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## Franchising in Europe: An Agenda for Harmonisation and Reform?

The franchising industry in the European Union (EU) currently faces a patchwork of regulation.

A small but significant minority of Member States (such as France, Italy, and Spain) have enacted specific laws focused on the manner in which franchisors sell their franchises to franchisees, as well as the rights and duties of the parties once a franchise has been granted. Most EU Member States (including the UK) do not, however, have specific franchising laws and leave regulation of the franchising sector to laws applicable to commercial activity generally.

This includes generally applicable EU competition law, which impacts the franchising industry in a number of ways. For instance, it prohibits franchisors from imposing minimum resale prices on franchisees (a practice known as “resale price maintenance”) and from exercising effective control over the online sales activities of the franchisees (*e.g.*, by way of online sales bans). In this context, it should be noted that from a competition law perspective, franchisors and their franchisees constitute separate, independent market actors and the relationship and arrangements between them must be consistent and compliant with standard EU and national competition rules.

Against this backdrop, the Internal Market and Consumer Protection Committee (IMCO) of the European Parliament recently published a study<sup>1</sup> looking at the impact of regulation on the franchising industry in Europe (the study).

The study argues that the current regulatory environment at both an EU and Member State level is dysfunctional and creates disincentives to the use of franchising systems in the EU. This results in missed economic opportunities for franchisors and franchisees, and ultimately deprives consumers of the greater choice that healthy franchising activity can bring about. The study illustrates this by pointing to the fact that the franchising sector accounts for only 1.86 percent of the EU’s GDP compared with 5.95 percent of the GDP of the United States. In addition, a large proportion of franchising activity in the EU is concentrated in a small number of its Member States.

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<sup>1</sup> IMCO (2016) Legal Perspective of the Regulatory Framework and Challenges for Franchising in the EU. Available at: [http://www.europarl.europa.eu/RegData/etudes/STUD/2016/587317/IPOL\\_STU\(2016\)587317\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/STUD/2016/587317/IPOL_STU(2016)587317_EN.pdf).

To enable the franchising model to fulfil its potential, the study recommends harmonising regulation of franchising across the EU through the introduction of EU-wide targeted legislation. According to the study, this would remove the barriers to EU-wide rollouts of franchises created by the current patchwork of regulation.

The study puts forward the following three areas of focus for the proposed legislation:

### **1. Promoting market confidence in franchising**

The study highlights the importance of demonstrating that a franchising model offers positive advantages to all involved. According to the study, the proposed legislation should, therefore, increase market confidence in franchising by requiring adequate pre-contractual disclosure by franchisors, focusing regulation only where it is required and allowing franchisees to compete on a level playing field with large corporate chains.

In the latter context, the study strongly recommends changes to EU competition law to enable franchisors to set the prices which franchisees charge to their customers and to restrict franchisee sales over the internet. The study suggests these proposed amendments would enable franchised businesses to compete with large corporate groups which, due to their vertically-integrated nature, are not bound by the EU prohibitions of resale price maintenance and online sales bans. As a result they have the ability to deliver on “price promises” and can shape their online sales strategies much more effectively than a franchised business.

### **2. Ensuring pre-contractual “hygiene”**

The study suggests including the following requirements in the legislation to ensure that the parties, particularly franchisees, are fully aware of the rights and obligations attached to a franchise opportunity before entering into a franchise arrangement:

- > disclosure by franchisors of the key features of the franchise opportunity in a set form and plain language, to be provided 15 working days before execution of the agreement or payment;
- > disclosure of the identity and experience of the franchisor and its litigation and bankruptcy history, the franchise network in the target (or an analogous) market, a summary of the key terms of the franchise agreement and any earning claims, as well as a copy of the franchise agreement in the form in which it will be executed;
- > ensuring that franchisees are strongly encouraged to take and follow expert legal advice prior to entering into any franchise agreement; and
- > implementation of a cooling-off period of five days after execution of any franchise agreement.

Noncompliance with the above requirements would give rise to personal liability for individuals responsible for inaccuracies in the disclosed information. If noncompliance results in defective consent, franchisees would have the right to terminate or claim damages within 12 months of becoming aware of the noncompliance, or 24 months from the date of execution, whichever is later. In addition, penalties could be imposed on the franchisor by regulatory authorities including rescission of the franchise and related agreements, damages, or penalties including disqualification.

### **3. Ensuring a fair relationship between franchisors and franchisees**

In order to ensure a fair relationship between franchisors and franchisees after execution of a franchise agreement, the study suggests the imposition of the following mandatory terms on franchisors and franchisees.

*Mandatory terms on franchisees to act fairly towards the franchisor:*

- > not to challenge the franchisor's intellectual property;
- > to implement the business format;
- > not to compete with the franchisor during the term and for a reasonable period thereafter;
- > to allow the franchisor the right to purchase the franchisee's business upon termination;
- > to allow termination for cause without compensation;
- > to allow the franchisor a pre-emptive right of purchase;
- > to impose a duty of confidentiality; and
- > to purchase tied goods and services from the franchisor or its nominated suppliers.

*Mandatory terms on franchisors to act fairly towards the franchisee:*

- > to be the owner of, or have the right to licence, the intellectual property rights on which the franchise is based;
- > to provide a reasonable level of support and training to the franchisee;
- > to refrain from encroachment;
- > to allow the franchisee the right to sell its business, subject to the franchisor's pre-emptive right of purchase; and
- > not to supply goods or services to the franchisee at inflated prices or goods or services which are unfit for purpose.

**Conclusion**

The deliberations of the IMCO regarding the regulation of franchising in the EU are set to continue for some time, with the final committee vote scheduled for April 2017. Whether or not this initiative results in the significant level of intervention envisaged by the proposed EU-wide legislation, it certainly indicates an increased level of support for harmonisation of regulation in this area and for the use of franchising models more generally. For franchise businesses interested in expanding in the EU, but who have encountered difficulties in navigating the current regulatory patchwork, this presents an opportunity to contribute to the debate and push for change.

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