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International Franchising in a Changing World

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NEWS FROM AROUND THE WORLD:

Will the Dutch Franchise Code receive a basis in statutory law?

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1. Introduction

In the Netherlands, there is no statutory law on franchising. There is a wide range of case law on franchising from which it is clear that civil law applies, including statutory and case law on contracts, as well as the specific rules on trademarks, trade names, and Dutch and European competition law. In addition, franchisors who are members of the Netherlands Franchise Association have to comply with the European Franchise Federation's European Code of Ethics for Franchising.

On 17 February 2016, the Dutch Franchise Code ("**DFC**")[1]was published. Although the DFC currently only has the status of a self-regulatory code (which normally should only apply if parties declare it applicable to their agreement), the Minister of Economic Affairs ("**Minister**") has on 12 February 2017 published a draft bill that gives the DFC a statutory basis.[1] There is a public consultation of six weeks as of the publication date to respond to the draft bill. The daft bill, as well as the DFC itself, is based on a 'comply or explain' principle. This means that deviating from the Code is possible but it needs to be motivated in writing. If the criteria therefore are not met, the contract(clause) can be nullified by the franchisee.

2. Statutory basis DFC

Because many large franchisors and the Netherlands Franchise Association have rejected the code as 'unbalanced' and in violation of the principle of freedom of contract, the Minister wants to give the code a statutory basis. The draft bill introduces an article in the Dutch Civil Code which gives a legal basis for an order in council ('*AMvB'*), that will declare the code binding for franchise relationships. An order in council is a Royal Decree, this is a law of lower standing that does not need to be approved by the Dutch Parliament. If sufficient basis in statutory law for the rules is absent, this may raise questions as to whether it meets 'democracy standards' and trias politica. AMvB's therefore usually will have a statutory basis in which the main elements and structure and scope of the rules are summarized. The draft bill is merely a formal 'delegation' to lower law makers. Some types of law cannot be delegated to AMvB's all, such as criminal law, but this is not the case for contract law. One could criticize the fact that the draft bill only lists topics that should be included in the code, but does not give any direction as to what the content of such rules could be (except for disclosure obligations, which are clear by listing them in the draft bill).

3. Content DFC

The DFC contains many 'open standards'. This is common in Dutch contract law and for many of these terms, case law has already developed a clear meaning.
Most of the 'rules' in the DFC, however in my view not perfectly drafted[2], are similar to the rules which currently apply. For example, a franchisor should protect and develop the franchise concept, should provide assistance to a franchisee if he needs it, etc. Another good example is termination of the franchise agreement. Pursuant to the DFC, parties must act in accordance with reasonableness and fairness (*redelijkheid en billijkheid*) in decisions on renewal and termination of the franchise agreement. This 'rule' is in accordance with Dutch contract law and the role of the reasonableness and fairness. Reasonableness and fairness can only be successfully invoked to set aside a contract term if the outcome in the given circumstances is 'unacceptable', a rather high standards. In reality, Dutch courts tend to be reluctant to set a contract term aside, even in franchise contracts which are usually very one-sided in favour of the

[1] http://www.franchise.nl/Portals/0/Nederlandse%20Franchise%20Code_1.pdf.

[1] https://www.rijksoverheid.nl/actueel/nieuws/2017/04/12/minister-kamp-presenteert-wetsvoorstel-voor-afspraken-franchisesector

[2] See for example the definitions and mixing of rules and explanatory comments.

franchisor. Similarly, Dutch law nor the DFC provide for goodwill or other forms of compensation upon termination. This can only be different if the termination itself was unlawful (a reasonable notice period has to be applied in case of a termination for convenience), or if the franchisee has made investments at the request of the franchisor or at a time he could not have foreseen the termination, that he has not been able to earn back before the end date. The DFC introduces a set of disclosure obligations, that are not yet present in statutory Dutch contract law. Some practice of disclosure is however common in the Netherlands, and the general rules for cancellation of contracts on the basis of 'error', or 'deceit' also make it in the franchisor's interest to disclose facts that are relevant for the franchisee's decision to enter into the agreement. Disclosure obligations are in line with international practice. Many franchisors have franchise systems and contracts that already include disclosure, and the DFC is based on 'comply or explain', so a franchisor may deviate if he does not want to disclose certain information. Proper disclosure in a way protects the franchisor from claims based on 'error' and 'deceit'. Dutch contracts law does not include an obligation to provide financial forecasts or prognosis, but if a franchisor does so, he may be liable for faults in particular if he is aware of the faults and does not inform the franchise thereof. The recent Supreme Court judgment in the case *Street One*[4]clarifies its earlier *Paalman / Lampenier*[5] judgment that if a third party provided the prognosis and it contains mistakes that the franchisor did not know about, the franchisor is not liable, but the contract may be cancelled based on (mutual) error. The situation is different if the franchisor prepared the prognosis. In this case he may be liable if he did not prepare the prognosis diligently. The DFC seems to imply that the franchisor should represent (or even guarantee) that the prognosis is correct, but this is already rejected by the Advocate General in his conclusion in the Street One case, and even though this wording is not included in the Supreme Court's judgment, usually the opinions of the Advocate General put in a lot of weight.

The DFC introduces that a franchisor should have operated pilot store(s) before rolling out a franchise system. Since this is also included in the EFF, and a franchisor may explain why he does not comply with this, it probably does not pose huge problems for franchisors.
More controversial is in my view the rule that a franchiser should not operate competing or secondary formulas. I think the presumption that this would harm the franchisees is not supported by facts, and the situation should rather be assessed on a case by case basis. Also, the rule that a franchisor should not unreasonably withhold consent if the franchisee wishes to open a new location or wishes to assign or terminate the franchise business, limits the freedom of contract, a recognized principle of Dutch contract law. The limitation that sourcing from particular suppliers (including the franchisor) may only be prescribed insofar as directly related to the performance of the franchise agreement raises the question whether this is aimed to follow the competition principles or to go further in restricting the franchisor. Also, the DFC presumes that there is an association of franchisees, that should agree to topics that have a material effect on the operation of the collective network. For major changes, a qualified majority of franchisee votes shall be necessary. If an individual franchisee does not agree but the association agrees, this franchisee may be terminated, but it may be necessary to release him of the non compete clause.

The franchise agreement should be in the language of the country where the franchisee is located. Even though language requirements are common throughout the world, these are very unusual in Dutch law. Not even employment contracts have to be in Dutch. Certain clauses may not be unilaterally changeable by the franchisor (such as franchise fees, payment conditions, use of trademarks, exclusivity, e-commerce and processing consumer data). The principle of reasonableness and fairness and contract law would in my view in certain circumstances limit a franchisor anyway to make certain clauses unilaterally revisable, and

[4] HR 24 februari 2017, ECLI:NL:HR:2017:311 *(Street One)*.

[5] HR 25 januari 2002, ECLI:NL:HR:2002:AD7329 *(Paalman/Lampenier).*

these topics seem to be key for the franchisee. Finally, the DFC refers to a dispute resolution committee (that does not exist yet), but it follows clearly from the draft bill that this is not mandatory and the parties may agree to as *ultimum remedium* to regular courts or arbitration.

4. Conclusion

At the moment, there is tension between franchisors and franchisees in the Dutch market. This has led to self-regulation, the DFC, which is not embraced by many franchisors causing the Minister's to publish a draft bill, that gives the DFC a statutory hook in the Dutch Civil Code.

Much of the content of the code is in my view not controversial, because such rules apply in many other countries in the world, and most internationally operating franchisors have already crafted the franchise system and their agreement in line with these requirements (for example disclosure, no rash terminations, etc.). The few controversial topics that are in the draft bill and the DFC may create the need for franchisors, to explain deviations in the agreement following the rules regarding form and content. If the draft bill would be adopted, and this is not certain at all because it should still go through the full parliamentary process including possible amendments, franchisors shall be recommended to review their franchise agreements and add on these points an explanation to the franchise agreement why the DFC is not complied with and to provide for Dutch language agreements..

Biography
Martine de Koning
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Specialisms:
Franchising, Distribution, Agency
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Martine studied law at the University of Utrecht graduating in 1995. She studied and lectured in the U.S.A. and Australia. In 1997 Martine joined Kennedy Van der Laan, where she started in information technology law and has in the last 15 years developed a practice in EU and Dutch competition law and international franchising, agency, distribution, sales, procurement, logistics and other commercial contracts and disputes. Martine has extensive experience with cross border franchising in the EMEA region and competition law compliance issues in this context. In particular North American clients seek her out for her experience in working with Anglo-American partners. She works for multinationals as well as strong national players with an international business or ambition. Martine handles the drafting and negotiating of contracts as well as litigation and (international) arbitration in national and international courts and arbitration institutes. Martine receives praise for her hands-on, pragmatic approach and sharp strategic vision. Martine regularly publishes articles and lectures on competition law, international franchising and related subjects.