (from 0.9 to 1.4 per cent), additional municipal tax (0.1 to 0.8 per cent) and IRAP (applicable to those that have their own VAT position and are resident in Italy).

A non-resident individual is subject to taxation on the income generated in Italy. As mentioned above, according to article 23.2(c) of Ministerial Decree 917/1986, remuneration deriving from the use of intellectual property, trademarks, processes, formulae and industrial and commercial information in connection with know-how is deemed as being generated in Italy if it is paid by the state, by entities resident in the state or by permanent establishments of non-resident entities. The income will be subject to 30 per cent WT according to article 25(4) of Presidential Decree No. 600/73. A tax treaty against double taxation may provide for more favourable tax rates.

6 **Are there any relevant labour and employment considerations for typical franchisors? What is the risk that a franchisee or employees of a franchisee could be deemed employees of the franchisor? What can be done to reduce this risk?**

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 either the franchisee or the franchisee’s employees. In conclusion, as long as the relationship that affects the employees of the franchisee is, and remains, an internal relationship between the franchisor and the franchisee under the franchise terms, there should be no risk. In this respect, to reduce this risk, the franchisor must avoid, to the best of its abilities, having any direct contact and providing any instructions directly to such employees.

7 **How are trademarks and know-how protected?**

Trademarks are protected in Italian territory by means of registration with the Italian Trademarks and Patents Office (based in Rome) or, with regard to European or international trademarks, through registration to be made respectively with the Office for Harmonization in the Internal Market (based in Alicante) and the World International Property Organization (based in Geneva).

Trademarks are regulated by the Industrial Property Code (IPC) enacted in Italy by Legislative Decree No. 30 of 10 February 2005. A duly registered trademark provides the owner with exclusivity rights for 10 years starting from the date of the filing of 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 were expressly recognised for the first time in Italy by sections 98 and 99 of the IPC. 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 needs to be secret, carry economic value through its secrecy and be kept by the owner in a proper manner to maintain its secrecy.

8 **What are the relevant aspects of the real estate market and real estate law?**

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

Real estate is quite expensive compared with other countries. Prices, however, differ depending on whether the real estate object is located in a major city and in a central area.

Real estate law is governed mainly by the Italian Civil Code with regard to ownership. Lease agreements are regulated by the Italian Civil Code and specific laws. Specific legislation regulates all relevant administrative town planning issues. Leases of real estate for commercial purposes must be for a minimum term of six years, or 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.

**Laws and agencies that regulate the offer and sale of franchises**

9 **What is the legal definition of a franchise?**

The definition of franchising is given in the Franchising Act (see question 10), according to which franchising is 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 payments, grants the franchisee a set of industrial and intellectual property rights that may include trademarks, commercial trade names, displays, utility models, designs, copyrights, know-how, patents and technical and commercial assistance.
or consulting. In executing a franchise agreement, the franchisee becomes part of a 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 of a productive distribution network.

10 Which 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:

- Act No. 129 of 6 May 2004 (rules on commercial franchising), which became effective on 23 May 2004 (the Franchising Act);
- Ministerial Decree No. 204 of 2 September 2005 (regulation on commercial franchising - the Franchising Regulation);
- Act No. 287 of 10 October 1990 (rules on protection of competition and the market – the Italian Antitrust Law);
- Commission Regulation (EC) No. 330/2010, issued on 23 April 2010 by the EU Commission on the application of article 101/3 of the Treaty on the Functioning of the European Union to categories of vertical restraints (EU Block Exemption Regulation on vertical restraints), which is also directly applicable in Italy (the previous Regulation No. 795/1999 expired); and
- Act No. 192 of 18 June 1998 (regulation of sub-supply within the production activities), in particular, article 9 on the abuse of economic dependence (the Anti-Economic Abuse Law).

Italian laws and regulations do not provide for any agency to regulate the offer and sale of franchises. However, a significant role is played by private organisations that may help in finding partners, namely the Italian Franchising Association and the Italian Federation of Franchising.

11 Describe the relevant requirements of these laws and agencies.

The Franchise Act

The Franchise Act provides the most common mandatory rules applicable to franchise agreements, generally aimed at protecting the prospective franchisee.

According to section 3 of the Franchising Act, the 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 be that which is necessary to allow the amortisation of the investment, and in any event the duration cannot be less than three years. Furthermore, it requires that at least 30 days prior to the contemplated execution date of the agreement, the franchisor provides the prospective franchisee with complete information, including a copy of the agreement to be signed and any relevant information concerning the franchisor's activity, including the following:

- basic information relevant to the agreement, including:
  - 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;
  - the 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. Among the latter, 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, upon 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 Franchise Regulation

The Franchise Regulation applies exclusively to franchisors active outside Italy. It mainly sets forth the rules on the pre-disclosure obligations of a foreign franchisor towards the franchisee.

The Franchise Regulation states that, at least 30 days prior to the contemplated execution date of the agreement, the franchisor must deliver to the prospective franchisee a complete set of all contractual documents and the attachments thereto. Moreover, 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. Upon 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.

Furthermore, upon the request of the prospective franchisee, the franchisor must deliver a copy of all the information concerning the agreement and the attachments thereto in Italian.

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 agreement falls under the EU Block Exemption Regulation on vertical restraints No. 330/2010 dated 23 April 2010 (directly applicable also in Italy), it may be prohibited by the Italian Antitrust Law. See question 17.

The Anti-Economic Abuse Law

This legislation has played a role in the most recent court cases. Article 9 states that any agreement that is the result of one or more undertaking's abuse of the existing economic dependence of another undertaking (supplying or client), shall be null and void.

Abuse exists if the dominant undertaking can take advantage of the other undertaking, 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 undertaking 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 is applicable to franchises, whereas some scholars are of the opinion that it is. The reason for the negative view is that in general a franchise contract is per se an agreement between a strong and a weak undertaking, where the strong one imposes its business model, which is the essence of the franchise agreement. A franchise agreement 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 the correct one, although risk exists and the issue must be addressed on a case-by-case basis.

12 What are the exemptions and exclusions from any franchise laws and regulations?

The Franchising Act does not provide for any exemption or exclusion from its application. The Franchise Regulation, however, applies only to franchisors that have operated their franchise business exclusively outside Italy.

In the opinion of most scholars, the Franchise Act does not introduce any exception to the general international legal principles on conflict of laws. Hence, the parties are free to choose the law under which the contract will be governed. However, ‘opting out’ of Italian law will not apply with respect to those provisions set forth in the interest of the weakest party of the contract (the franchisee), such as, for instance, those concerning disclosure obligations (section 4 of the Franchising Act) and minimum content of the contract (section 3.4 of the Franchising Act).

13 Does any law or regulation create a requirement that must be met before a franchisor may offer franchises?

Neither the Franchise Act (applicable to franchise contracts governed by Italian law for franchisors that already operate in Italy) nor the Franchise 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 prior to operating in Italy.

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87

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However, the Franchise Act requires the franchisor to provide the franchisee, as part of its pre-contractual information duties, 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.

The Franchise Regulation, however, sets a more stringent requirement for the pre-contractual information duties of franchisors that have operated exclusively outside Italy. They need to provide the prospective franchisee with a list of franchisees divided per country of operation. Upon the appointment 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 Franchise Act, for foreign franchisors the minimum business requirements 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 the franchisor 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, article 3 of the Franchising Act provides that in order to create a franchising system, the franchisor must have tested such commercial system in a relevant market; this rule aims to protect potential franchisees from becoming involved with commercial systems that exist only ‘on paper’. Market testing is not limited to the Italian market, but also includes testing in European or global markets, and will generally consist of the franchisor directly operating various pilot outlets. In the absence of any provision in the Franchising Act, the code of Ethics of the Franchising Italian Association provides for a minimum duration of one year for such market testing.

Alternatively, the franchisor may expressly indicate in the franchising agreement that a franchising formula has not yet been tested in the market. Should this be the case, the potential franchisee will be aware of such connected risks when deciding whether to enter into the franchising agreement. If the franchisor does not inform the potential franchisee about a lack of a previous testing in the market of its franchising system, the franchisor would be entitled to take action to annul the franchising agreement pursuant to articles 1377 and 1338 of the Italian Civil Code, and specifically for a violation of pre-contractual good faith obligation.

### 14 Are there any laws, regulations or government policies that restrict the manner in which a franchisor recruits franchisees or selects its or its franchisees’ suppliers?

Neither the Franchise Act (applicable to franchise contracts governed by Italian law for franchisees that already operate in Italy) nor the Franchise Regulation (applicable exclusively to franchisees that operate only outside Italy, where the agreement is subject to Italian law) set any policies that restrict the manner in which a franchisor recruits franchisees or selects its own or its franchisees’ suppliers.

In particular, there are no specific restrictions on or requirements as to:

- the number of franchisees or franchisees that form the franchise network, and their characteristics;
- the number of franchising agreements executed, or shops held, by a single franchisee, or their locations;
- the locations of the franchised outlets, or the distances between outlets;
- the local content of goods and services purchased by franchisors or franchisees;
- the effect of the entry of a franchised network upon local companies; and
- the percentage yearly growth of the franchised network.

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 Franchise Act, the franchisee is part of a network of franchisees operating ‘within a determined territory’, so to be strategically distributed. That is the reason why:

- the franchisor must inform the franchisee about the outlets involved within the network (section 4.1(d) of the Franchising Act) and must inform the franchisee on an yearly basis about the changes concerning the other franchised outlets forming the franchised network (section 4.1(e)); 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).

Apart from the provisions set forth under the Franchise Act and the Franchise Regulation (in the case of a franchisor originally operating outside Italy), any other commercial provisions are left to the contracting parties, franchisor and franchisees. All parties should act in good faith while respecting the general contract and commercial laws, always balancing the interest of the franchisor in developing his uniform franchise network, with the interests of the franchisee who should be protected by the franchisor with respect to their rights as part of the network itself.

### 15 What is the compliance procedure for making pre-contractual disclosure in your country? How often must the disclosures be updated?

Pursuant to sections 4 and 6 of the Franchising Act, the franchisor must disclose to the franchisee a complete set of information, with the exception of that which is actually reserved or whose disclosure may violate third parties’ rights, at least 30 days before the stipulation of the contract.

Section 4 of the Franchising Act also states that the franchisor must make this disclosure to the prospective franchisee within the time frame indicated above. 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 forth by section 1375 of the Italian Civil Code. In light of the above, the Franchising Act sets no duty on the franchisor to update the information disclosed in the pre-contractual phase. However, in conformity with the good faith principle, the franchisor may be required by the franchisee to update the information provided in the pre-contractual phase if the update may be considered to be in the interests of the franchisee.

### 16 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 Franchise Act also applies to sub-franchising. The Franchise Act, however, does not provide any rules as to who must make pre-sale disclosures to the sub-franchisees. That said, given the fact that the sub-franchisor is delegated to manage the entire franchise structure of the franchisor 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 the franchisor apply as such to the sub-franchisor, it must therefore disclose at least what is provided for in article 4 of the Franchising Act (see question 17).

The sub-franchisor is obliged to act with regard to the sub-franchisees according to good faith, fair dealing and loyalty (article 6 of the Franchise Act) in the pre-sale phase (and also after); as to its relationship with the franchisor, it must in principle disclose any further information requested by the sub-franchisee that is reasonably relevant to the franchise business, unless such information can be regarded as confidential or the communication of the information would violate third parties’ rights.

### 17 What information must the disclosure document contain?

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, including the company name and registered capital and, if requested by the prospective franchisee, a copy of the franchisee’s balance sheets for the past three years or of the balance sheets drafted from the date of the beginning of the activity if it started less than three years earlier;
the performance of the franchise contract.

4. close and fair collaboration between franchisor and franchisee during relevant case law defines this good faith duty as the duty to maintain a franchise contract and franchising activity in general. In particular, the behave in good faith. As part of this is the duty for each party to disclose closure obligation is particularly strong in the pre-contractual phase.

18 Is there any obligation for continuing disclosure?

Pursuant to section 6 of the Franchise Act, the typical franchisor’s disclosure obligation is particularly strong in the pre-contractual phase. However, according to section 1575 of the Italian Civil Code, during the performance of the contract both parties are subject to a general duty to behave in good faith. As part of this is the duty for each party to disclose to the other any information or document that may be relevant for the franchise contract and franchising activity in general. In particular, the relevant case law defines this good faith duty as the duty to maintain a close and fair collaboration between franchisor and franchisee during the performance of the franchise contract.

19 How do the relevant government agencies enforce the disclosure requirements?

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, thus generating a legal remedy. On the other hand, violation of said obligation does not lead to any criminal consequences or involve any government agencies.

20 What actions can franchisees take to obtain relief for violations of disclosure requirements? What are the legal remedies for such violations? How are damages calculated?

As mentioned in question 19, the Franchising Act expressly provides for the remedy of 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 party to sign the contract.

As to damages, in principle only the material loss suffered and proved should be recoverable. Loss of profit should be excluded according to general principles of law. It is not yet clear whether loss of profit will be recoverable, as this provision of the Franchising Act has not yet been interpreted by the Italian courts.

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?

There is no statutory provision on this specific issue, however, as mentioned in question 15, in the case of sub-franchising the sub-franchisor must disclose to the sub-franchisees all the information required under section 4 of the Franchising Act. That said, the franchisor will be held liable for any disclosure violation to the sub-franchisor and the sub-franchisee connected to the information required under section 4 of the Franchising Act. On the other hand, if the disclosure violation occurs in the process of disclosure from the sub-franchisor and the sub-franchisees (such as, for example, delivering the information outside the 30-day term required by the Franchising Act) or does not consist of false information disclosed by the franchisor, or both, the latter will not be held liable for disclosure violation. In this case only the sub-franchisor will 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 have acted under tort (fraud or negligence) or have committed a crime sanctioned under the Italian Criminal Code.

This is the case provided that the franchisor and the sub-franchisor are structured as legal entities with limited liability (corporations) under the legal person rules.

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

As mentioned above, the Franchising Act provides for specific pre-contractual obligations both for the franchisor and the franchisee. The franchisor must exercise goodwill, fairness and good faith at all times in dealing with the prospective franchisee. Furthermore, the franchisor must provide the prospective franchisee with any information the franchisee should consider necessary or useful for the purposes of the franchise agreement in a timely manner. However, the franchisor can withhold such information which is reasonably deemed to be confidential information or if such a disclosure could infringe third parties’ rights. At the same time, the prospective franchisee must exercise goodwill, fairness and good faith at all times in dealing with the franchisor. The prospective franchisee 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, even if such disclosure is not expressly requested by the franchisor.

In light of the foregoing, as in any type of agreement, good faith, fairness and also loyalty general principles affect the offer and sale of franchises during pre-contractual, contractual and post-contractual phases pursuant to articles 1175, 1137, 1358 and 1375 of the Italian Civil Code.

In addition to the Franchising Act and Franchise Regulation, private organisations that may have an influence on franchise activity
include the Italian Franchising Association and the Italian Federation of Franchising, which have issued specific codes of conduct that all their members have to comply with.

23 Other than franchise-specific rules on what disclosures a franchisor should make to a potential franchisee or a franchisee should make to a sub-franchisee regarding predecessors, litigation, trademarks, fees, etc., are there any general rules on pre-sale disclosure that might apply to such transactions?

In addition to the provisions on pre-contractual disclosure set forth in the Franchise Act, any franchise transaction is also subject to the general obligations provided by the Italian Civil Code; in particular, the duty to act in good faith and therefore the duty of each party to disclose to the other any information or document that may be relevant to the franchise contract itself. There are no specific references to particular obligations for pre-sale disclosure.

24 What actions may franchisees take if a franchisor engages in fraudulent or deceptive practices in connection with the offer and sale of franchises? How does this protection differ from the protection provided under franchise sales disclosure laws?

See questions 19, 20, 28 and 29.

Legal restrictions on the terms of franchise contracts and the relationship between parties in a franchise relationship

25 Are there specific laws regulating the ongoing relationship between franchisor and franchisee after the franchise contract comes into effect?

Apart from those indicated in question 10, the general provisions set forth by the Italian Civil Code govern the contractual relationship.

26 Do other laws affect the franchise relationship?

In principle, the Italian Civil Code affects the franchise relationship, as it contains the general contract law. Both domestic and EU antitrust laws affect the franchise relationship; industrial (trademark, patents and industrial secrets) and other intellectual property laws also apply, mainly regarding the regulation of intellectual property rights in the absence of contractual regulations. Labour and employment laws and practices, consumer protection laws, data protection laws and bankruptcy laws may all also be relevant.

27 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 Franchising Association and the Italian Federation of Franchising have issued specific codes of conduct that all their members have to comply with. In principle, such codes may extend the obligations set forth by law to further protect the weaker party in the franchise relationship.

28 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?

A franchisor may terminate the 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, such as a default in payment of fees and royalties, violation of any exclusivity rights on the product or non-compliance with the franchisor’s standards. Given that it is a matter of interpretation, the agreement should clearly state the cases in which the franchisor can terminate the franchise relationship.

29 In what circumstances may a franchisee terminate a franchise relationship?

Similarly to termination by the franchisor, the franchisee may terminate in the case of default or non-performance of the contract terms by the franchisor. The breach must be serious, such as the franchisor unreasonably suspending the supply of goods to the franchisee.

If the franchisee terminates the agreement, it is also entitled to the reimbursement of initial fees and costs, damages, or both. In practice, because of the extreme difficulties of proving and quantifying damages, franchise agreements usually grant the right for the franchisee 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.

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

Pursuant to section 3.4(g) of the Franchising Act, renewal conditions must be set forth in the agreement. It is therefore crucial to state such conditions clearly in the agreement. In principle, however, there is no legal obligation for the franchisor to renew the franchise agreement.

31 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 within the contract. Restrictions are therefore permitted.

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

None of the legislative measures currently in force expressly rule on or restrict the nature and amount of fees.

33 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. In this case, however, the interest rate cannot exceed the usury rate that is fixed every three months by a ministerial decree. In general, the maximum rate is 10 to 20 per cent per annum, 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 (a variable rate of interest, depending on the fluctuation of certain institutional standard rates) and the Italian Civil Code.

34 Are there laws or regulations restricting a franchisee’s ability to make payments to a foreign franchisor in the franchisee’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. There are, however, certain anti-money laundering requirements that may impose specific restrictions. In principle, payments can be made only through an authorised bank or a financial intermediary (bank wire, cheques, etc). Cash over a certain amount (€12,500) can, in principle, be carried out of the country only if this is communicated to the competent authority (the Bank of Italy or the Financial Information Unit) and the relevant documentation is obtained.

35 Are confidentiality covenants in franchise agreements enforceable?

Yes. See question 40.

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

Article 6 of the Franchising Act sets forth the franchisor’s express duty to act under the principles of good faith, fair dealing and loyalty with regard to the prospective franchisee while in the pre-sale phase.

According to sections 1337 and 1375 of the Civil Code, any party has an obligation to deal with the other in good faith, during both the pre-sale and the after-sales phase (after the formation of the contract). This principle is also reaffirmed by a recent decision of the Italian Supreme Court stating that a franchising agreement requires a tight and loyal collaboration between the franchisor and the franchisees, both before closing and for the entire duration of the contractual relationship.
Failure to comply with such obligations can be taken into consideration by the judge in evaluating the liability of the parties, in calculating the damages and with respect to termination issues.

37 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 an undertaking. Therefore it has a fiscal code, and in general it is required to request a VAT 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 the franchisee from being treated as a consumer (but 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 products, where the franchisee is not obliged 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 the consequences linked to that, especially regarding the rights to withdrawal and other protection rights.

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

In principle, there is no obligation to provide franchise agreements in the Italian language. However, should the franchisee request an Italian version of the same, the franchisor must comply with said request as per section 3, paragraph 1 of the Franchise Regulation. As mentioned, the Franchise Regulation applies only to franchisors that operate their business exclusively outside Italy; however, the majority of scholars believe that this obligation also applies to foreign franchisors that operate in Italy.

39 What restrictions are there on provisions in franchise contracts?

Pursuant to section 3, paragraph 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, please note that such restrictions may be considered as harsh conditions that, according to article 1341(2) of the Italian Civil Code, must be expressly approved by a second signature.

Parties are free to choose the law governing the contract, as well as to enter into any agreements on arbitration or alternative dispute resolution rules.

With regard to competition restrictions, see question 40.

40 Describe the aspects of competition law in your country that are relevant to the typical franchisor. How are they enforced?

Market partitioning by territory or by custom is considered by the judge in evaluating the liability of the parties, in calculating the damages and with respect to termination issues.

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

The Italian court system has different kinds of 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 court of first instance, 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 an arbitration proceeding instead.

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

42 Describe the principal advantages and disadvantages of arbitration for foreign franchisors considering doing business in your jurisdiction.

The advantages of choosing an arbitration procedure for a foreign franchisor over ordinary court proceedings are as follows:

- speed (even though the arbitration decision may be appealed, which will 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 the common delays experienced in court; and

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Rödl & Partner

Roberto Pera
Irene Morgillo

Piazza Santa Anastasia 7
00186 Rome
Italy

roberto.pera@roedl.it
irene.morgillo@roedl.it

Tel: +39 06 96701270
Fax: +39 06 3223394
www.roedl.com
confidentiality – this is possibly the most important advantage granted by choosing arbitration over a court procedure.

The fact that the arbitration procedure and its relevant decision are 'private' may represent a significant advantage for a party who wishes to keep the results of litigation undisclosed. Furthermore, the franchisor may choose the applicable rules governing the procedure, the language of the arbitration and the seat. On the other hand, should the parties to a contract decide on arbitration, the major disadvantages are the very high cost of the procedure and the difficulty of finding experienced arbitrators (especially if the arbitration refers to highly specific areas of interest). Usually this is also a problem from another perspective: the parties to an arbitration are more inclined to choose an arbitrator for the arbitrator’s 'impartiality' than for the arbitrator’s skills as a judge. Another disadvantage is the growing standardisation of the arbitration procedure, which is increasingly making it seem like an ordinary proceeding.

43 In what respects, if at all, are foreign franchisors treated differently from domestic franchisors?

In principle, the only differences are laid down in the Franchise Regulation regarding pre-contractual duties where the franchisor operates outside Italy and provided that the agreement is subject to Italian law (see questions 11 and 17).

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 from national franchisors where a dispute arises in court.