



International Distribution Institute

Franchisor's liability and commercial risks



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Goal

- ❖ This panel will analyse franchisor's liability vis-a-vis its franchisees and their customers due to behavior of system suppliers.
- ❖ *e.g.* can a franchisor be held vicariously liable for the actions of a supplier or a supplier's employees? Is there franchisor's liability for incorrect labeling, marketing and advertising by its suppliers? What happens if the supplier goes bankrupted?

Overview of our presentation

- **Introduction**

- i. Franchisors and their suppliers are independent and responsible for their own actions
- ii. Cases where the franchisor may be liable (or not)
 - A. Special liability regime for defective products (composition, packaging, labelling)
 - B. Defects in listed products and the franchisor's role (cause: the listing)
 - C.
 1. Excessive control of the franchisee by the franchisor: coverage of liabilities
 2. Excessive control of the franchisee by the franchisor: reclassification as a contract of employment
 - D. Commercial advantages received by the franchisor on behalf of franchisees must be returned to them
 - E. Liability of the franchisor based on brutal/sudden termination of established commercial relationships (delisting of suppliers)

- **Austrian approach**

- **A Swedish example**

- **Discussion with the audience**



Introduction

i. Franchisors and their suppliers are independent and responsible for their own actions

- Franchisor and franchisee / Franchisor and suppliers are independent companies
- The supplier – who charges excessive prices for the franchisor's brand, which the franchisee is obliged to buy – subjects the franchisee to a **significant imbalance**

Amiens Court of Appeal, January 10th, 2019, nbr. 17/01699



Introduction

ii. Cases where the franchisor may be liable (or not)

A. Special liability regime for defective products (composition, packaging, labelling)

- The **franchisor** may be held **liable** in the event of a breach by the supplier, when the franchisor is **qualified as a producer** (the product bore the franchisor's trademark): joint liability of the franchisor, the intra-Community importer, the manufacturer who packed the can and the supplier of the empty can and the cap.

[Toulouse Court of Appeal, May 25th, 2021, nbr. 19/01901](#)

B. Defects in listed products and the franchisor's role (somewhat different from the case referred to in A: the event giving rise to the franchisor's liability is the listing)

- The franchisor **cannot be held contractually liable for the actions of a third party**, including when that third party is a supplier exclusively referenced by the franchisor, whose choice is imposed by the franchisor.
- The Paris Court of Appeal clearly states that, as part of its assistance obligation, **it is not the franchisor's responsibility to ensure that the suppliers - it has listed on an exclusive basis - properly perform the contracts they have signed with the franchisees** in its network, and that it cannot be held liable for their failure to do so.

[Paris Court of Appeal, February 11th, 2015, nbr. 12/20128](#)

C1. Excessive control of the franchisee by the franchisor: **coverage of liabilities**

- The franchisee must comply with the know-how and the conditions governing the use of the distinctive signs set out in the franchise agreement.
- The franchisor can legitimately control the franchisee's compliance with these obligations.
- But there's a line between close collaboration and too much control
- By **interfering too much** in the franchisee's business, in the event of insolvency proceedings, the franchisor incurs liability in an action to cover the franchisee's liabilities.
 - ⇒ Franchisor considered as "de facto director" (e.g. commercial policy, accounting, bank signatures).

[Court of cassation, Commercial Chamber, November 9th, 1993, Juris-Data nbr. 91-18.351](#)

C2. Excessive control of the franchisee by the franchisor: **reclassification as an employment contract**

- Too much control on the part of the franchisor is likely to result in the reclassification of the franchise contract.
- Case law is consistent: possible **reclassification of a franchise contract as an employment contract** if the facts reveal subordination between the franchisee and the franchisor.
- Requests to reclassify a franchise contract as an employment contract are most often rejected.

[Court of cassation, Social Chamber, March 22nd, 2007, Juris-Data nbr. 2007-038157](#)

[Limoges Court of Appeal, February 3rd, 2020, nbr. 18/01198](#)

- The difficulty lies in defining the boundary between simple economic dependence, which is inherent in any distribution network, and a contractual relationship that reveals a genuine legal relationship of subordination, a key criterion of an employment contract, *i.e.* the **actual conditions under which the workers' activities are carried out**.

[Dijon Court of Appeal, April 23rd, 2009, nbr. 2009-376577](#)

[Douai Court of Appeal, November 23rd, 2006, nbr. 2006-325137](#)

D. Commercial advantages received by the franchisor on behalf of franchisees must be returned to them

- The franchisor may be required to repay its franchisees the sums it has received from suppliers, where the franchisor is qualified as the franchisee's agent for listing these suppliers and negotiating their terms of sale.
- If the franchisor acts as an **agent** (central referencing body), it must return to the franchisees any **rebates received** from suppliers.

Paris Court of Appeal, December 4th, 2013, nbr. 11/21615

E. Liability of the franchisor based on brutal/sudden termination of established commercial relationships in the case of delisting of suppliers

- Can a franchisor be held liable if its franchisees give notice of the termination of a contract with a supplier?
- A franchisor may be held liable for the termination of an established commercial relationship with a supplier if the companies in the network do not have **autonomy of decision** as to the choice of their suppliers and, where applicable, as to the continuation of their relationship with them.

Court of cassation, Commercial Chamber, June 22nd, 2022, nbr. 21-14.230

- Liability of a parent company, also a franchisor, after finding that it was the **sole decision-maker** for its wholly-owned subsidiaries and that it alone had taken the decision to terminate the relationship, which meant that the subsidiaries and franchisees had **no real autonomy** in the decision to enter into the commercial relationship and subsequently in the decision to terminate it.

Court of cassation, Commercial Chamber, July 5th, 2016, nbr. 14-27.030

Austrian approach

- **tying supply/purchase agreements**
 - such contractual clauses are permissible (also from an Austrian perspective)

(LG Düsseldorf, 21.11.2013 – 14 c O 129/12 U with reference to BHG, 11.11.2008 – KVR 17/08 ‘*Praktiker-case*’, LG Kiel, 18.01.2013 – 14 O 63/11.Kart; OLG Schleswig, 26.09.2013 – 16 U (Kart) 50/13, ‘*Subway-case*’; *Liebscher/Flohr/Petsche/Metzlaff*, Handbuch der EU-Gruppenfreistellungsverordnungen³, Rn. 319, with reference to OLG Düsseldorf, 11.04.2007 - U (Kart) 13/06, *Body-Shop case*’ and EuGH, Urt. v. 28.1.1986, Rs. EUGH C16184 C-161/84 - Pronuptia , NJW 1986, page 1415)

- supply/purchase obligation are justified for reasons of **quality** assurance and to ensure that the **brand** is recognised and thus serves to ensure the **functionality of the franchise system**
- are not contra bonos mores

Austrian approach

- **Franchisor's liability for his vicarious agent ('Erfüllungsgehilfe') ?**
 - anyone who is obliged to provide a service / works to another person is liable for the fault of their legal representative and the persons they engage for fulfilment as for their own (§1313a ABGB).
 - Liability is assessed according to whether the vicarious agent was involved in the Franchisor's pursuit of interests and thus in the Franchisor's sphere of risk.
 - liability under §1313a ABGB presupposes the **obligation of the Franchisor to perform**. Furthermore, the Franchisor causes the vicarious agent to act in the context of the fulfilment of his contractual obligations.

Austrian approach

- **the independent contractor as a vicarious agent ('Erfüllungsgehilfe')?**
 - The decisive factor is **which specific performance obligations or duties** of protection and care the **Franchisor has assumed towards its Franchisee**. In principle, independent companies can also be "vicarious agents" to this extent. The Franchisor's authority to issue instructions is irrelevant, as is the principal's expertise.
 - As a rule, **liability for the breach of performance obligations of the Franchisor** arising from the contract is therefore to be affirmed, **even if the Franchisor uses an independent third party** to fulfil its obligations (Supreme Court 29 August 2013, 8 Ob 106/12i)
 - **case:** tying supply/purchase agreement without any performance obligations for Franchisor – default of supply/performance by third party (no vicarious agent)
 - Franchisor's liability for fault in selecting (culpa in eligendo)?

A Swedish example

PANAXIA-case

- Cash transport company Panaxia
- Franchisor authorised to contract with suppliers on behalf of franchisees
- Franchisor contracted cash deposit services with Panaxia *on behalf of* franchisees

A Swedish example

PANAXIA-case

- Panaxis used franchisees' deposits to finance its business (criminal)
- Panaxia bankruptcy
- Most deposits lost
- One franchisee requested arbitration against franchisor damages