

Franchise

In 25 jurisdictions worldwide

Contributing editor
Philip F Zeidman



2016

GETTING THE
DEAL THROUGH 

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DEAL THROUGH 

Franchise 2016

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Italy

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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 has been granted new structures, including the 'dual structure', where the management is appointed by a supervisory board (also exercising the control function) rather than by the shareholders. The Srl has been granted new forms of management, which can now be organised as 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, a simplified Srl was recently introduced. This entity 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 limited partnership and the partnership limited by shares. With some exceptions for the latter two entities, these forms of business entities do not enjoy the limited liability of shareholders.

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 €50,000 for an SpA (before 25 June 2014 the minimum share capital was equal to €120,000), €10,000 for an ordinary Srl and from €100 to €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 a foreign investor trying to acquire company participation 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, at a flat rate of 27.5 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 tax rate is set at a minimum of 3.9 per cent. Regions may increase this by up to 1 per cent;
- VAT – in general, VAT is 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 (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. 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.

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 no less than 25 per cent of the voting rights in the company receiving the payment, or a third company directly holds no less than 25 per cent of the voting rights both in the paying and in the receiving company or in the company the permanent establishment of which obtains the royalty payment (article 26-querter of Law 600/1973). A similar regime also applies to business entities located 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. 633/72) 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:

- he or she is registered with the Registry of the Resident Population and stays in Italy for more than 183 days;
- he or she is resident or domiciled (principal place of business and interest) in Italian territory and stays in Italy for more than 183 days; or
- he or she stays in Italy for more than 183 days.

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 that have their own VAT position and are resident in Italy).

Tax on certain types of income, however, is subject only to WT at source. Applicable tax treaties against double taxation may provide for more favourable tax rates for individuals.

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 recently approved 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 to 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 25 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. 2790/1999 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 anti-competitive 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 (namely 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.

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 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 Franchise Act, for foreign franchisors the minimum business requirements must be evaluated on a case-by-case basis.

In conclusion, 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.

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 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 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 franchises 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, lett '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, lett 'd' of the Franchising Act) and must inform the franchisee on an yearly basis about the changing concerning the other franchised outlets forming the franchised network (section 4.1, lett. 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).

Aside 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 1,375 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:

- (i) data regarding the franchisor, including the company name and registered capital and, if requested by the prospective franchisee, a copy of the franchisor'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;
- (ii) information concerning the trademarks used in the network, including registration details, or (if applicable) information concerning the licence granted to the franchisor by the owner of the trademarks;
- (iii) a summary description of the activities and characteristics of the business concept of the franchise network;
- (iv) a list of franchisees operating within the network and the stores of the franchisor;
- (v) 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 franchising activity if it started less than three years ago; and
- (vi) a summary description of court or arbitration proceedings, or both, involving the franchise network at issue, which 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. The requirement of respecting the relevant data protection provisions is fulfilled if the information disclosed regards the judicial authority issuing the decision, the date of the decision, its registration number and its summary description. The latter can be limited to the description of the claims raised within the proceedings and the outcome of the same.

With reference to the information mentioned under (iv), (v) and (vi) above, the franchisor may only supply information linked to activities carried out within Italian territory.

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

- a list of franchisees operating within the network and of the stores of the franchisor sorted country by country; if requested by the franchisee, the franchisor will also have to supply the former with a list of at least 20 franchisees operating within the network and their relevant locations. Should the number of franchisees be lower than that mentioned above, the franchisor will have to supply the franchisee with the list of all franchisees of the network. Both lists may also be provided by digital means;
- an indication of the annual variation - sorted country by country - of the number of franchisees and their relevant location within the past three years, or, if it started less than three years ago, from the beginning of the franchising activity; and
- a summary description of any court proceedings concluded with a final judgment within the three years preceding the stipulation of the contract; also, arbitral proceedings concluded with a final award within the same term as that described above. Both the court and arbitration proceedings must concern the franchise system. In this regard, the franchisor will have to provide at least the following information: the parties involved, the judicial or arbitral authority, the claims and the decision or award.

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 1,375 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 1,439 of the Italian Civil Code, together with compensation for damages, if due, as per section 8 of the Franchising Act.

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? If the franchisee can cancel or rescind the franchise contract, is the franchisee also entitled to reimbursement or damages?

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 1,439 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 or not, as this provision of the Franchising Act has not yet been interpreted by the Italian courts.

21 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.

22 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, 1337, 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 which 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 franchisors'

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, due to 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, paragraph 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, paragraph 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 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. 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 1,337 and 1,375 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-sale 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 which, 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 EU Vertical Restraints Regulation and the Italian Antitrust Law as a hardcore restriction, and is therefore not exempt from sanctions. There are, however, some exceptions to said rule that can be included in a franchise agreement in favour of the franchisee.

Resale price maintenance (RPM) is considered illegal under the EU Vertical Restraints Regulation and the Italian Antitrust Law. There is an exception for fixing a maximum price level, or recommending a certain price for products or services, provided that 'they do not amount to a fixed or a minimum sale price as a result of pressure from, or incentives offered by, any of the parties' (article 4.1(a), Regulation 330/2010).

Following the release of the new version of the Commission Regulation (330/2010), the EU Commission issued additional policy guidelines on vertical restraints, dated 19 May 2010, introducing some new interpretations on the RPM. As a general rule, section 223 and 224 of the guidelines expressly confirms that RPM has to be treated as a hard-core restriction; however, section 225 provides that companies have the possibility to use the RPM in particular circumstances, and provided that its use generates an increase in the efficiency levels and a positive effect on the market and on the consumer; a positive effect that is able to set-off and overcome any possible negative effect usually created by vertical agreements.

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.

Italy has specific arbitration rules, which are set forth in the Code of Civil Procedure. Parties may choose between a 'ritual' arbitration under said rules, an arbitration under the rules of a chamber of commerce (typically Milan), or any other relevant domestic or international organisation (eg, ICC, Rome branch).

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
- 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.

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