

Wright, Johnston & Mackenzie LLP



Franchise Disputes



Wright, Johnston & Mackenzie LLP

302 St Vincent Street, Glasgow, G2 5RZ. Tel 0141 248 3434 Fax 0141 221 1226
40 Torphichen Street, Edinburgh, EH3 8JB Tel 0131 221 5560 Fax 0131 221 5570

Web Site: www.wjm.co.uk

Email to sd@wjm.co.uk

Franchise Disputes

When negotiations are taking place in relation to entering into a Franchise Agreement, both the Franchisor's and the Franchisee's focus is often solely on getting the Franchise up and running. It can be only at a later date when, regrettably, relationships may have broken down that parties will look in detail at the terms of the Franchise Agreement.

Resolving disputes via the Courts can be both time consuming and expensive and there are certain issues to be considered for both Franchisors and Franchisees in order to try and avoid disputes arising. Set out below, are some of the most common issues that arise for both Franchisors and Franchisees.

Franchisors

Intellectual Property and Domain Names

When a Franchise comes to an end, whether on the expiry of a fixed term or due to a dispute, there are often arguments regarding what should happen with the Franchisee's website. It is common for a Franchisee to be permitted to register a domain name to allow them to set up a website for the purposes of the new franchised business. This will often be a variation on the name of the Franchise.

It would be normal for the Franchisor to retain intellectual property rights under the Franchise Agreement including rights in the name of the Franchise. There can be substantial goodwill in the name of a Franchise as the goodwill associated with that name may often be one of the main selling points.

Accordingly, in order to avoid any difficulties in relation to the website, Franchisors should ensure that they retain control of the process of registering the domain name.

They need to:

- Draft the Franchise Agreement so as to make it clear that the Franchisee is not permitted to register any domain name containing the trademarked or copyrighted name.
- Dictate to the Franchisee in the Franchise Agreement what domain name he or she should use, which should already have been registered by the Franchisor.
- Make it clear to the Franchisee, before taking their Franchise fee, that they (the Franchisor) will register the domain name and will be simply granting him or her permission in the Franchise Agreement to use it for as long as the Franchise lasts.
- Make it clear in the Franchise Agreement that on expiry or termination of the agreement, the name reverts back to the Franchisor's control.

Representations prior to entering into Franchise Agreement

The Franchisor should always be wary of making definite claims to a Franchisee as to the level of sales, turnover or profits that a Franchisee could expect to generate under a Franchise Agreement. Franchisors should be aware that there are a wide range of circumstances which could dictate the success or otherwise of a Franchise and should

not, even in the hope of getting a Franchise Agreement entered into, make unrealistic claims.

The reason for this is that if a Franchisee enters into a Franchise Agreement on the basis of these representations and they prove to be false, then it would open to the Franchisee to bring a claim for fraudulent or negligent misrepresentation. This would be on the basis that they simply would never have entered into the agreement had it not been for the fact that they had been made these promises. While this is not an easy claim for a Franchisee to make, if it was successful then it could result in a large claim for damages.

In order to protect a Franchisor, the Franchisee Agreement should make quite clear that there were no prior representations which induced the Franchisee to enter into the Franchise Agreement. The Franchise Agreement should also include an “Entire Agreement” Clause. This makes clear that any other documents that were issued previously were indicative only and were of no relevance in resolving any disputes that may have arisen. If the Franchisor is based in Scotland, it is also sensible to ensure that it is made clear that the Agreement is governed by Scots Law and that the Scottish Courts will deal with any dispute that arises.

Notice Provisions

It is common to have specific provisions in a Franchise Agreement setting out how information should be provided, in particular, with reference to termination of the Agreement. Franchisors should be aware that any such requirements, such as the requirement to issue notices within a certain time period or in a certain way such as by recorded delivery, must be strictly complied with if there is a specific mechanism outlined. If it is not complied with then it could be held that the notice was ineffective. For this reason, professional advice should be taken in drafting any such clauses and in issuing any notices.

Franchisee

Misrepresentation

When you are considering entering into a Franchise Agreement it is vital that you carry out your own research into the strengths of the Franchise that you are going to be operating. You require to carry out as much research as possible into the Franchise before entering into the Agreement. This will give you the best possible opportunity of running a successful Franchise. It is important that you do not simply rely on the statements of the Franchisor. It will clearly be in their interests to paint the rosiest possible picture.

While it is always open to someone to claim that they were induced to enter into a Contract by fraudulent or negative misrepresentation, this is not an easy claim to make. This is particularly so in relation to Franchise Agreements, which will usually have a Clause making clear that any information that was provided prior to the Franchise Agreement being entered into was for information only and was not to be relied upon.

For similar reasons in the event that you want anything to form part of the Franchise Agreement or you have any information that you wish to convey to the Franchisor, you should ensure that all information is put in writing. Even leaving aside the fact that this may be a requirement of the Franchise Agreement, in the event there was a dispute, then for evidential reasons you should ensure that you have documentary evidence to support your position.

Property

For a Franchisee the choice of premises from which they trade is potentially the most important decision they will require to take. It is always sensible to take professional advice to ensure that the premises meet the needs of your business and that you can afford the premises. You should also ensure that the terms under which you either buy or lease the premises are clear and meet your needs. You should try and ensure that you maintain a level of control and that the Landlord (who may also be your Franchisor) is not in a position to increase the rent excessively unduly or take steps to remove you from the premises without giving you adequate notice.

Given the importance of having the correct premises you should also make sure that any payments due in respect of rent or other service charges are always paid on time. In the event that they are not, then it is likely that your Landlord (who may also be the Franchisor) would be able to take steps to terminate the lease which would mean that you would have to remove yourself from the premises. This could have potentially catastrophic effects on the ability of the Franchise to continue. It is also likely that if you faced an action of termination, you would have to pay not only any rent that was outstanding but also the legal costs of the other side in the dispute. As in all such situations legal costs can be significant.

Whether you are a Franchisor or Franchisee, the Franchise Group at Wright, Johnston & Mackenzie LLP can give you detailed advice on resolving any disputes which may arise.

For further information please contact

Steven Docherty: sd@wjm.co.uk or

John Grant: jzg@wjm.co.uk

0141 248 3434

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