

PRACTICE GUIDES

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# Franchise

Editor  
Philip F Zeidman



# Franchise

## Practice Guide

Editor

Philip F Zeidman

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For further information please contact [editorial@gettingthedealthrough.com](mailto:editorial@gettingthedealthrough.com)



**Publisher**

Tom Barnes  
tom.barnes@lbresearch.com

**Subscriptions**

Claire Bagnall  
claire.bagnall@lbresearch.com

**Senior business development managers**

Adam Sargent  
adam.sargent@gettingthedealthrough.com

Dan White  
dan.white@gettingthedealthrough.com

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87 Lancaster Road  
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# Preface

## Philip F Zeidman<sup>1</sup>

In my introduction to *Lexology Getting The Deal Through – Franchise*, I described an experience many of us have had. I recounted a general counsel's arrival at the office to find a message from his boss, posing a series of questions about franchising in a number of countries around the world – questions to which the general counsel, understandably, has no ready answers. The same experience, of course, is familiar to outside counsel encountering a client's expectations.

A survey of the available sources of information comes up empty. None is sufficiently comprehensive yet digestible. *Lexology Getting The Deal Through – Franchise* seeks to meet that need by posing and answering the key questions one must address about franchising in a country. Now in its 13th edition, it covers 26 countries, and has proven its value many times over. It is a classic 'desk book' that belongs next to your telephone (if you still have one) or your computer.

But what then? After your rapid and impressive response, what happens when you need to delve more deeply into the issues raised by your company's or client's plan to expand by franchising? For that purpose, a book that provides succinct answers to threshold questions, however authoritative, is, as social scientists say, 'indispensable but insufficient'.

By now you know that franchising touches, glancingly or with full force, on almost every legal discipline. And you also know that none of those disciplines addresses franchising as squarely as you would like; that there are shockingly few law schools that include franchising in their curriculum; and that there are no course books that adequately cover the territory you will need to traverse.

Enter *Lexology Getting The Deal Through's Practice Guide – Franchise*.

If *Lexology Getting The Deal Through – Franchise* was designed to be left on your desk, *Practice Guide – Franchise* can perhaps best be thought of as the book you will take on your next flight.

So settle in.

*Adjust your seat, your footrest and your reading light.*

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<sup>1</sup> Philip F Zeidman is a partner at DLA Piper LLP (US).

You will almost certainly want to begin by examining the fundamental legal doctrines, statutes and regulations that govern how franchising is treated in law. That obviously requires an understanding of how different countries have chosen to regulate franchising explicitly (or declined to do so). So you begin with Global Overview of Specific Franchise Statutes and Regulations, which includes a handy chart at the end, keyed to the various approaches. But you will also want to step back and examine two broader and older legal constructs that are essential. One of those inquiries will be to learn how franchising is treated in the foundational legal structures of different countries, in Common Law and Civil Law on Franchising Issues. Under what circumstances will the analyses under those two systems lead to different results? And, you will need to have a grasp of another overarching theme, depending on how a country has chosen to apply it, or not, as the case may be (see Good Faith and International Franchising).

Now that you have an overview of the legal structures you will need to understand, it's time to get a sense of how franchisors go about selecting the form of expansion that best suits the company's business model, culture and management practices (Selecting the Appropriate Vehicle for International Expansion). One of those techniques – sub-franchising – is given special attention, not necessarily because it is the 'right' choice, but rather because it is the most complex of the hierarchy of approaches to expansion, and because it is much more commonly utilised in cross-border than in domestic franchising (Sub-franchising, Master Franchising and Development Agents).

It is also important to keep in mind that franchising is constantly evolving to take advantage of new techniques and approaches. Prominent among the new techniques are e-commerce and social media (see Electronic Commerce, Social Media and Franchising). There, as you will see, problems that arise are frequently owing to e-commerce not having been addressed adequately in the original franchise agreement and relationship.

The decision of how best to go about the business of expansion is, along with selecting the countries you wish to target, certainly at the threshold of your business and legal initiative. And understanding these critical 'first issues' will surely consume a sizable share of the time on your flight.

Now it's time to turn to the heart of the franchise relationship, and examine how the franchisor and the franchisee choose to express the bargain they have reached. Much of this process is understanding how elements of that bargain can best be articulated to leave as little as possible to be the subject of differing interpretations. But the parties are not entirely free to do whatever they wish, nor is one party free to demand that its wishes be adopted in all respects, because franchise laws and other bodies of law impose limits and restrictions on the parties. Some of the key provisions of the Franchise Agreement are discussed. Confidential and Proprietary Information, and Trade Secrets points out the pivotal role this plays in the essential intellectual property associated with the franchise, and the challenge to protect it in each country where the franchisor anticipates selling franchises. Special attention is given to Approaches to Resolving Cross-Border Disputes between Franchisee and Franchisor, including a separate chapter on the Choice of Law and Choice of Dispute Resolution Mechanism in Cross-Border Franchise Agreements.

Other bodies of law, of course, impinge upon franchising, and an understanding of how they interface is important to a competent franchise lawyer (see M&A in International Franchising). Consumer Protection begins by addressing the concept of a consumer, which may differ by jurisdiction, and discusses the consequence of applying consumer protection laws to franchising.

## Preface

Data Protection and Privacy highlights the challenge presented to multinational franchisors in complying with the laws in this area adopted in nearly 120 countries, and suggests some approaches to meeting that challenge. Joint Employer and General Labour and Employment Issues examines the threat posed by this rapidly evolving field of law.

Among the subjects addressed by countries that have chosen to regulate franchising, the most common obligation is probably the duty to provide a prospective franchisee with information on the basis of which an informed investment decision can be made. The most robust embodiment of that obligation is the franchise disclosure document, discussed here in some detail in the chapter on Franchise Disclosure Documents.

*Ladies and gentlemen, we are beginning our descent.*

You have not, of course, been exposed to every nook and cranny of franchise law. That would require, at a minimum, several trips around the world.

But you can disembark now. You're off to a good start.

# Part 1

## Regulation of Franchising around the World

# 3

## Good Faith and International Franchising

**Bruno Floriani, Marissa Carnevale and Tanya Nakhoul<sup>1</sup>**

### Introduction

In recent years, the notion of good faith has been gaining traction in the context of both national and international franchising.<sup>2</sup> In both civil law and common law jurisdictions, courts have sometimes relied on the notion of good faith to compensate for the power imbalance that often exists in a franchise relationship. In most civil law jurisdictions, the duty to act in good faith in commercial dealings is a general and free-standing obligation that arises in addition to the contractual terms between parties. With regard specifically to franchise agreements, recent decisions have arguably extended the implied duty of good faith owed by a franchisor to a franchisee. For a franchisor to fulfil its obligations, courts have held that a franchisor is required to act in good faith throughout the franchise relationship, respond promptly to its franchisees' concerns regarding competitive threats, as well as generally take steps to protect its brand and franchise network.

Although a statutory duty of good faith applicable to all contracts has not been enacted in common law jurisdictions, many franchise-specific and business relationship statutes provide for a duty of good faith and fair dealing in these types of contracts. Common law courts are also increasingly inclined to recognise a duty of good faith in the performance of commercial contracts. For example, Canadian courts have applied the duty of good faith as a general organising principle of common law contracts, particularly in the context of commercial agreements such as franchise arrangements, involving vulnerable parties, .

The notion of good faith has been given various interpretations and has been applied on a case-by-case basis, especially in the context of franchise law. This chapter seeks to provide an overview of the manner in which the duty to act in good faith has been interpreted and applied by

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1 Bruno Floriani is a partner and Marissa Carnevale and Tanya Nakhoul are associates at Lapointe Rosenstein Marchand Melançon LLP. The authors would like to thank Maria Bechakjian for her contribution to this article.

2 Zoubair Mrabet, 'Les comportements opportunistes du franchiseur: étude du droit civil et du droit international uniforme' (2007) 41 R.J.T. 429 at 464.

courts, particularly in civil and common law jurisdictions. The various difficulties and challenges created by the current state of the law on good faith, particularly as it applies in the franchise context, will also be discussed. Finally, the authors will present practical tips for franchisors in order to comply with their duty to act in good faith. It is important to note that although this chapter draws on examples of Canadian case law, the issues addressed in this article commonly arise in cross-border franchising.

## Principles of good faith in the civil law tradition

### General overview

In many civil law jurisdictions, the duty to act in good faith in commercial dealings is a general and free-standing obligation codified by statute.<sup>3</sup> For example, a fulsome obligation applicable to all contracts exists in Canada's civil law province, Quebec, which imposes a legal requirement for all parties to conduct themselves in good faith during both contractual and pre-contractual dealings. The obligation to act in good faith applies to the execution of the agreement, the fulfilment of the parties' respective obligations, and the way in which the contract is terminated. Therefore, parties are required to act in good faith throughout the entirety of their contractual relationship, in addition to respecting the express terms of their contractual agreement. Moreover, while the notion of good faith is far-reaching and applicable to many situations in the civil law tradition, the principle is not typically viewed as yielding a particular result or outcome, but rather informs the manner in which parties to a contract must conduct themselves, and provides the basis for considering the reasonableness and sufficiency of their actions in a given set of circumstances.<sup>4</sup>

### Good faith in franchise agreements

Civil law courts have often characterised franchise agreements as contracts of adhesion given that they typically contain standardised clauses that are not freely negotiated between the parties.<sup>5</sup> Courts have justified reading an implied duty to act in good faith into franchise agreements and have imposed obligations on franchisors that go beyond the terms of the franchise agreement based on the existence of an inherent power imbalance between the franchisor and the franchisee.<sup>6</sup>

Furthermore, the relationship between a franchisor and a franchisee is often described as being of a long-term and relational nature.<sup>7</sup> Therefore, the judiciary is inclined to read in a more robust duty of good faith into franchise agreements considering that such agreements do not always spell out all of the terms between the parties in an explicit manner, as is often the case

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3 Articles 6, 7 CCQ; article 1134 C civ; Dr Mark Abell and Victoria Hobbs, 'The Duty of Good Faith in Franchise Agreements – A Comparative Study of the Civil and Common Law Approaches in the EU' (2014) 12:1 *Int'l J. Franchising L.* 25.

4 CCQ sections 1375, 1434; Craig Trachtenberg, Jean-Philippe Turgeon and Stéphane Destrempe, 'The Franchisor's Duty to Police the Franchise System', (2016) 36:1 *Franchise Law Journal* 87 at 97–103; Daniel F So, *Canadian Franchise Law: A Practical Guide*, 2nd ed (Toronto: LexisNexis, 2010) at 93–94.

5 Frederic P Gilbert, *Le Droit de la Franchise au Québec* (Montreal: Éditions Yvon Blais, 2014) at 43–44.

6 *ibid* at 161–163; Mrabet, *supra* note 2 at 464.

7 *Dunkin' Brands Canada Ltd v Bertico inc*, 2015 QCCA 624 at para 71 (*Dunkin*).

with long-term relationships.<sup>8</sup> However, courts have also held that there is no fiduciary duty that exists between a franchisor and a franchisee.<sup>9</sup>

In recent decisions, Canadian civil law courts in particular have broadly interpreted, and arguably significantly extended, the duty of good faith owed by a franchisor to a franchisee. Various examples of specific duties that flow from the duty to act in good faith in franchise agreements are discussed below.

### **Duty to disclose**

To act in good faith, franchisors have a pre-contractual duty to furnish accurate and up-to-date information to prospective franchisees regarding their business operations. This requirement is based on the general duty of good faith in contracts, and may in certain cases extend to the fulsome disclosure requirements set forth in specific franchise disclosure laws. In any event, this pre-contractual disclosure is typically required in order to allow franchisees to access information they need in order to make informed investment decisions.<sup>10</sup> The franchisor must therefore disclose all material information that is likely to influence the franchisee's decision in acquiring a franchise, as well as all information that the franchisee needs to operate the franchise.<sup>11</sup>

Given the general nature of the good faith obligation in civil law, there is no specific disclosure checklist that must be satisfied in each franchise context; however, a franchisor is required to exercise discretion and judgment in making its pre-contractual disclosures. As such, any facts or occurrences known to the franchisor that may impact a franchisee's decision to contract must be brought to light in a timely manner.

### **Duty to collaborate and provide technical and commercial support**

According to case law, franchisors are required to collaborate with their franchisees, meaning that franchisors must act in a reasonable manner and diligently towards their franchisees.<sup>12</sup> Similarly, franchisors are required to provide technical and commercial assistance to their franchisees throughout the course of their relationship.<sup>13</sup> The rationale is that the franchisor possesses a certain level of know-how and expertise required to thrive in its domain and must therefore support its franchisees to counterbalance the 'asymmetry of knowledge' that exists between the franchisor and the franchisee.<sup>14</sup> This entails that the franchisor must provide its franchisees with the tools that will enable them to (i) develop their business, (ii) prevent economic loss or at least minimise its impact and (iii) resist competition from other franchise networks.<sup>15</sup>

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8 *ibid* at paras 62-63.

9 *Provigo Distribution inc v Supermarché ARG inc*, 1997 CanLII 10209 (QC CA) at 25-26 (*Provigo*).

10 *So*, *supra* note 4 at 241-248.

11 *ibid*; Gilbert, *supra* note 5 at 163.

12 Gilbert, *supra* note 5 at 177.

13 *Provigo*, *supra* note 9 at 30-1.

14 *ibid*; James Judson, 'The Duty to Protect the Brand Against Competition: How Bertico Affects Franchisors in Ontario', (2018) 60 *CBLJ* 405 at 406-408.

15 *Provigo*, *supra* note 8 at 34.

### Duty to compete fairly with the franchisee

The duty to act in good faith would not preclude a franchisor from competing with its franchisees (assuming, of course, the absence of contractual obligations to this effect in favour of the franchisee). However, the franchisor owes an obligation of loyalty towards its franchisees in that, if a franchisor opts to compete with its franchisee, it must ensure that it continues to perform its legal obligations towards the latter and that it acts in such a way that the franchisee may continue to enjoy the benefits of its franchise.<sup>16</sup>

### Duty to protect the franchise brand

Civil law courts have also held that a franchisor has a duty to protect its brand and network that goes beyond the explicit terms of the franchise agreement. This is a duty that is owed not only to each individual franchisee, but also to the franchise network as a whole.<sup>17</sup> To fulfil this duty, a franchisor is required to (i) act in good faith throughout the franchise relationship, (ii) respond promptly to its franchisees' concerns regarding competitive threats and (iii) generally take steps to provide adequate brand management and protect its brand and franchise network.<sup>18</sup> What must be avoided by franchisors is a maintenance of the status quo or a 'business as usual' attitude in the face of significant changes in the market. If the franchisor demonstrates that it has made concrete efforts in protecting and enhancing its brand, and yet in spite of these efforts, competitors have encroached on the franchisee's business, the franchisee will likely have no basis for a complaint.<sup>19</sup>

In line with its duty to protect the franchise brand, the franchisor is also required to 'police' the franchise network, meaning that franchisors must actively monitor and endeavour to curtail relationships with delinquent or 'free-riding' franchisees in order to ensure the viability and profitability of the franchise network as a whole.<sup>20</sup>

## Principles of good faith in the common law tradition

### General overview

Unlike in the civil law tradition, a freestanding general duty of good faith in contracts does not specifically exist under common law.<sup>21</sup> Common law courts have traditionally described the concept of good faith as 'inherently repugnant to the adversarial position of the parties' and 'unworkable in practice'.<sup>22</sup> However, good faith and the role of implied contractual terms are gaining traction, particularly under Canadian common law. Canadian courts have recently held that contractual parties have a duty to act honestly in contractual performance, which is a manifestation of an 'organising principle of good faith performance in contracts'. Parties must

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16 *Provigo*, supra note 9 at 30–31; Trachtenberg, Turgeon and Destremes, supra note 4 at 98.

17 Gilbert, supra note 5 at 178–179.

18 *Dunkin*, supra note 7 at paras 77–88; Trachtenberg, Turgeon and Destremes, supra note 4 at 99–100.

19 *Dunkin*, supra note 7 at paras 93–105; *Provigo*, supra note 9 at 33.

20 *Dunkin*, supra note 7 at paras 83–85; Trachtenberg, Turgeon and Destremes, supra note 4 at 99–100; Gilbert, supra note 5 at 178–179.

21 *Bhasin v Hrynew*, [2014] 3 SCR 494, 2014 SCC 71 (*Bhasin*); Abell and Hobbs, supra note 3.

22 *Walford and Others v Miles and Another* [1992] 2 AC 128, [1992] 1 All ER 453, [1992] 2 WLR 174, 64 P & CR 166, [1992] 11 EG 115, [1992] 1 EGLR 207.



therefore refrain from lying or otherwise knowingly misleading each other about matters directly linked to the performance of the contract.<sup>23</sup> It has essentially been found that a basic level of honesty is required so as to guarantee the 'proper functioning of commerce'.<sup>24</sup>

Although courts have provided helpful tools to understand the current state of the good faith notion at common law, it remains unclear whether a good faith obligation is being imposed as a matter of law, as a matter of contractual terms implied by law or facts, or as a matter of contract interpretation.<sup>25</sup>

### Good faith in franchise agreements

As is the case in civil law jurisdictions, vulnerable contractual parties, such as franchisees, have often been given special consideration under the common law. Despite the lack of a general free-standing obligation, a duty to act in good faith has been recognised in certain common law cases in the context of a franchisor–franchisee relationship. Courts have found that a franchise agreement is a type of contract of adhesion, implying long-term partnerships that require mutual cooperation and consideration.<sup>26</sup> Courts have therefore taken these factors into account when interpreting the scope of the duties to act honestly and in good faith as they apply to franchisors and franchisees.<sup>27</sup> Courts have also cautioned that the determination as to whether a duty of good faith has been breached will be contingent upon all of the surrounding circumstances of a particular case – namely, the specific conduct that would be expected of a party must be considered on a case-by-case basis.<sup>28</sup>

Moreover, unlike in the civil law tradition, common law courts are divided as to whether terms can be implied in a contract by reason of the duties of good faith and honest performance where there is otherwise no indication that contracting parties agreed to an implied term or where the term sought to be implied was found to be inconsistent with the express terms of the contract.<sup>29</sup>

Although the approach of common law courts to the duty of good faith in franchise agreements has been inconsistent at times, the content of the duty of good faith in the franchise context may be summarised as follows:

- the franchisor must exercise its powers under the franchise agreement in good faith and with due regard to the interests of the franchisee;
- the franchisor must observe standards of 'honesty, fairness and reasonableness' and take into account the interests of its franchisees;
- the parties must not act in such a way that 'eviscerates or defeats the objectives of the agreement' or 'destroys the rights of the franchisee to enjoy the fruits of the contract';

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23 *Bhasin*, supra note 21 at para 73.

24 *ibid.* at para 60; Trachtenberg, Turgeon and Destrempes, supra note 4 at 95–96.

25 *Bhasin*, supra note 21 at para 52; Trachtenberg, Turgeon and Destrempes, supra note 4 at 95–96.

26 *Shelanu Inc v Print Three Franchising Corp*, 2003 CanLII 52151 (ON CA) (*Shelanu*).

27 *ibid.*

28 *ibid.*; *Bhasin*, supra note 21.

29 *Energy Fundamentals Group Inc v Veresen Inc*, 2015 ONCA 514 at paras 30–35; *Moulton Contracting Ltd v British Columbia*, 2015 BCCA 89 at para 78.

- neither party must substantially reduce the benefit of the bargain for the other, or cause significant harm to the other, in a manner contrary to the original intention and expectation of the parties; and
- where the franchisor is given discretion under the franchise agreement, it must be exercised reasonably and with proper justification, and may not be done subjectively, capriciously, or in a manner inconsistent with the reasonable expectations of the parties.<sup>30</sup>

While common law courts have not been as explicit as civil law courts with regard to the duties that flow from the organising principle of good faith, many franchise and business relationship statutes impose a duty of fair dealing on parties to such agreements.

### Statutory duty of fair dealing in franchise relationships

Franchise legislation in many jurisdictions imposes a general obligation of fair dealing on the parties in the performance and enforcement of their franchise agreement; for example, Canadian franchise disclosure laws set out such duties.<sup>31</sup> To fulfil this duty, franchisors must perform and enforce the franchise agreement in a manner that takes into account the interests of franchisees.<sup>32</sup> More specifically, when contemplating system-wide changes, a franchisor must consider the interests of the entire franchise network, as opposed to the interests of individual franchisees.<sup>33</sup> Additionally, before making system-wide changes, franchisors should engage in 'meaningful consultation' with their franchisees; it has even been suggested that engaging in a non-binding consultation process can allow a franchisor to potentially 'build an evidentiary record that can be deployed . . . in defence of allegations of bad faith'.<sup>34</sup>

Furthermore, franchisors are usually subject to stringent statutory pre-contractual disclosure obligations, which require them to provide a franchise disclosure document to every proposed franchisee before the sale of a franchise.<sup>35</sup> In the context of the renewal of franchise agreements, Canadian common law courts have held that a franchisor will have breached its duty of fair dealing if it unduly withholds information so as to preclude a franchisee from exercising its

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30 *Fairview Donut Inc v The TDL Group Corp*, 2012 ONSC 1252 (CanLII) at paras 502–503 (*Fairview Donut*); Edward (Ned) Levitt, 'Good Faith in Franchising', presented at Lexpert Conference on Implied Obligation of Good Faith, 2 June 2015, 1 at 4.

31 Arthur Wishart Act (Franchise Disclosure), 2000, SO 2000, c 3; The Franchises Act, CCSM c F156; Franchises Act, RSNB 2014, c 111; Franchises Act, RSPEI 1988, c F-14.1; Franchises Act, RSA 2000, c F-23.

32 Levitt, *supra* note 30.

33 Adam Ship and Eli Lederman, 'The State of the Law on Good Faith in Franchising: Best Practices and Practical Tips to Maximize Compliance and Mitigate Risk', presented at the Canadian Franchise Association's 2016 Law Day, 28 January 2016, 1 at 16–17.

34 *ibid*; *Fairview Donut*, *supra* note 28.

35 *Mendoza v Active Tire & Auto Inc*, 2017 ONCA 471 (CanLII); Levitt, *supra* note 30 at 7–10; So, *supra* note 4 at 241–248.

right to renewal.<sup>36</sup> The duty of fair dealing also prevents franchisors from exercising termination rights in an unreasonable or abusive manner.<sup>37</sup>

Although case law has provided some guidance as to how the statutory duty of fair dealing should be interpreted, the extent of this codified common law obligation is far from settled. Still, given that the duty of fair dealing does not generally 'override' unequivocal contractual provisions in the common law tradition, the breadth and scope of this duty may be mitigated by clearly drafted provisions of a franchise agreement.<sup>38</sup>

### **Challenges created by the duty of good faith**

There are several difficulties and challenges that arise as a result of the current state of the law on good faith, particularly as it applies in the franchise context. These issues include a lack of a uniform definition of the notion of good faith, limited guidance on the practical application of the notion of good faith, as well as difficulty in reconciling an implied duty of good faith with the freedom of contract of parties to a franchise relationship.

### **Lack of a uniform definition of the notion of good faith**

As discussed above, the civil law and common law traditions have very different approaches in characterising the notion of good faith. In each case, the duty of good faith, as it applies in the context of franchise agreements, plays a different role. On the one hand, in civil law jurisdictions, the duty to act in good faith appears to imply a positive obligation to take affirmative steps to, inter alia, support franchisees throughout the franchise relationship and be responsive to threats faced by the franchise brand against competition. On the other hand, the common law duty of honest performance, which originates from a general organising principle of good faith, seems to call for a negative obligation for franchisors to refrain from acting in a capricious manner towards franchisees.<sup>39</sup> Perhaps more importantly, while the distinction between the application of the principle of good faith in these diverging legal traditions may not always be described as simply, it is generally accepted that the notion of good faith in civil law would impose more significant expectations and obligations on a franchisor, and likely sooner, than would similar concepts under common law.

### **Practical application of the notion of good faith**

The concept of good faith remains difficult to apply in practice. Courts have used sweeping terms such as 'loyalty', 'reasonableness', 'collaboration' and 'honesty' to describe the notion of good faith. Although courts have stated that the duty of good faith is not a 'panacea', and that a franchisor is not required to guarantee the success of its franchisee's business, courts have provided limited guidance as to the practical application of the notion of good faith and the duties that flow

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36 *Salah v Timothy's Coffees of the World Inc*, 2010 ONCA 673 (CanLII) at paras 19-22; Levitt, *supra* note 30 at 11; Ship and Lederman, *supra* note 33 at 9-12.

37 *Shelanu*, *supra* note 26; Levitt, *supra* note 30 at 15-17; Ship and Lederman, *supra* note 33 at 6-9.

38 Levitt, *supra* note 30 at 5.

39 Manasvin Goswami, 'Coherence and Consistency in a System of Good Faith: Assessing and Explaining the Impact of *Bhasin v. Hrynew* on Canadian Contract Law' (2017), 77 S.C.L.R. (2d) 309; Judson, *supra* note 14 at 411-415.

from this notion, including in the context of franchise agreements, as well as other categories of contracts involving vulnerable parties.<sup>40</sup>

Moreover, many of the cases that have shaped franchisors' good faith obligations in both civil law and common law jurisdictions rely heavily on the factual circumstances arising in a particular context, which suggests that they may be rightfully distinguished in all but a few cases. It has even been posited that the malleable nature of the notion of good faith has given rise to inconsistent 'ad hoc jurisprudence'.<sup>41</sup> The extent to which these cases may be applied to franchisors and franchisees at large is therefore debatable.

### **Implied duty of good faith versus the freedom of contract**

Some authors contend that the far-reaching nature of the obligation of good faith, particularly in the civil law tradition, unduly interferes with the parties' freedom of contract and may lead to uncertainty and unpredictability in commercial relationships.<sup>42</sup> Where a duty of good faith is read into franchise agreements, it makes it difficult for franchisors to anticipate the types of obligations they must uphold. Indeed, in certain circumstances, a franchisor who has otherwise respected the explicit terms of its contract with a franchisee may be found to have breached its duty to act in good faith.<sup>43</sup> This lack of certainty can be quite disturbing in practice.

### **Practical suggestions for franchisors**

While the meaning of good faith is likely to continue to significantly evolve in response to current trends and future litigation, franchisors are encouraged to perform and enforce the terms of their franchise agreements in a manner consistent with the principles presented in this chapter. Regardless of where their franchise network is operating, franchisors should proceed with caution as the fundamental principles of good faith and honesty will undoubtedly continue to inform their conduct throughout their relationship with franchisees. More particularly, franchisors may consider implementing some or all of the following practical tips, with a view to complying with the duty to act in good faith and circumscribing the scope of their obligations that may lead to claims of unfair practices or conduct inconsistent with the requirements of good faith in any particular circumstances:

- ensure that they have carefully studied the good faith requirements in each jurisdiction where they wish to operate and, in particular, consider that their good faith obligations will likely prove to be more cumbersome in civil law jurisdictions;
- to avoid interpretative ambiguity and mitigate the risk that courts will read in more onerous obligations for a brand than were intended, franchisors should critically review their franchise agreements with a view to removing statements pertaining to the significant value and goodwill of their trademarks and business model, as well as any provisions that may be construed as commitments to enhance or engage in continued development of their brand;

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40 *Bhasin*, supra note 21 at para 70; Andrea M Bolieiro, 'Bhasin v. Hrynew and the principle of good faith in contracts: Moving towards a modern view of commercial relationships' (2015) 33:4 Adv J 23.

41 Judson, supra note 14 at 408-411.

42 *ibid.*

43 Trachtenberg, Turgeon and Destrempe, supra note 4 at 94.

- include provisions in the franchise agreement pursuant to which franchisees expressly acknowledge and agree that the franchisor is entitled to make decisions and take actions in the exercise of its discretion or rights with respect to an individual franchisee with a view to protecting or otherwise benefiting the franchised system or network generally;
- considering the significant operational requirements often imposed on franchisees that are central to their contractual compliance, franchisors should be mindful of possible corollary obligations for them to enforce these obligations across the franchised network. As a result, franchisors may consider including in their franchise agreements specific defaults and termination rights where franchisees fail to comply with imperative operating requirements or otherwise engage in behaviour that may tarnish the reputation of the franchised network, and franchisors should not be too reluctant to exercise their rights under such provisions;
- act responsibly and not fail to take timely steps to protect their franchised networks when threatened, including as a result of competitive threats in the market, by offering some attempt at resolving genuine concerns of franchisees about the viability of the franchised system or the future of the franchised business. If a franchisor is in a position to demonstrate that it genuinely took some measure of response in order to assist its franchised network in dealing with competitive forces, it is unlikely that its conduct will be met with severe scrutiny; and
- avoid drastically changing tack during the course of renewal discussions and refrain from engaging in conduct that could be seen as provoking an arbitrary impasse in the renewal process.

Other steps to mitigate risks for franchisors may also be explored and will vary based on a franchisor's operations and market segment. Specific solutions may need to be adapted based on the nature of any given business and its approach to franchising.

### **Conclusion**

The obligation to act in good faith, as it applies in the context of franchise agreements, is a burgeoning field. In light of the developing recognition of the duty to act in good faith in both common law and civil law jurisdictions, it will not be surprising if the trend continues in cases where one party's conduct is inherently unreasonable, unfair or otherwise offends the basic tenets of commercial dealings. Given the recent shifts in the scope of protections recognised for franchisees in various jurisdictions worldwide, it will be important for franchisors conducting business both nationally and internationally to monitor and comply with their good faith obligations for the foreseeable future.

# Appendix 1

## About the Authors

### **Bruno Floriani**

Lapointe Rosenstein Marchand Melançon LLP

Bruno Floriani is a leading practitioner in business law, with a particular focus on franchise, distribution, licensing and technology. For over 30 years, Bruno has advised a wide range of business clients, from large corporations and public companies to SMEs, in various industries, including retail, hospitality, manufacturing, professional services and IT.

Bruno has extensive experience in structuring complex franchising, licensing, supply and joint venture arrangements, including in connection with the international expansion of his clients' business operations around the world, as well as advising foreign companies with respect to their entry into the Canadian market and continued compliance with Canadian law.

His experience with general business matters, combined with his expertise in the fields of domestic and international distribution, franchising, licensing and technology, allow him to provide clients with a comprehensive and invaluable perspective on matters that concern them, both locally and abroad. By familiarising himself with the important aspects of his clients' business operations, Bruno provides practical legal and business advice geared towards each client's specific industry.

Given his proficiency in these areas, Bruno has frequently lectured at various conferences on domestic and international distribution, franchising, licensing and joint ventures, as well as intellectual property issues and privacy law, including at conferences organised by the International Franchise Association (IFA), the International Council of Shopping Centers (ICSC), the Quebec Retail Council (CQCD), the American Bar Association (ABA), the Quebec Bar Association and the Licensing Executive Society (LES).

He has also written extensively on these topics in various national and international legal journals and trade periodicals, and currently writes quarterly for the International Law Office, an internet newsletter, in the area of Canadian franchise law. Bruno has been the editor (and Canadian co-contributor) of the multinational annual guide for legal practitioners, *Getting the Deal Through: Licensing*, since 2009, and the Canadian co-contributor for *Getting the Deal Through: Franchising* since 2008 and *Getting the Deal Through: Distribution & Agency* since 2016.

Bruno is recognised in Canada and abroad as a leading practitioner in the franchise field by *Chambers*, *Expert*, *Who's Who Legal: Franchise* and *Who's Who Legal: Canada*, and is recognised as an expert in licensing by *Global Law Expert*, in business law by *Who's Who Legal* and in the technology field by *Best Lawyers*.

### **Marissa Carnevale**

Lapointe Rosenstein Marchand Melançon LLP

Marissa Carnevale practises law in the firm's commercial law group. She has extensive experience in franchising, licensing and technology law, as well as experience with supply and distribution matters and various other commercial arrangements. By familiarising herself with all aspects of a client's business operations, she is able to provide substantial legal advice geared towards any specific industry, including but not limited to manufacturing, franchising, retail and the technology sector.

Marissa specialises in negotiating and drafting complex legal agreements relating to licensing, franchising and distribution agreements as well as technology-related agreements. Her skilled expertise allows her to regularly advise corporations of all sizes in matters such as franchising, licensing, e-commerce, intellectual property matters, privacy, social media, contests, product labelling, marketing and advertising, consumer protection, French language, export controls, and other regulatory areas in order to comply with Canadian legal requirements, including those specific to the province of Quebec. She also advises foreign companies with respect to their entry into the Canadian market and continued compliance with Canadian law.

Marissa's experience has provided her with the opportunity to co-author publications on franchising in Canada for the International Law Office, an online periodical, as well as *Getting the Deal Through*, a guide for legal practitioners, in both its *Franchise* and *Licensing* editions. In addition, she presented on advertising in social media as part of a panel of counsel at the 38th Annual Forum on Franchising of the American Bar Association.

Marissa is fluent in English and French.

### **Tanya Nakhoul**

Lapointe Rosenstein Marchand Melançon LLP

Tanya Nakhoul practises law within the firm's commercial law, and licensing and technology groups, as well as in franchising. Her practice supports the firm's international and national clients by providing legal advice pertaining to a variety of industries, such as franchising, retail, e-commerce, manufacturing and technology.

Tanya specialises in negotiating and drafting legal agreements relating to licensing, franchising and distribution, as well as technology-related agreements. Her expertise allows her to advise clients in a variety of matters, including, but not limited to, supply and distribution, e-commerce, social media, intellectual property matters, marketing, advertising, consumer protection, French language compliance in the province of Quebec and other regulatory areas. She also regularly advises international clients with respect to Canadian business practices and regulatory compliance with Canadian law.

Tanya's knowledge and experience has allowed her to contribute to the drafting of various publications for both internal newsletters and external publications pertaining to legal

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developments, as well as guides for legal practitioners, relating to franchising, licensing, distribution and technology. She has also presented on the legal implications of financial technology (fintech), mobile payments and cyber currency.

Tanya is fluent in English and French.

### **Lapointe Rosenstein Marchand Melançon LLP**

1 Place Ville Marie

Suite 1300

Montreal, QC, H3B 0E6

Canada

Tel: +1 514 925 6300

Fax: +1 514 925 9001

[bruno.floriani@lrmm.com](mailto:bruno.floriani@lrmm.com)

[marissa.carnevale@lrmm.com](mailto:marissa.carnevale@lrmm.com)

[tanya.nakhoul@lrmm.com](mailto:tanya.nakhoul@lrmm.com)

[www.lrmm.com](http://www.lrmm.com)



