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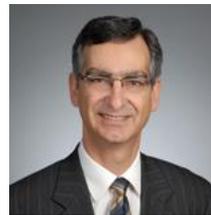
Franchise Law in Canada

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To the end of the term and beyond: perpetual renewal clauses are considered legal



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Introduction

Automatic renewal provisions are common in franchise agreements, and the Quebec Court of Appeal recently addressed the previously unanswered question of whether a franchise agreement may include a clause that would have the effect of renewing the agreement perpetually. In other words, the Court was called upon to determine whether perpetual obligations are enforceable pursuant to Quebec civil law. In *Uniprix v. Gestion Gosselin et Bérubé inc.*,⁽¹⁾ the Quebec Court of Appeal dismissed an appeal lodged by a drugstore franchisor, Uniprix, in respect of a judgment of the Superior Court of Quebec rendered in December 2013 which upheld the validity of a renewal clause that did not provide any limitation on the number of times a contract of affiliation could be renewed.

Facts

In 1998, Uniprix entered into a contract of affiliation with the respondents, members of the Gosselin group, pursuant to which the Gosselin group operated a pharmacy under the Uniprix banner and concept, within premises owned by Uniprix. The contract provided a five-year term, and contained a renewal clause that required the Gosselin group to notify Uniprix of its intention to renew or not renew the contract of affiliation six months before the expiration of the term, failing which the contract was deemed to be renewed for an additional five years. The express terms of the renewal clause did not confer upon Uniprix any role in the decision to end or renew the affiliation, and Uniprix could only terminate the contract *with cause* in accordance with its contractual termination rights. Therefore, unless the Gosselin group elected not to renew the term of the contract by giving

the required notice to Uniprix, the contract of affiliation could potentially remain in force perpetually, particularly given that the contract did not limit the number of times it could be so renewed.

In fact, the contract had already been renewed twice, both in 2003 and 2008, as a result of the absence of any notice of non-renewal by the Gosselin group. When the second renewal term was nearing expiration, Uniprix sent a notice to the Gosselin group stating that it had decided not to renew the contract of affiliation a third time.

The Gosselin group instituted proceedings contesting the validity of Uniprix's non-renewal notice, arguing that the renewal option could only be exercised by the Gosselin Group, and filed a motion for declaratory judgment to the effect that Uniprix remained bound by the contract of affiliation, and requested the issuance of a permanent injunction to compel Uniprix to comply with the contract.

Decision

The Superior Court agreed with the Gosselin group,⁽²⁾ holding that the renewal clause was clear and unambiguous and that automatic renewal clauses under which unilateral renewal rights are granted in favour of one party are valid under Quebec civil law. The Superior Court also held that the renewal option in the case at hand could only be exercised by the Gosselin group. Therefore, without elaborating on the question of perpetual obligations in contracts, the Superior Court determined that Uniprix's notice of non-renewal was not valid. Uniprix appealed the decision before the Quebec Court of Appeal.

The majority of the Court of Appeal dismissed the appeal and upheld the Superior Court's judgment, finding that the renewal option could only be exercised by the Gosselin group and was valid despite the potentially unlimited number of renewals of the term of the contract, given that the term of the contract between Uniprix and the Gosselin group was to be automatically renewed unless the Gosselin group provided the required notice of its intention not to renew.

The majority further stated that perpetual obligations are perfectly enforceable under Quebec civil law, and emphasized that they failed to find any general prohibition against perpetual obligations in the *Civil Code of Quebec*.

Furthermore, the majority found that the fundamentals of Quebec's contract law would not be compromised by recognizing that perpetual obligations may flow from a contract, and placed emphasis on the fact that Uniprix was a sophisticated corporation and that its freedom was not significantly compromised by the perpetually renewable term of the contract of affiliation. The majority also stressed the importance of preserving the parties' contractual freedom where the law imposes no limitations, and clearly stated that perpetual obligations are enforceable.

Moreover, the majority found the contract of affiliation to be a fixed term contract, terminable in accordance with its provisions, as opposed to the dissenting judge, who was of the view that this type of the renewal clause had the effect of transforming the term from fixed to indeterminate, thereby concluding that the contract of affiliation could be terminated at will by either party upon providing reasonable notice to the other party. This determination by the majority of the Court of Appeal has important implications with respect to termination rights, given the previous uncertainty as to whether perpetually renewable contracts should be considered fixed term contracts or contracts with an indeterminate term for purposes of Quebec civil law.

The appeal was dismissed.

Comment

With this long-awaited decision, the Court of Appeal has clarified that perpetual renewal clauses are not prohibited in Quebec. Franchise and affiliate networks as well as banner associations will be required to respect renewal clauses in their agreements even where no strict time limits are provided, and courts will likely enforce such provisions even though they may lead to perpetual obligations.

This decision is a reminder of the importance of having clear renewal conditions and processes in place in the context of franchise, affiliate and banner association agreements: the notices and other formalities required for renewals, and the party or parties entitled to exercise renewal rights, should always be clearly described in the agreement.

Automatic renewal clauses would not typically be recommended for franchise, affiliate and banner networks, given that repeated renewals and/or perpetuity in such arrangements may be detrimental to a network insofar as they may limit the possibility for franchisors or banners to be responsive to changes in the market and evolving operational considerations.

Where automatic renewal provisions cannot be avoided, the renewal of an agreement should be expressly stated to be contingent upon the satisfaction of various conditions, such as the franchisee or affiliate not being in default under its current agreement, and the execution of the current form of agreement put forth by the franchisor or banner at the time of renewal.

In addition, renewal clauses should clearly provide the consequences of any failure to satisfy the prescribed renewal conditions, namely that the term of the agreement will terminate without any further right to renew.

Parties should take care to avoid drafting renewal clauses that may be exercised unilaterally by one party indefinitely. Among a variety of options, parties may limit the number of times an agreement may be renewed by one party or consider the possibility of allowing either party to end the relationship after a certain number of renewals by providing reasonable notice to the other, thereby allowing both parties the flexibility to eventually stop the renewal cycle if desired.

Uniprix has further appealed the Court of Appeal's decision and was granted leave to appeal before the Supreme Court of Canada in May 2016. We will continue to monitor developments in this regard.

(1) 2015 QCCA 1427

(2) *Gestion Gosselin et Bérubé inc. c. Uniprix inc.*, 2013 QCCS 6251

The content of this article is intended to provide general commentary only and should not be relied upon as legal advice.

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