

NOTE ON:

LAWS REGULATING FRANCHISE BUSINESS IN DIFFERENT JURISDICTIONS

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Abstract

In franchise business the franchisor allows the franchisee to use its trade mark, trade name, logos, industrial designs, symbols, emblems and designations in return for royalty related payments. In this rapidly expanding form of doing business, different jurisdictions regulate it differently: by enacting franchise specific regulations; developing court practices or through general contracts provision that protect. Such regulations are primarily meant to protect the franchisee from the information asymmetry and financial and technical power of franchisor. Franchise business regulations and general contract provisions jointly regulate contemporary national and international franchise business.

Keywords: Business, contract, franchise, royal,

I. INTRODUCTION

Franchise is “a marketing channel, business structure, legal relationships and the form of governance of business between the franchisor and the franchisee”.¹ It is national and international strategy for doing business. In this system of doing business franchisor allows the franchisee to use its trade mark, trade name, logos, industrial designs, symbols, emblems and designations. The franchisee in return pays royal fees and other fees based on their agreements. It is a rapidly expanding form of doing business in the international trade.

This mode of business is formally developed in 1950s in US from the lived experience. Later on, it has expanded to the other parts of the world. Nowadays, business franchise has significant contribution to the development of international business since companies can easily franchise their products and services in foreign markets through forming business channel. In relation to regulation of franchise business, there were no specific regulations before 1970s. However, after 1970s, since there were significant problems between the franchisor and franchisee which cannot be resolved by the conventional agreement of the parties, legislations and court actions which regulate the circumstances were developed. In this regard, more than 30 countries have enacted franchise specific regulations to regulate franchise relations. In addition to this, some countries regulate franchise relations by consumer protection laws, competition laws, commercial laws, and general contract laws while other states regulate it simply through court practices of interdisciplinary application and interpretation of laws. Currently, there is no

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¹ ELIZABETH CRAWFORD SPENCER, THE REGULATION OF FRANCHISING IN THE NEW GLOBAL Economy (Edward Elgar Publishing) 47 (2010).

binding international franchise law. However, international model franchise laws, tax conventions, bilateral trade agreements, investment treaties etc. actually affect business franchise internationally.

In Ethiopia, there is no specific law that regulates franchise business. However, franchise business is technically regulated by general contract law, commercial law, competition law, investment law, intellectual property law, commercial registration and business license laws. This note provides a review of laws in different jurisdictions, more specifically US, Poland, South Africa and Model Law. The selection was made taking in to account the approaches that the states follow in the regulation of business franchising, the strength of the jurisdiction and similarity of the character that the states have with Ethiopia in government structure, development policy, and legal system. Besides, the approach followed by the UNIDROIT model laws are also selected for discussion.

II. CHARACTERISTICS OF FRANCHISE BUSINESS VIS-A-VIS GENERAL CONTRACTS

Franchise business has certain similarities and differences with general contracts. It had basically developed from general contracts. General contract refers to a negotiation in which two parties having capacity and equal bargaining power come together to conclude binding agreement. However, franchise business refers to an agreement by which franchisor grants the franchisee the right to carry out business under his/her marketing system. In case of business franchise, the franchisor and the franchisee have no equal power to make negotiation.² The franchisor's offer is take or leave type in which the franchisee have no negotiating power and the franchisor have the power to dominate the negotiation. The unequal power of the franchisor and the franchisee affects the fairness of the contract among themselves. Franchise business also includes a wide range of agreement which is very much complicated.³ In franchise business, the franchisor has asymmetric power over the franchisee mainly to bring product uniformity.⁴ Such uniformity of quality of products have great place in franchise relationship.

Franchise business had been regulated by the general contract law in the past in different jurisdictions. However, nowadays, in most countries where franchise business is well developed, it is regulated by the government regulatory laws in addition to the contract of the parties. In countries that have franchise specific regulations, the regulation of franchise business is not something which is entirely left for freedom of contract of the parties unlike in the case of countries that regulate their franchise business by general contract. In general contract law, the contracting parties have freedom to negotiate and fix terms of contract as long as it does not violate the laws of the state and public morals.⁵ Likewise, under franchise business regulations, there are things that parties are necessarily required to do and not to do.

² Mark Abell & Victoria Hobbs, *The Duty of Good Faith in Franchise Agreements: A Comparative Study of the Civil and Common Law Approaches in the EU*, 11 (X) INTERNATIONAL JOURNAL OF FRANCHISING LAW 2-5, (2013), p.2-5

³ LARRY A. DIMATTEO, *THE LAW OF INTERNATIONAL BUSINESS TRANSACTIONS* (2003), 90-93

⁴ *Id.*

⁵ Civil Code of the Empire of Ethiopia, Proc. No. 165/1960, Negarit Gazeta, *Gazzet Extraordinary*, 19th Year No. 3, Addis Ababa, 5th May, 1960, Art.1678.

In franchise business relationship, the franchisor and the franchisee are institutionally independent. The franchisor and the franchisee operate their own capital, labor, and administration. However, the two institutions provide uniform service or products under the control of the franchisor.⁶ Further, the two institutions run their business under the same trademark, brand and business plan of the franchisor. Besides, they share common trade secret, promotion advantage etc. That means they are independent institutions on one hand and interdependent on the other hand. The franchisor and the franchisee do business in coordinated way. In such case, the franchisor who owns the already successful business allows the franchisee to use his/her trade mark, trade name and products in return for payment of royalty fee.

In this nature of relationship, the problem emanates from information asymmetry and financial and technical power of franchisor. Franchisor can dominate the negotiation between the two due to his/her financial and technical advantages. As a result, governments play the regulatory role by intervening in franchise business relations to protect the interest of franchisees-the weaker party in the transaction.

The way governments approach the regulation of franchise business may differ from jurisdiction to jurisdiction. Some countries have regulated franchise business by enacting franchise specific regulations; some have developed franchise regulations from court practices and some others have regulated the franchise business in their general contracts law by having provisions which protect parties which have no equal bargaining power during negotiation of contract. The development of contemporary franchise specific regulations is primarily aimed at restricting the power of the franchisor, the grandfather of the relationship. Once again, even if the regulation intervenes or limits freedom of contract of the parties, it has left some issues for the agreement of the parties.

Franchise business regulations and general contract provisions jointly regulate contemporary national and international franchise business. Franchise specific regulations require effective general contracts laws to fully regulate franchise business. In the absence of general contracts law, franchise business cannot be solely regulated by franchise specific regulations. In this regard, the two are mutually interdependent. Even in countries where franchise specific regulations are available, the rights and obligations of franchisors and franchisees emanate from both franchise specific laws and contracts. Moreover, general contract law has great contribution in regulating franchise business particularly in jurisdictions where franchise specific regulations are missing.

III. ADVANTAGES AND DISADVANTAGES OF FRANCHISE BUSINESS

Franchise business has both advantages and disadvantages for both the franchisee and the franchisor.⁷ To start with its advantages, currently, franchise business are used as a tool for

⁶ Rajiv P. Dant, Marko Grünhagen and Josef Windsperger, *Franchising Research Frontiers for the Twenty-First Century*, 87 (3) JOURNAL OF RETAILING 253-268 (2011).

⁷ David E. Holmes, *The Advantages and Disadvantages of Franchising*, Southern California Office, at 2, available at; http://www.holmeslofstrom.com/z_pdf/articles/franchisors/Fran%20Advantages.pdf (accessed on October 2016).

promoting development particularly in Africa.⁸ Franchise business contributes for economic development by facilitating technology transfer and know-how as the franchisor usually provides training for the franchisee.⁹

The franchisee among other things starts business with already tested and successful products. This drives him/her to the advantage of access to existing brand and operating systems.¹⁰ The customers' prior awareness of brand has its own positive value for franchisee. Besides, the centrally organized marketing and brand promotions have advantage for the franchisee.¹¹ Moreover, the ongoing advice, guidance, support, consultations and training offered by the franchisor are also the advantage that franchisee can get.¹² Franchise business is especially beneficial for small and medium scale business institutions that want to expand their products and services. Moreover, the franchisee will exercise individual ownership of businesses, get reduced risk of running new business, easily enter in to the business, and even get reduced burden of opening business.¹³

From franchisor point of view, franchise business has advantages of spreading capital costs for products and services, rapid market expansion and easily developing trademarks. Moreover, it facilitates the distribution of services, maintaining quality control and it brings overall economic efficiency for the franchisor. Similarly, it enables international business franchises to easily penetrate their goods and services in the foreign markets. They can expand their markets in foreign markets without having challenge with the legal requirements, licensing, construction costs etc in foreign states. This facilitates international business by reducing transaction costs.

On the contrary, franchise business has its own disadvantages.¹⁴ The disadvantages start with the existing power balance between franchisor and franchisee.¹⁵ Because franchisor and franchisee have no equal bargaining power, franchisors may abuse their powers. The abuses, the overreaching and the opportunistic behavior of franchisor can be taken as the disadvantages of franchise business.¹⁶ Not only this but also franchise business might have disadvantages from trade competition perspective. The existence of fair trade competition ultimately benefits consumers. The existence of strong trade competition promotes consumer wellbeing. Since there is no trade competition between franchisor and franchisee, it avoids the benefits that consumers can derive from competition. The other disadvantage of franchise is that franchise business does not encourage creativity and innovation. Franchisees have no independence to create new

⁸ The African Development Bank Group, Enhancing Development in Africa: Franchising Report, at, 1-3 available at; https://www.afdb.org/fileadmin/uploads/afdb/Documents/Generic-Documents/003_FRANCHISING.pdf (accessed on September 2016)

⁹ *Id.*

¹⁰ *Id.* at 5-8.

¹¹ *Id.*

¹² *Id.*

¹³ *Id.*, at 3-5.

¹⁴ *Ibid.* See also Griffith University-Asia Pacific Center for Franchising Excellence, Advantages and Disadvantages of Franchising, available at; https://www.griffith.edu.au/_data/assets/pdf_file/0011/599627/Advantages-and-Disadvantages-of-Franchising.pdf?bustCache=52013702 (accessed on September 2016).

¹⁵ *Id.*

¹⁶ *Id.*

products or services. Franchisees have to act under the strict guidance of franchisor. This has the effect of discouraging creativity and innovation.¹⁷ Besides, franchise business is limited by time. Franchisors allow franchisees to use their franchised trademarks or brands for a limited period of time. This can also be the other disadvantage of the franchise business as its age may be shortened irrespective of its profitability.¹⁸ Finally, franchisee's obligation to pay franchise fees to the franchisor can also be considered as disadvantage.¹⁹

IV. TYPES OF FRANCHISE BUSINESS

Depending on the circumstances franchise business can be divided into different categories. As mentioned above, historically, there were two different types of franchise business; traditional franchise business and formal business franchise.²⁰ Traditional franchise business as the name implies is informal franchise business that was the prevailing before 1950s.²¹ On the other hand, formal business franchise is the formal and broader form of business franchising which has developed after 1950s.²²

The other category of business franchising is the product or trade mark franchising and business format franchising.²³ These are the two primary forms of business franchising. This category depends on the type and scope of rights that franchisors give the franchisees. The product or trade mark franchising is the simple form of business franchising.²⁴ In product/trade name franchising, a franchisor owns the right to the name or trademark and sells that right to a franchisees.²⁵ In this type of business franchising, only a single or limited number of intellectual property rights are used. It is most often seen in the soft drink or automotive industry, where a product is sold or distributed through a franchisee. However, business format franchising is broader than the product/trade mark franchising. In this type of franchising, the franchisor and franchisee have an ongoing relationship, and the franchisor provides a full range of services, including site selection, training, product supply, marketing plans, and even assistance in obtaining financing.²⁶

Further, franchise business can be divided into masters franchising and direct franchising based on the relationship between the franchisor and the franchisee.²⁷ In master franchise business, the franchisor makes contract with the sub-franchisor or the master franchisor and

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ Tamara Milenkovic Kerkovic, *The Main Directions in Comparative Franchising Regulation – UNIDROIT Initiative and its Influence*, 13 (1) EUROPEAN RESEARCH STUDIES 105-109 (2010)

²¹ *Id.*

²² *Id.* See also UNIDROIT, Model Franchise Disclosure Law, (Rome) 13(2002). Available at <http://www.unidroit.org/english/modellaws/2002franchise/2002modellaw-e.pdf> (Accessed on September 2016).

²³ *Id.*

²⁴ *Id.*

²⁵ *Id.*

²⁶ *Id.*

²⁷ UNIDROIT, UNIDROIT Franchising Guide, (Rome, Italy, 2nd ed., UNIDROIT), 300-301, available at; <http://www.unidroit.org/english/guides/2007franchising/franchising2007-guide-2nd-e.pdf> (Accessed on April 2017).

licenses the master franchisor to further franchise the business to the sub-franchise.²⁸ In master franchising, there is contractual relationship between three parties, the franchisor, master franchisor and sub-franchisee. The franchisors have contractual relationship only with the master franchisors. In this complicated type of franchising, the master franchisor controls the franchisee (sub-franchisee). This type of business franchise is applicable especially in international franchises. However, in case of direct franchise the franchisor directly makes franchise agreement with the franchisee.

V. NATIONAL AND INTERNATIONAL FRANCHISE BUSINESS

Franchise business can be done at national or international level. National franchise as the name implies is the franchise which is conducted in a single country's political territory between the franchisor and the franchisee. It is governed solely by the domestic laws of the country. In federal set up like the USA, the national franchising is regulated by the laws of the specific states in which the business is operated subject to compliance with the federal franchise laws. Further, if the franchise companies run their business in different states, it is regulated by the law of the franchisor state or by the federal franchise disclosure law. All in all, the business franchising is regulated by the national laws at the national level.

International business franchising implies the franchising business that is extra territorial. In this type of franchising, the franchisor and the franchisee live in different states. Currently, this type of business franchise is becoming one mode of penetrating or investing in a certain foreign markets.²⁹ There are a number of international business franchises in the world. The international business franchise can be direct unit franchising or the master franchising based on the agreement of the parties.³⁰ However, master franchising is the best type of franchising as it can easily facilitate the administration, market promotion, and protection of brand for the companies. Regarding the regulation of international business franchising, there is no international law which regulate this type of business. Even if there were some initiatives to have international business franchise laws, there was no success owing to countries reluctance to endorse it. In practice international franchise business is basically governed by the laws of the franchisors states.³¹ Besides, different laws of the franchisee states also have an indirect impact on the regulation of the franchise business.³²

²⁸ Id. See also Héctor R. Lozada, J. Hunter, Jr., Gary H. Kritz, *Master Franchising as an Entry strategy: Marketing and Legal Implications*, 4 (1) THE COASTAL BUSINESS JOURNAL 16-18 (2012).

²⁹ LARRY A. DIMATTEO (2000). THE LAW OF INTERNATIONAL CONTRACTING, (Kluwer Law International) 360 (2000).

³⁰ *Id.*

³¹ *Id.* See also <http://whoswholegal.com/news/features/article/28705/regulation-international-franchising> (Accessed on May 2017).

³² UNIDROIT, Guidelines to International Master Franchise Arrangements, (Rome, 2nd ed.) (2007).

VI. LAWS GOVERNING FRANCHISES IN DIFFERENT JURISDICTIONS

Laws governing franchise business are different in different countries, and follows different approaches.³³ Some countries have pure franchise specific regulations which govern the business relationship between the franchisor and the franchisee. In these countries, the regulations specifically focus on the areas of potential abuse in franchising such as pre-contractual disclosure and the inter-relationship between the franchisor and franchisees. These are generally symptomatic of more developed markets and are found in the USA, Australia, Canada, Brazil, Taiwan, Georgia, Mexico, France, Spain, Italy, Belgium and Sweden. Some of the laws in these countries are developed from the consumers' protection laws and competition laws. Currently, literatures show that there are around 30 states that have franchise specific laws in the world.³⁴

On the other hand, some countries have franchise specific regulations in the form of foreign trade/investment regulations. These types of regulations have protectionist economic policy or other political aims, such as the distribution of wealth. These are found in developing countries like China, Indonesia, South Korea, Malaysia, Moldova, Russia, Ukraine, Belarus, Barbados, South Africa and Vietnam.³⁵ Some other countries have no franchise specific regulations which govern the franchise business but they govern the relation by the general commercial law, contract laws and antitrust regulations that are aimed at preventing restraint of trade and generally focus on competition laws. These types of laws are found in Poland, German³⁶ and Japan.³⁷ In these countries, the courts apply general legal concepts and laws dealing with other forms of inter party relationship in the regulation of business franchising.

In addition to the above mentioned laws, the International Institute for Unification of Private Laws (UNIDROIT) has prepared franchise specific model laws. UNIDROIT has prepared two model laws for regulation of franchise business; the guide to the master franchising and model franchise disclosure law.

The franchising laws of the USA, Poland, South Korea, South Africa and the UNIDROIT Model Law are briefly discussed below.

A. United States

United States is considered as the creator of the modern franchises business. In USA, there are a number of franchise business (both national and international) which are regulated by franchise specific legislation.³⁸ As the USA is a federal state, franchise business is regulated by

³³ John Sotos, *Recent Trends In Franchise Relationship Laws*, paper presented by the International Franchising Committee at the IBA Annual Conference in Dubai on 30 October 2011 to 4 November 2011, 3-6

³⁴ *Id.*

³⁵ *Id.*, see also <http://whoswholegal.com/news/features/article/28705/regulation-international-franchising> (Accessed on April 2017).

³⁶ Article, 101 of the Treaty on the Functioning of the European Union (TFEU) and the Vertical Restraints Block Exemption.

³⁷ Japan Fair Trade Commission Guidelines (2002) – These provide for disclosure and offer guidance on vertical restraints, see also Mark Abell, *The Regulation of Franchising Around the World*, INTERNATIONAL JOURNAL OF FRANCHISING LAW VOLUME 9 - Issue 3 – 2011, Claerhout Publishing Lt, p.1

³⁸ Lafontaine and Fiona Scott Morton, *Markets State Franchise Laws, Dealer Terminations, and the Auto Crisis Francine*, 24 (3) JOURNAL OF ECONOMIC PERSPECTIVES 233–250 (2010); Douglas D. Smith, Ryan D. Smith, Bradley

both the federal government and the states governments.³⁹ At the federal level, the Federal Trade Commission (here after FTC) is an organ that has the mandate to govern business franchise. This organ has enacted rule on Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures in 1979 to regulate the information that franchisors are required to supply the prospective franchisees. Later on, the rule was amended again in 2007. The main reason for the amendment was to take notice from the past experience and to provide more protection for the interests of the franchisee. Like the 1979 franchise rule, the 2007 FTC franchise rule allows the state regulators to impose additional protection for franchisee such as registration and strict disclosure requirements.

Regarding the scope of application, the FTC rule is applicable all over the country. In US, since the federal laws are superior to state laws, the federal franchise rule overrides the states franchise laws if there is conflict between the two. But the federal franchise rule provides minimum requirements for the regulation of business franchise. Hence, states cannot provide a protection less than the minimum protection stipulated under the federal franchise rule. But they can provide better protection for the franchisee.

The FTC rule only deals with the disclosure laws. It has detailed information that the franchisor has to provide the franchisee before conclusion of franchise agreement. It does not provide any registration requirement and also does not govern the relationship issue. Similarly, it does not require registration, filing and approval of the disclosure document. At the federal level, the FTC rule only provides the pre-sale disclosure law. It has made pre-sale disclosure mandatory requirement. At the federal level, the relationship issue is not regulated. However, the two federal statutes regulate the relationship issue in specific industries. The Automobiles Dealer Franchise Act⁴⁰ and Petroleum Marketing practices Act⁴¹ require the franchisor to act in good faith during termination, cancellation and renewal of franchise contract. If franchisors fail to comply with these principles, the acts impose civil liability on them.

Equally important, the FTC has the power to investigate whether the franchisors are complied with the franchise rule or not and to take measures on the violation of franchise rule. When the franchisors are found to violate the rule, the FTC may issue cease-and-desist orders;⁴² bring suit in federal court for preliminary and temporary injunctions and restraining orders;⁴³ seek and obtain permanent injunctions; and seek civil penalties of up to \$10,000 for each act or practice found to be unfair or deceptive if the defendant had actual knowledge that the act or practice was unfair or deceptive.⁴⁴ In addition to this, it can also seek criminal penalties for the

D. Smith, Government Regulation of Franchises, Available at <http://www.franchisesmith.com/site/1040fran/Franchise-Government-Regulation-of-Franchises.pdf> (Accessed on May 2017).

³⁹ Susan Grueneberg, *Entering the US Franchise Market: A Summary of Legal Considerations*, 11 (3) INTERNATIONAL JOURNAL OF FRANCHISING LAW 12-15 (2013).

⁴⁰ Douglas, *supra* note 38. See also 15 USC §§1221–1225.

⁴¹ *Id.* see also 15 USC §§2801–2806.

⁴² *Id.* see also (15 USC §45(b)).

⁴³ *Id.* see also (15 U.S.C. §53).

⁴⁴ *Id.* see also 15 USC §45(m) (1)(B).

violation of the rules. The federal franchise rule does not provide private remedies for violation of the FTC rule. It is only the FTC who can bring action for the violation of the rule.

Further, “non-US franchisors or international franchisor that want to enter in to US market must investigate and comply with anti-terrorism and other similar laws especially if they form a US entity to conduct business in the United States”.⁴⁵

Regarding the regulation of franchise business at states level, the states provide more protection to the franchisee than the federal rule. At the states level, franchise issue is regulated by different agencies. Most states regulate franchise business by the federal franchise rule. However, dozens of states have franchise disclosure requirements. Most of the states use franchise disclosure format guidelines. This guideline is the amended version of Uniform Franchise Offering Circular which was formerly adopted by the North American Securities Administrators Association.⁴⁶ This guideline is acceptable in all states that have registration requirements. The guidelines include detailed information that the franchisor should disclose for the prospective franchisee before conclusion of franchise contracts. The registration requirement issues are provided in various state laws even if it is not provided under the FTC rule.

The other key point is the remedies for violation of the disclosure requirements, the registration requirements and the relationship issues under states franchise regulations. State franchise laws often provide franchisees the civil remedies when the franchisors violate the franchise regulation in relation to disclosure laws, relationship laws and the registration laws. It provides two major remedies for the franchisees rescission and damages.⁴⁷ In many states, principal officers and directors for violating franchisors may be severally and jointly liable. States laws often provide criminal penalties for willful violation of franchise laws up to \$100,000 and one-year imprisonment.⁴⁸ Further, under states laws franchisees are allowed to bring class action if they have common question of law and common question of facts.⁴⁹ In short, compared to the FTC rule, the states’ franchise regulations have provided better protection for the franchisees.

B. Poland

Poland has no specific laws dealing with business franchises.⁵⁰ Hence, parties conclude franchise contract based on the principle of freedom of contract. The only limitation to freedom of contract of the parties is the parties cannot make agreement contrary to law, morality and the principle of good faith. The franchise system is developed by court judgments in Poland.⁵¹ The

⁴⁵ Susan, *supra* note 39, at 46.

⁴⁶ UNIDROIT, UNIDROIT Franchising Guide available at; <http://www.unidroit.org/english/guides/2007franchising/franchising2007-guide-2nd-e.pdf> (accessed on October 2016).

⁴⁷ Douglas, *supra* note 38.

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ Krzysztof Kazmierczyk & FilipKijowski, Enforcement of contracts in Poland, in STEFAN MESSMANN & TIBOR TAJTI (EDS), THE CASE LAW OF CENTRAL AND EASTERN EUROPE – ENFORCEMENT OF CONTRACTS (European University Press, Bochum, 2009), at 654-659.

⁵¹ *Id.*

Polish Court of Appeal in Katowice on 4 March 1998, 1Aca 636/98 take the asymmetric and an innominate nature of contract between the franchisor and the franchisee into account and finally concluded that the franchise contract has to be treated differently from the other ordinary contracts.⁵²

In the case of Family Frost – Polska Sp. Z o. O as franchisor and two businessmen as franchisees entered in to agreement on 24 June 1993.⁵³ In this agreement, they agreed for distribution of ice cream by using mobile sales points. However, the franchise business became unprofitable for the businessmen. Due to this, the franchisor terminated the contract and required payment of the balance. The franchisee brought suit against the franchisor requiring the court to declare the franchise contract was void for several reasons. First, they argued that the obligations under the contract were impossible to perform for several reasons of economic nature. Secondly, they claimed the contract violated the nature of legal relationship since it allocated the risks and responsibility only to one party. They raised the high degree of subordination of the franchisees and severe limitation of their freedom to make business decisions. Thirdly, they argued that the contract was null and void because it violated good morals. The franchisees argued for return of the initial license fees arguing that it was contrary to good morals; there was no equivalency of performance to be rendered by each party.

The franchisor on his part claimed the payment of the unpaid balance of PLN 497,242.52. In response to the franchisees argument, he argued that the contract concluded between them was franchise contract and in such type of contract subordination is natural. He further argued that the economic effects of an undertaking cannot be associated with good morals and as a result it cannot be a defense. The appellate court ordered the franchisor to return the initial license fee. The court recognized the subordination, the obligation of franchisor and the nature of the franchise business in its reasoning.

As mentioned above, Poland had no specific laws regulating franchising. Hence, franchisors are not required to make disclosure, to register with government offices and also not subject to any laws dealing with the relations between the franchisor and the franchisee. Franchise contract is totally left for the contractual freedom of the parties. That means franchise contract is innominate contract which needs no government intervention. However, the general principles of contract law in the civil code, principles of good faith on pre-contractual negotiations, formations, terminations, and cancellations of contracts and Poland competition law of 2003 indirectly regulates franchise business.⁵⁴ This shows that even if the Polish laws require no pre-contractual disclosure requirements, it requires pre-contractual good faith negotiations.

⁵² *Id.*

⁵³ *Id.* See also MAGDALENA KARPIŃSKA, COMMENTARY ON POLISH FRANCHISE LAW. Dentons Rondo ONZ 100-124 Warsaw, Poland, at 5.

⁵⁴ *Id.*, at 6.

C. South Africa

In South Africa, business franchise is the rapidly growing form of doing business. South Africa is becoming a major franchising country⁵⁵ in that franchise contributes to about 12% of the country's gross domestic product (GDP).⁵⁶ To regulate the growing economic influence of franchising, the South African government has enacted the Consumer Protection Act on 24 April 2009.

The South African Consumer Protection Act has taken in to account the country's history of apartheid system that leads in to unfair distribution of resources and unequal educational opportunities between the white and the black.⁵⁷ The act is aimed at protecting the consumers. The act considered franchisees as consumers when the franchise agreement is offered. Being considered as consumers, franchisees are given a bundle of rights designed to promote social and economic welfare of the consumers.⁵⁸ Accordingly, franchise agreement has to be made in writing especially in plain language that can be easily understood by average literate populations.⁵⁹

The other key feature of franchise business in South Africa is the compulsory cooling off period provided for the franchisee.⁶⁰ Under the South African Consumer Protection Act, the franchisee has the right to cancel franchise agreement within 10 days after franchise agreement was signed without paying damage or any penalty. The franchisee is only expected to notify the franchisor in writing. The franchisors have no chance of claiming the losses they incurred due to cancellation of the franchise agreement.⁶¹ This aspect of the law is criticized as the future threat to sustainability of the business.

The other feature of South Africans consumer act is its prohibition of the use of physical force against consumer, the prohibition of coercion, pressure, duress, and undue influence.⁶² this regard, if physical force is used against the franchisee, the agreement will be *void ab initio*. These rules are applicable especially during marketing, negotiation, execution and enforcement of the franchise agreements. Some commentators say this rule is the extension of the principles of good faith that requires the parties to act in good faith.

D. Model Laws

The International Institute for Unification of Private Law (UNIDROIT) has developed two model laws on the regulation of franchise business with a view to bring harmonization and unification of private laws. These laws are the Guide to International Master Franchising

⁵⁵ Robert W. Emerson, *Franchisees as Consumers: The South African Example*, 37 FORDHAM INTERNATIONAL LAW JOURNAL 456 (2015).

⁵⁶ *Id.* See also Kendal H. Tyre, Courtney L. Lindsay II, and Jessica Gallinaro (2013) *Africa Alert: Recent Development in Cross Boarder Legal Issues*, A Publication of Nexon Peabody LLP.

⁵⁷ *Id.*, at 1.

⁵⁸ *Id.*

⁵⁹ Robert, *supra* note 55, at 463.

⁶⁰ *Id.*, at 466.

⁶¹ *Id.*, at 467.

⁶² *Id.*, at 464.

Arrangement which was passed in 1998 and later revised in 2007, and the Model Franchising Disclosure Law which was enacted in 2002. Besides, it has also prepared the explanatory note which explains the details of the Model law and how it should be interpreted.⁶³

The model franchise disclosure law deals with the franchisors duty to disclose detailed information before the conclusion of franchise agreement and payment of the fees.⁶⁴ This model law is not prepared for adoption by the states. It is rather made as a model from which states can take notice or experience, as the law that the state legislators can consult or refer to when they want to enact their own national laws. The law is flexible in that it permits the states to make their own modification with their practical situations. The definition of franchising under this model law includes different types of franchising such as unit franchising, master franchising and area development franchising.⁶⁵ The model franchising is applicable for both national and international franchising.⁶⁶ However, the model disclosure law does not regulate the relation between franchisor and franchisee. But, it has provided some issues such as the conditions for the renewal, terminations, and limitation to the territory in franchise.⁶⁷ The model law intends to bring development of franchise business by taking in to account its advantage to the economic development. It requires the franchisor to provide necessary information for the franchisee in the offer to form franchise agreement. Under the model law, in principle, the disclosure document is not required to follow a certain format. However, the disclosure document has to be in writing even though there are certain exceptions. Regarding the receipt of disclosure document, it has to be acknowledged by the franchisee. Further, the model law has provided that the waiver by the franchisee of rights given under the law is void.⁶⁸

The other key issue provided in the model law is that in master franchise agreement, the master franchisor has the duty to disclose material information for the sub franchisee.⁶⁹ Further, master franchisor has duty to inform sub franchisee the destiny of master franchisor in case of termination of master franchisor.⁷⁰ Moreover, it provided remedies for the violation of disclosure requirement by the franchisor: the franchisee can terminate the agreement and ask for payment of damage from the franchisor.⁷¹

VII. CONCLUSIONS

Franchise business is a rapidly expanding form of doing business in international trade. Nowadays, it is one means of reducing poverty, creating job opportunities and bringing economic development. However, it can only smoothly function if there are effective

⁶³ UNIDOIT Guide to Master Franchising, Model Franchise Disclosure Law and Explanatory Report, Available at <http://www.unidroit.org/english/modellaws/2002franchise/2002modellaw-e.pdf>. (Accessed on October 2016).

⁶⁴ UNIDROIT Model Franchise Disclosure Law, Art 6(1-3).

⁶⁵ *Id.*, Art 2.

⁶⁶ *Id.*, at 13 (the explanatory report part).

⁶⁷ *Id.*, Art 6(2).

⁶⁸ *Id.*, Art 10.

⁶⁹ *Id.*, Art 6(3) & at 40 (the explanatory report part).

⁷⁰ *Id.*

⁷¹ *Id.*, Art 8 & at 40-42 (the explanatory report part).

government regulatory laws which regulate the abusive and opportunistic behavior of the franchisor.

In this regard, governments follow three different approaches in regulating franchise business. The first approach to regulation of franchise business is having pure franchise specific laws. Countries that have pure franchise laws regulate the business franchise in coordinated way. In these countries there are organs which specifically regulate the franchise business in addition to effective franchise law. The laws in these countries regulate the disclosure requirements, the relationship issue and the registration requirements. This is the most effective and developed approach to regulating business franchise since it regulates the overall process of the franchise business. The second approach is by having different laws such as competition laws, consumer's laws, intellectual property law, investment laws and commercial laws. Countries that follow this approach also have the organs that regulate franchise business in the form of consumer protection authority, Fair Trade Commission, and the like. The third approach is through the courts interpretation of the general principles of contract law, the commercial laws and the like, especially good faith principles. In this approach there are no franchise specific laws, nor are there organs or authorities that regulate business franchise.

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