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U N I D R O I T

INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW  
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COMMITTEE OF GOVERNMENTAL EXPERTS FOR THE PREPARATION OF A  
MODEL FRANCHISE DISCLOSURE LAW

Second session  
(Rome, 8 - 12 April 2002)

Comments submitted by the World Franchise Council

Rome, March 2002

## INTRODUCTION

1. The World Franchise Council (WFC) was established by the Major Franchise Associations in Europe, North America and the Pacific Rim in 1994 so as to define, represent and promote the standards of good franchising being established around the world.
2. The WFC is particularly aware of, and involved in, the wide variety of developmental stages reached in franchising in different countries and the different kinds of business methods that are regarded as falling within the scope of franchising in different countries.
3. The WFC supports the need to ensure that the legislative environment around the world is conducive to good franchising in all its various forms. The WFC is equally concerned to ensure that the legislative environment in any one country does not stifle legitimate "franchising" activity in that country for the sake of a world wide uniformity that is not a characteristic of the franchising sector.

## WFC'S RESPONSE TO THE NEW PROPOSAL FOR A MODEL LAW

### PREAMBLE AND PREFACE:

UNIDROIT proposes two choices in the order of presentation of the provisions of the draft Model law and its detailed explanatory report:

- 1) Preamble, Provisions of the Model Law, detailed Explanatory Report on the background of the ML and on each of the provisions, OR
- 2) Preamble, Introductory part of the Explanatory Report, Provisions of the Model Law, 2nd part of the Explanatory Report detailing each of the provisions of the Model Law.

**The WFC marks its preference for the 2nd option.**

### ARTICLE 5: CATEGORIES OF EXEMPTIONS FROM THE OBLIGATION TO DISCLOSE

**5 - B:** The WFC suggests adding a provision to this category of exemption: this category is acceptable on condition that the assignee or transferee be clearly given the chance to receive all the relevant information (including financial) from the assignor or transferor of the franchise contract in order to protect the assignee or transferee from the undisclosed information of an assignor or transferor who wishes to escape from a contract, and who in order to do so would deliberately not disclose information which could later prove problematic for the future franchisee.

**5 - G:** The WFC is of the view that small annual contractual payments by the franchisee does not constitute as such a guarantee against dishonesty or fraud, and **should therefore not constitute a reason for exemption** of disclosure on the part of the franchisor. The purpose of Disclosure is to protect the smaller investor, in this case the franchisee, and fraud can be all the easier when contrived around small amounts of dues.

**the WFC supports the Chinese view that 5-G should be deleted as a category of exemption**

## **ARTICLE 6**

**Article 6 - 1 - G** : the WFC is of the view that disclosure should carry on the relevant details relating to any criminal convictions or any finding of liability in a civil action [or arbitration] involving franchises, or other businesses, relating to fraud, misrepresentation, or similar acts or practices of [delete (ii) and (iii) and keep only] **the franchisor** [or predecessor of the franchisor], in other words the moral entity and/or the (physical) person of the franchisor. As the franchisor is morally responsible for his senior managers and affiliates, information on these persons is not necessary, because covered by the franchisor's responsibility.

**the WFC recommends deleting paragraph (ii) and (iii) of this provision**

**Paragraph 6 – 1 – (M)(iii) and (iv) : Information on pricing arrangements between franchisor and up stream suppliers, and treatment of revenue/benefits (direct or indirect) between franchisor and up stream suppliers:**

The draft “Model Law” requires the disclosure of information concerning the relationship between a franchisor and its suppliers. In a number of industry sectors a franchisor's relationships with its suppliers (and in particular its financial relationships) are a material part of the “know how” which supports that franchisor's competitive position.

The difference must be stressed here between the information that is made available to contracted franchisees of the franchisor, and the information that is to be made available to prospective franchisees.

In the absence of a confidentiality agreement, disclosure to prospective franchisees is, in effect, to put the information into the public domain.

In practice, a confidentiality agreement will offer no real protection to a franchisor whose competitors choose to act as “prospective franchisees” for the purpose of securing commercially confidential information on supply arrangements with no intention of signing a franchise agreement.

Thus, these provisions of the “Model Law” are inappropriate. Neither will the more widespread (and expensive) adoption of pre-contractual confidentiality agreements make them practical.

**the WFC is of the opinion that more thought be given to this issue, and that any mechanism of supply between the franchisor and its suppliers be considered as significant know how of the franchise business, and thus not be revealed at the pre-contractual disclosure stage.**

### **Paragraph 6 – 1 - (N) –( i)-(c): Financial matters**

Regarding the financial statements that have to be produced by the franchisor, the WFC's choice is Option 3: the financial statements of the franchisor, and when available audited or otherwise independently verified financial statements, including balance sheets and statements of profit and loss, for the previous three years;

**However, the WFC wishes to add a provision to this obligation as regards franchise companies that are less than three years old. In most cases, such companies cannot produce three consecutive audited balance sheets. This situation needs to be recognized, along with the possibility that the young franchisor clearly state this objective impossibility to any prospective franchisee, and not be penalized for it.**

**In fact, the WFC would like to see included in the Model Law a general provision governing Article 6, which recognized the idea that in certain circumstances, a franchisor may not/cannot disclose a certain provisioned information. In such a case, the franchisor must be able to provide the other party with a reasonable and adequate justification for not disclosing this information.**

### **ARTICLE 9: REMEDIES**

In the wording of this article, it is stated several times that "the franchisee is entitled to terminate the franchise agreement unless...".

**The WFC is of the view, and contrary to paragraph 130 of the Explanatory Report, that a franchisee cannot unilaterally, without any other form of procedure, terminate a franchise contract.**

**This must always be done according to the procedures of either mediation, arbitration or a judicial procedure.**

**If termination is the result, it must be termination under the terms of the agreement, and not automatic annulment. This is important for clauses like the non-compete clauses to be able to produce their full effects.**

**Furthermore, the WFC believes that the Model law should say that if an undisclosed provisioned information was not disclosed, but that this fact was not essential to the franchisee's decision of contracting, this non-disclosure does not annul the agreement. A situation of this kind must come under the appreciation of an arbitration committee or a court.**

**If the provisions above are taken into account in the Model Law, then the WFC's choice is Option 3.**

**WFC Members favorable to this position:**

**Argentina, Australia, Belgium, Brazil, Britain, Canada, China, Colombia, Denmark, Europe, Finland, France, Germany, Greece, Hong Kong, Hungary, India, USA, Italy, Japan, Latvijas, Malaysia, Netherland, New Zealand, Philippines, Portugal, Singapore, South Africa, Spain, Sweden, Switzerland, Slovenia, Taiwan.**

**WFC member against this position and against any legislation: Austria.**