

A NEW ERA

IN INTERNATIONAL FRANCHISING

34TH ANNUAL

IBA/IFA JOINT CONFERENCE

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News from Around the World

Europe

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European GDPR

The European General Data
Protection Regulation (GDPR):
Time For A Change Of Perspective

European GDPR

- I. Background
- II. What's new (and what is not)?
- III. Effects on (international) franchise networks
- IV. Cross-border data processing
- V. Is there anything good about it?

European GDPR

I. Background

1. From Directive 95/46/EC to Regulation (EU) 2016/679
2. The term “Data protection” as used in the EU
3. May 25, 2018: Are you ready?

European GDPR

- II. What's new (and what is not)?
 1. Burden of proof
 2. Market place principle vs. location of processor
 3. Increased level of fines
 4. General principles + “the right to be forgotten”
 5. Consent, Consent, Consent

European GDPR

- III. Effects on (international) franchise networks
 - 1. Material and territorial scope of GDPR
 - 2. Data protection by design and by default
 - 3. Appointment of data protection officer (DPO)
 - 4. Third party processors

European GDPR

- IV. Cross-border data processing
 - 1. Data transfers to “third countries”
 - a. General principles
 - b. Data transfer to the US: the EU – US Privacy Shield
 - 2. One Stop Shop

European GDPR

V. Is there anything good about it?

Well, that depends on the perspective:

1. Article 8 EU Charter of Fundamental Rights
2. IT experts' heaven – lawyers' so so delight
3. We're all data subjects
4. Marketing departments: time to cheer up!

News from Around the World

UNITED STATES OF AMERICA

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Franchising and the US Economy

- Expected 1.9% increase in outlets, to 760K in 2018
- Employment of > 8 million people in 2018
- Franchise output expected to grow 6.2% in 2018, to reach \$757 billion
- Growth Areas?
 - Personal services and health care franchises

Joint Employer Test: Shifting Sands

- Browning-Ferris: Flip-flop from Hy-Brand case
- Salinas case (FLSA): tougher standard
- US Congress: “Save Local Business Act” – failed
- State Laws: 19 states with “positive” or “proactive” joint employment laws

Anti-Poaching and No-Hire Provisions in Franchise Agreements Under Attack

- Anti-poaching provisions: franchisees cannot hire employees of another franchisee
- Antitrust and unfair competition challenges
- Class action suits from employees
- Washington State Attorney General investigations
- US Senate bill: “End Employer Collusion Act”

Franchise Disclosure: Changes?

- FTC Rule: Time to start the re-evaluation for an amended FTC Rule
- NASAA's FPR Commentary – fully implemented in 2018

Federal, State and Local Legislation

- State franchise relationship laws:
 - Florida, Pennsylvania, New Jersey
- Minimum wage laws: 29 states and DC
- Discriminatory franchise related laws

THE ECJ JUDGMENT IN THE COTY CASE

Europe

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THE ECJ JUDGMENT IN THE COTY CASE

- The facts of the case
- The legal framework for assessing restrictions on internet sales within the European Union
- The questions submitted to the European Court of Justice

THE ECJ JUDGMENT IN THE COTY CASE

1. Whether selective distribution systems are subject to the general prohibition of agreements restrictive of competition
2. Whether a ban for authorized dealers to use third parties online market places fall within the prohibition of agreements restrictive of competition

THE ECJ JUDGMENT IN THE COTY CASE

3. Whether a ban on the use of third parties online market places is exempted from the prohibition of agreements restrictive of competition
- Online selective distribution in third parties market places after the Coty judgment

THE ECJ JUDGMENT IN THE COTY CASE

- Restrictions to the use of online market places in franchising within the EU

News From Around the World

Canada

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In the Ontario Court of Appeal:

- *Raibex Canada Ltd v ASWR Franchising Corp*, 2018 ONCA 62
- *Mendoza v Active Tire & Auto Inc.*, 2017 ONCA 471
- *Trillium Motor World Ltd v General Motors of Canada Limited*, 2017 ONCA 545



Implemented and Planned Changes in Ontario



Employment Law Issues in Ontario





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PIPEDA

An orange graphic with a pattern of small icons. A white banner at the top left says 'ANNOUNCEMENT'. The main text reads 'Canadian mandatory breach notification starts November 1st' with 'No regulations yet' below it. A circular inset on the right shows server racks.

ANNOUNCEMENT

Canadian mandatory breach notification starts November 1st

No regulations yet

News from around the World

UK

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Overview

- **Liquidated Damages and the Rule against penalties**
- **Misrepresentation and Disclosure duties**
- **Good Faith and Fair Dealing**
 - Enforcing restrictive covenants
 - Exemption Clauses
 - Trademark protection
- And despite Brexit, GDPR will apply

Penalty Clauses

- Penalty clauses are not enforceable under English Law as a matter of public policy.
- A penalty is a payment of money stipulated in the contract that is excessive when compared with common law damages.
- Dunlop Test: Liquidated Damages must be “*a genuine pre-estimate of loss*”.
- New Development: It is thought that the Dunlop test has been applied too rigidly. This opens up for franchisors the possibility of imposing an additional financial burden on the franchisee to protect its non financial interests.

New Rule “Penalty is out of all proportion”

- *Makdessi*: Sale of Business. If the Seller breached the restrictive covenants he lost his entitlement to the outstanding (deferred) part of the purchase price.
- The Court of Appeal held that these provisions were penal, but this was overturned on appeal by the Supreme Court.
- The Supreme Court set the new test as follows: "whether the provision is a secondary obligation which imposes a detriment on the contract breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation".

New Rule “Penalty is out of all proportion”

- Lord Hodge stated the "correct test for a penalty is whether the sum is exorbitant or unconscionable when regard is had to the innocent party's interest in the performance of the contract".
- In *Makdessi*, the Court concluded that the provision protected the buyer's legitimate interest in enforcing the non-compete restrictions so that the goodwill of the business was protected. The goodwill of the business was critical to its value to the buyer. The provisions therefore did not go beyond protecting the buyer's legitimate interests.

Penalties Conclusion

- Excessive interest rates remain a penalty – the standard UK rate is 8 % so a rate of 2 % per month (25 % per annum) would not be valid.
- In my view this means that excessive liquidated damages for early termination of the franchise agreement also remain a penalty.
- However, liquidated damages for breach of non-compete can now be set higher, arguably at a more punitive level to protect the goodwill of the franchisor.

Good Faith

- There appears to be growing recognition that a duty of good faith may be implied into a relational contract such as a franchise agreement.
- This question first came up some years ago in *Yang Sen* where a duty of good faith was implied into a long term distribution agreement.
- Subsequently the point was argued unsuccessfully in a number of franchise cases where the contract already clearly set out the rights and obligations of the parties so that the Courts felt that an implied obligation was not required to give business efficacy to the contract.

Good Faith

- In *Tahnoon v Kent* the parties had entered into a Framework Agreement (joint venture) and claims were made based on breach of a duty of good faith.
- A duty of good faith was implied because the nature of the relationship was one in which the parties naturally and legitimately expected of each other greater candor and cooperation and greater regard for each other's interests than ordinary commercial parties dealing with each other at arm's length.
- In the circumstances the contract made between the parties was seen to be a classic instance of a relational contract. The implication of a duty of good faith in the contract was essential to give effect to the parties' reasonable expectations and satisfied the business necessity test as the relevant standard for the implication of a term into a contract.

Duty of Good Faith: Content

- “...the obligation of fair dealing is not a demanding one and does no more than require a party to refrain from conduct which in the relevant context would be regarded as commercially unacceptable by reasonable and honest people...”

Negligent Misrepresentation and disclosure of full facts

- There is no Franchise Disclosure Law in the UK.
- Franchisors are therefore only liable if there has been a misrepresentation.
- Typically this means that the Franchisor must have made a positive misstatement.
- However sometimes situations can arise where failure to disclose the full facts can amount to misrepresentation.

Negligent Misrepresentation and disclosure of full facts

- The extent of the duty was examined in *Property Alliance* a case of alleged miss-selling of financial products by a UK Bank. The Court had to decide the extent to which the Bank had to give “a full and proper explanation’ of the risks associated with the products it was selling.
- *“The ... duty would extend to correcting any obvious misunderstandings communicated by the customer and answering any reasonable questions the customer might ask about those products in respect of which the bank had chosen to volunteer information.”*

Disclosure and Misrepresentation

- The duty only arises if the banks decides to give an explanation. So there is an option to say nothing. Indeed many franchisors opt not to make any earnings representations
- In other words, if a franchisor does say not anything about the profitability of the franchise business, there is no duty to disclose key facts but if the franchisor does give explanations and recommendations it may be required to provide a “full” and “proper” explanation.
- However there is not a “duty to educate” or give a comprehensive “tutorial”

Disclosure and Misrepresentation

- But, can franchisors protect themselves, using “no reliance clauses” ?
- Typically a well drafted franchise agreement will include a no-reliance clause. Such a clause is an exemption clause and needs to pass the test of reasonableness under the Unfair Contract Terms Act (UCTA)
- When selling a franchise to an inexperienced new franchisee it can be unreasonable to impose a no reliance clause unless that clause is specifically brought to the attention of the franchisee and the franchisee is given a chance to fully clarify any misunderstandings

Other Points

- **Brexit and GDPR** – Dagmar will cover GDPR, the only difference for the UK will be that post-brexit the UK rules will begin to differ from GDPR – this is expected to be a small “creep erosion” but franchisors will need to ensure that for their UK businesses the UK version of GDPR is followed

News from around the World

Middle East

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Key Developments

- Kuwait: New Agency Law (2016)
- Oman: New Agency Law (2014)
- Qatar: New Agency Law (2016)
- Saudi Arabia: Draft Franchise Law (2017)

Principles of GCC Agency Laws

- Where a franchisee has successfully registered as a commercial agent, they enjoy certain benefits including:
 - Protection from termination and non-renewal;
 - Compensation payable at the end of the contract; and
 - Ability to prevent the appointment of another franchisee often through confiscation of imported products at customs

Principles of GCC Agency Laws

- Generally, to benefit from the protections of the law the agency needs to meet three requirements:
 - It needs to be exclusive;
 - It needs to be registered; and
 - Typically only 100% locally owned companies are able to make a registration.

Oman

- Mandatory Compensation for registered agents has been abolished
- The parties are free to determine the terms of renewal and termination
- Agents can still claim for breach of contract
- Foreign principal may sell directly in the territory so the agency is no longer exclusive
- The agent can no longer claim commission from parallel imports
- Finally the goods that are the subject of an agency dispute can no longer be banned

Kuwait

- Kuwait has one of the oldest agency laws in the Gulf dating back to 1964
- As of March 2016 the new agency law applies
- Agents can now be non-exclusive; this removes the monopoly
- The law clarifies that franchisees and distributors are deemed to be commercial agents (this was unclear under the old law)
- BUT: Registered agents can continue to claim compensation

Kuwait

- Only registered agents enjoy protection
- BUT: without registration the agency is not valid and no claim can be brought pursuant to an unregistered agency agreement
- Some authors read this provision to mean that no claim for compensation can be brought unless the agency is not registered
- BUT : the risk is that a franchise agreement that has not been registered may not be valid and enforceable.

Qatar

- New Agency Law in 2016
- Distributors are now expressly deemed as agents
- Franchisees that sell products of the franchisor are likely to be caught
- Only exclusive agents enjoy the protection of the law
- Law abolishes commission on parallel imports

Saudi Arabia

- Draft Franchise Law proposed in 2017
- Will enter into force 180 days after publication
- Has not yet been published

Saudi Arabia

- Whilst only Saudi Arabian Nationals can be registered agents the new franchise law proposes no such restriction on franchisees
- The Franchise Agreement will have to be registered
- A Disclosure Document will be required
- If financial performance representations are made they must be based on certain reasonable assumptions which may be verified by the Registration Authority

Saudi Arabia

- A new 2+1 rule
- Cooling off period: it is proposed that the franchisee has 7 days to walk away if they change their mind.
- Central Marketing Fee must be paid into an independent bank account
- Franchisee would have a renewal right
- Choice of Law and jurisdiction unclear.

Saudi Arabia

- Until the new franchise law comes into force, the commercial agency law will continue to apply
- Under that law a registered agent enjoys the usual protection
- As a matter of law registration is a legal requirement
- But in practice, most franchise agreements remain unregistered.
- Failure to register does not render the agreement unenforceable so the risk is on the agent.