

CorporateLiveWire

FRANCHISING 2020 VIRTUAL ROUND TABLE

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Introduction & Contents

In this roundtable, six franchise law experts discuss the importance of due diligence, exit strategies and intellectual property management in franchising. They also identify common disputes and mistakes franchisors/franchisees typically make, as well as outlining the impact of COVID-19 on franchise opportunities. Featured countries are: Australia, Colombia, Denmark, Malaysia, New Zealand, and USA.



James Drakeford
Editor In Chief

Meet The Experts



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I have been in practice and/or partnership since 1982. I merged my firm after 17 years in practice with Wisewoulds Lawyers in January 2003 and recently joined Marsh & Maher in January 2015.

I have numerous published articles in the Australian Financial Review, Business Franchise magazine, Franchise Australia and New Zealand Guide and online.

I have developed considerable business expertise from my own experience in retail business with the Ted's Camera Stores Group and acting for a large range of clients including Philip Murphy Wine and Spirits, Dilmah Tea (Australia), Vapiano Restaurants (Germany), Aeroklas (Thailand); I provide strategic advice to business in a wide range of industries.

I enjoy the challenge of finding lateral solutions and giving direct "no bull" advice to clients.

We operate with clients in an open and transparent manner regarding fees and have flexible fee arrangements for clients including fixed fees based on scope of works for many services we provide. This gives our clients the ability to monitor and budget for legal fees.

I am an old dog who plays soccer with the over 45's and over summer I race a one design sabre boat. I enjoy playing guitar and song writing with my brother Tom and enjoying time with my family.



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Andrew Sherman is a Partner in the Corporate Department of Seyfarth Shaw LLP. He focuses his practice on issues affecting business growth for companies at all stages, including developing strategies for licensing and leveraging intellectual property and technology assets, intellectual asset management and harvesting, as well as international corporate transactional and franchising matters.

He has served as a legal and strategic advisor to dozens of Fortune 500 companies and hundreds of emerging growth companies. He has represented U.S. and international clients from early stage, rapidly growing start-ups, to closely held franchisors and middle market companies, to multibillion dollar international conglomerates. He also counsels on issues such as franchising, licensing, joint ventures, strategic alliances, capital formation, distribution channels, technology development, and mergers and acquisitions.

Mr. Sherman has written nearly 30 books on the legal and strategic aspects of business growth, franchising, capital formation, and the leveraging of intellectual property, most of which can be found on Amazon. He also has published many articles on similar topics and is a frequent keynote speaker at business conferences, seminars, and webinars. He has appeared as a guest commentator on CNN, NPR, and CBS News Radio, among others, and has been interviewed on legal topics by The Wall Street Journal, USA Today, Forbes, U.S. News & World Report, and other publications.

Mr. Sherman serves as an adjunct professor in the M.B.A. programs at the University of Maryland and as well as the law school at Georgetown University and is a multiple recipient of the University of Maryland at College Park's Krowe Excellence in Teaching Award.



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Meet The Experts



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From my involvement on copyright and trademark matters I have developed a strong practice on franchising and advertising law that focus on compliance with consumer protection statutes and third parties rights. Recently advised the most important credit card brands, and companies involved in cutting edge technology and social media such as Intel and Facebook, as well as many other with equally demanding high standards of legal counsel.

Also with my IP expertise and contractual background I have helped foreign and local companies implement franchise operations in our country that take advantage of of the current propitious business climate. To name a few of the recent Franchise companies that have initiated their operations in Colombia with our help we have The Gap, P.F Chang's, Johnny Rockets, Villa Pizza, Engel & Volkers, Hard Rock Hotels, Hertz.



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Stewart Germann who is acknowledged as New Zealand's leading franchising lawyer with over 35 years experience in this area, is a recognised national and international guest speaker at franchise conferences (New Zealand, Australia, USA).

Stewart Germann Law Office is New Zealand's longest established specialist franchising law firm and Stewart is one of only two New Zealand lawyers included in the International Who's Who of Franchise Lawyers for 2014.

Stewart's clients include many of New Zealand's best known national and international franchise brands and he has extensive franchising contacts worldwide and locally.

He is actively involved in international franchising and has published articles in the International Journal of Franchising Law.



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Adhuna is the Managing Partner of the firm and handles and advises clients on a broad range of intellectual property ("IP") issues including franchising, licensing, related corporate matters as well as ICT agreements. With regard to franchising, she focuses on assisting foreign companies looking to enter the Malaysian market, and in particular has advised and acted for several successful foreign franchisors in the food and beverage and retail industry.

She also handles IP litigation matters, as well as advises clients on issues relating to copyright, trade mark, patents and industrial design protection and prosecution.

Adhuna has been in practice for almost 20 years, is a member of the Malaysian Bar and is a registered patent, trade mark and industrial design agent. She is also a member of MIPA, INTA, LES (Malaysia), LES International and APAA, and has been recognised in the International Who's Who Legal: Franchise in 2014, 2015, 2016, 2017, 2018 and 2019.



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Dan Bjerg Geary is a partner with the top Danish law firm Bech-Bruun where he leads the work within franchising and distribution. Dan has more than 15 years' experience for Danish and international clients. He is regularly involved in key mandates for development and roll-out of franchise concepts and establishment of Master Franchises. Dan also handles dispute resolution and brand protection for his clients with the right to appear before the Supreme Court and has a strong

track record in litigation. Dan sits on the board of the Danish Franchise Federation and enjoys endorsements in Chambers, Legal500, Client Choice, IAM Patent 1000, WTR1000.



Q1. What franchise opportunities are currently proving most popular at the moment, and why?



Andrew Sherman

Sherman: The most popular franchise opportunities at the moment are focused on the current work and life trends which have been affected by COVID-19 and global economic uncertainty. This includes sectors such as commercial, industrial, residential cleaning and sanitation services, health care and wellness (particularly if no physical interaction is required, such as online fitness classes), and food and grocery take-out and delivery. Home improvement and remodeling services are also proving popular as many homeowners are re-thinking the configuration of their living quarters with a greater emphasis on accommodations for greater home offices, home entertainment and home schooling.



Juan Carlos Uribe

Uribe: At the start of 2020, the most popular franchises in Colombia were in the gastronomy, service and health beauty sectors, according to *Colfranquicias* (the Colombian Chamber of Franchises) One of the reasons is that the entry cost is not as demanding as other industries. However, since the COVID-19 crisis has been particularly severe in the restaurants and hospitality sectors, there have been more enquiries towards health related activities.



Robert Toth

Toth: Putting aside COVID-19, which has affected the economies of most countries, we have seen an increase in overseas businesses from the USA, UK, Asia, and some parts of Europe looking to enter the Australian market over the past 12 months as a stable market to grow and expand into.

The franchises we have been involved in mostly relate to services that provide home maintenance and aged care support; health, fitness and beauty; and online business where the overheads are much lower as they do not need to lease premises. Other sectors are in the preschool education and professional services such as real estate advocacy, accountancy and bookkeeping, and even law firms are being franchised! Mobile franchise services are popular as they are a lower entry cost and give franchisees flexibility in how and when they work.



Adhuna Kamarul Ariffin

Ariffin: The Franchise Act 1998 was drafted with the business format franchise in mind, and of these, the lion's share is in the food and beverage industry, followed by clothing and accessories. Education and childcare, and services and maintenance are also growing fairly rapidly in Malaysia.

While there is healthy growth in the local franchise industry, about 40% of franchise concepts in Malaysia are foreign. A majority of these foreign franchisors are from USA, followed by Singapore and United Kingdom. Malaysia is proving to be quite popular with foreign franchises quite possibly because of the ease with which the locals are embracing new trends.

"Putting aside COVID-19, which has affected the economies of most countries, we have seen an increase in overseas businesses from the USA, UK, Asia, and some parts of Europe looking to enter the Australian market over the past 12 months as a stable market to grow and expand into."

- Robert Toth -

Q2. What legislative conditions make a particular jurisdiction appealing or unappealing to franchisors?



Andrew Sherman

Sherman: The legislative conditions that make a particular jurisdiction attractive to a franchisor typically include a general "pro-business, lower tax rate" environment, with incentives for development for new businesses and retail formats, such as the growth of opportunity zones in the United States.

There are also franchise specific statutes that can affect the attractiveness of a particular jurisdiction, such as registration and disclosure laws, ongoing relationship management statutes and anti-termination laws, which would adversely affect the procedures for handling franchise discrepancy to end the relationship with a given franchisee.

Finally, there are a wide variety of labour and employment laws which could directly or indirectly affect the franchisor business model, such as California's AB-6 laws, which very recently may force companies such as Uber and Lyft to hire their drivers as full-time employees, or look at alternative models such as franchising.



Juan Carlos Uribe

Uribe: Jurisdiction conditions and regimes about which we are asked about the most are: (i) taxation issues and currency controls; (ii) local employment policies (liability) and; (iii) alternative dispute resolution and governing law.

Q3. Are there any notable compliance issues franchisors/franchisees should be mindful of in your jurisdiction?



Andrew Sherman

Sherman: COVID-19 has created a multitude of new compliance challenges for both franchisors and their franchisees in the areas of health, safety, hygiene, employee testing, food handling and a wide variety of related compliance matters which are critical to the on-going viability of the franchise system, as well as protection of the brand and overall consumer trust. In addition to COVID-19, the uptick in racial and social unrest have caused additional compliance challenges in the area of diversity and inclusion in hiring, promotion, and firing of employees, as well as the need for diversity in board governance. One unfortunate consequence of this civil unrest has been that the protestors, looting and violence has also made safety and security and proper alarm systems an increasingly important compliance priority.



Juan Carlos Uribe

Uribe: Yes, given the reputation of Colombia, both the franchisee and the franchisor must do the transparency due diligence, including anti-money laundering. Franchisee compliance is a key factor in the success of the network.

Franchisors should consider implementing compliance programmes to both govern their own business activities in compliance with Colombian laws and also minimise the risk of franchisee misconduct. Compliance measures to consider include: (i) identifying compliance officials; (ii) screening potential business partners; (iii) educating key personnel; (iv) conducting on-going risk assessments, and identifying potential red flags in proposed and existing business relationships; (v) requiring compliance from business partners and individual shareholders of franchisees; and (vi) conducting internal audits to prevent money laundering.

Q3. Are there any notable compliance issues franchisors/franchisees should be mindful of in your jurisdiction?



Stewart Germann

Germann: New Zealand encourages and welcomes franchise systems from overseas and in all cases the legal documents will need changing for New Zealand conditions. An international franchisor can expand by a number of methods including (i) appointing a master franchisee in a country, (ii) appointing an area developer, (iii) appointing unit franchisees, or (iv) via a joint venture with a country representative.

Some clauses in the agreement will require attention when an overseas franchisor wants to enter a country. This includes franchise payments, taxation issues where non-resident withholding tax must be deducted, personal property securities, restraint of trade, dispute resolution, and the governing law. In New Zealand there is no franchise-specific legislation but there are a number of statutes which affect franchising, including the Fair Trading Act 1986 and the Commerce Act 1986 which was recently amended by the Commerce (Cartels and Other Matters) Amendment Act 2017.

There is no mandatory disclosure regime but there is the Franchise Association of New Zealand which has its own Code of Practice and Code of Ethics that all members must follow. Professional taxation advice should be obtained and if there is a double tax agreement with the relevant country, that will assist greatly. Those agreements generally limit the taxing rights of each country (depending on the type of income derived) as well as helping to reduce double taxation. For example, most agreements limit the foreign country's tax on royalty payments to 10% but accountants have a key role to play in relation to all tax aspects.

International franchising has matured greatly over the years and there are attorneys, accountants and consultants well experienced in all aspects so if you wish to embark on international franchising you should go to people with such experience.

Q4. What should be included in an effective franchise agreement and what are the biggest mistakes clients typically make from the offset?



Stewart Germann

Germann: A properly executed franchise agreement is the fundamental document to rely on in relation to franchising. Care must be taken to see that the document has been correctly executed.

Normally a franchisee will be a company, and in New Zealand our Companies Act 1993 requires that two directors sign on behalf of the company. If the company only has one director then that person would sign and his or her signature must be properly witnessed by an independent third party. When a franchisee is a company then there should be a personal guarantee by the directors and shareholders of that company. The agreement will contain a termination clause setting out events of termination. When a franchisee breaches the franchise agreement that might trigger a formal notice of breach of franchise agreement to be prepared by the franchisor and issued to the franchisee and all guarantors.

In relation to enforcement of the agreement, this would be done through the courts in New Zealand. For serious breaches like restraint on competition, the franchisor may apply for an interim injunction. For a breach like money owing, a franchisor would issue a statement of claim and sue the franchisee in the District Court.

“International franchising has matured greatly over the years and there are attorneys, accountants and consultants well experienced in all aspects so if you wish to embark on international franchising you should go to people with such experience.”
- Stewart Germann -



Adhuna Kamarul Ariffin

Ariffin: When the franchise agreement already clearly identifies incidences that amount to breaches of the agreement, it is imperative for the non-defaulting party to follow through with the provisions laid out in event of breach. The best drafted agreement will be of no assistance if the processes provided in case of breaches are ignored. Not following up on stipulated procedures, affirming or ignoring wrongdoings and erroneous notice processes are some of the mistakes that not only undermines the non-defaulting party's rights, they also delay the course of rectifying those mistakes, sometimes to the point where the communication between the parties have broken down beyond repair.



Dan Bjerg Geary

Geary: Many franchise agreements are well drafted to suit the current situation but allow little flexibility for the franchisor to adapt the franchise concept to new trends and developments, or simply a desire to change the revenue model. It is advisable to have a basis in the franchise agreement to impose new terms, introduce new elements in the franchise concept. Drivers for such changes can include new payment solutions, new online trade platforms and social media platforms. Also, increased competition or disruption of the core elements of the franchise concept may affect the types of products and services offered and the business model and franchise fee structure.

Among the biggest mistakes we often see fairly simple document processes being mistaken or flawed. This includes: (i) failure to obtain personal commitments from the individual person operating a franchisee through a limited liability company. Such commitments may be financial guarantees for debt and non-compete and secrecy commitments. Or (ii) failure to obtain relevant document adjacent to the franchise business, such as a pre-approved assignment of the lease, security for goods sold and fees due.

Q5. To what extent does a cross-border franchise require a different approach? Is an added element of due diligence required?



Andrew Sherman

Sherman: What works well in your home market will not always work or translate effectively overseas. Too often franchisors misjudge, misread, or misunderstand the demand patterns or business model adjustments that will be necessary to be successful abroad.

Important aspects for the franchisor to consider before opening a business abroad include knowing your system's strengths and weaknesses and its adaptability for overseas deployment. It is critical to have a secure domestic foundation from which the international programme can be launched. Make sure that adequate capital, resources, personnel, support systems and training programs are in place to assist your franchisees abroad.

In addition, it is also vitally important to know your targeted market. Going into a new market blindly can be costly and lead to disputes. An added element of due diligence should include market studies and research, which should be conducted to measure market demand and competition for your company's products and services. Obtaining information about the targeted country to gather data on economic trends, political stability, currency exchange rates, religious considerations, dietary restrictions, lifestyle issues, foreign investment and approval procedures should also be considered.

The recently adopted restrictions on immigration and business travel which were put into place late Spring/early Summer of 2020 by the Trump administration, have also significantly affected the growth of cross-border franchises (both in bound and out bound) for franchisors in the United States and overseas for franchisors interested in the United States market.

Q5. To what extent does a cross-border franchise require a different approach? Is an added element of due diligence required?



Juan Carlos Uribe

Uribe: The following are the main challenges regarding cross-border franchise agreements: (i) the erroneous idea that a franchise can be granted without the previous registration of the trademark before the local Trademark Office (Superintendence of Industry and Commerce); (ii) difficulties related to tax, customs and foreign exchange regulations in Colombia; (iii) the local licensing regulation that seem to contradict the independent ownership model of a franchise since we have joint responsibility of producers, retailers and suppliers before the costumers and; (iv) the local employment policies. We do not encourage this approach to our clients.

As for the due diligence, these are some factors that are not normally considered:

- The Franchisees have too broad expectations regarding the franchise that have been acquired if it is a foreign brand;
- The Franchisees do not request financial reports of the whole chain (not just some branches);
- The Franchisees do not request projections of growth of the economic sector of the franchise in equivalent markets.



Stewart Germann

Germann: Due diligence is very important in franchising. When a prospective franchisee is ascertaining information in relation to the franchise system, it will do its own due diligence. The same goes for the franchisor who will be doing due diligence on the franchisee.

By due diligence I mean checking all information provided to ensure that it is true and correct. Such information might include distribution contracts, approved products and approved suppliers, in the case of a prospective franchisee talking to existing franchisees and asking key questions about the franchisor and the system and checking on financial aspects of the franchisor. From a franchisor point of view, due diligence will include verifying the assets and liabilities of the prospective franchisee, obtaining references and checking upon them, credit checks, criminal checks and asking the right questions to obtain the correct answers.

Because most countries are multicultural, cultural due diligence is another key aspect. It would be important for a franchisor to check on the customs and social behaviour of the prospective franchisee. One definition of culture says that it is a "set of patterns of human activity within a community or social group and the symbolic structures that give significance to such activity. Customs, laws, dress, architectural style, social standards, religious beliefs, and traditions are all examples of cultural elements".

Culture will include customs, religion, language, government, economy and arts so from a franchising point of view the franchisor has a duty to ensure that the culture of a prospective franchisee will fit the system and any particular aspects of the culture should not be an impediment to being a franchisee. Also, in countries where English is the predominant language it would be important for a franchisee to speak English.

In summary, culture is often low down on the list of a franchisor when assessing a potential franchisee but it should be high on the list, for if the particular culture will not fit the system the relationship will probably not work.

"Because most countries are multicultural, cultural due diligence is another key aspect. It would be important for a franchisor to check on the customs and social behaviour of the prospective franchisee."
- Stewart Germann -



Robert Toth

Toth: Many franchise systems that are successful overseas may not translate readily to the Australian market. In fact, many franchise systems that are successful in one State or Territory in Australia often have difficulty in expanding to another State due to significant differences in the demographics, consumer trends and expectations. The most common disputes arise from a lack of support so appointing a master franchisor can assist with this issue as well as having developed a business entry plan. Linking in with specialist franchise lawyers and consultants can assist an overseas company avoid costly and often obvious mistakes which can be avoided by engaging local expertise who have local on-the-ground knowledge.

Another issue is ensuring compliance with our Australian Franchise Code that regulates the franchise sector throughout the whole country



Dan Bjerg Geary

Geary: Even the best drafted franchise agreements will require scrutiny and due diligence when being applied in a cross-border context. Obviously, a legalisation under local law to detect contract provisions that are illegal, void, or difficult to enforce is a must. Also, the existence of a franchise law and/or compliance with the local code of ethics for franchising may require further analysis of the franchise concept and the contract papers.

A more complex challenge is associated with the structural factors in a particular country as well as non-franchise relate areas with specific legislation and requirements, all of which may impact the efficiency and operation of the franchise ad its legality.

The handling of leases to premises is one that differs among countries on many areas (e.g. the ability to assign the lease, the duration of the lease). This, again, may affect the duration of the franchise agreement or reduce franchisor's control of the premises. Other areas with great diversity among countries include financial security for the franchisor and employment related issues. Once the contractual documents are adapted, the pre-signing phase may be critical for the franchisor and failure to disclose relevant information to the franchisee may in many countries result in damages claims or contract annulment.



Adhuna Kamarul Ariffin

Ariffin: Notwithstanding the readiness with which Malaysians embrace foreign franchises, some form of due diligence is always advisable. However attractive a foreign franchise system may appear from the outset, if a local, better and above all cheaper alternative already exists it may be difficult for the foreign business to penetrate the market, especially if the foreign element makes the overall costs for consumers higher without any perceived added value.

The Franchise Development Division requires all franchisors (including master franchisees) to provide three years audited financial statements of the franchised business in their applications for registrations. This requirement in some way helps to weed out franchisors without proven track records from entering the country, and protects potential franchisees from untested franchises and inexperienced master franchisees.

"Even the best drafted franchise agreements will require scrutiny and due diligence when being applied in a cross-border context. Obviously, a legalisation under local law to detect contract provisions that are illegal, void, or difficult to enforce is a must."
- Dan Bjerg Geary -

Q6. What are the most common areas for domestic/cross-border franchise-related disputes, and how can these be remedied?



Juan Carlos Uribe

Uribe: Frequent subjects of dispute arising in the franchisor/ franchisee relationship include: (i) the request of payment the amount due by the franchisee as royalties, advertising; (ii) the breach of non-compete clause and the unilateral change of the contractual conditions by the franchisor; (iii) the expectation of technical assistance, by the franchisor to the franchisee and; (iv) supervision and support.



Robert Toth

Toth: The Code requires overseas franchisors to ensure their disclosure documents and their franchise agreements are Franchise Code compliant. Australia has a strong compliance regime and a breach of the Code can impose hefty fines and penalties and damage a company's brand and reputation.



Adhuna Kamarul Ariffin

Ariffin: Communication is key in any relationship, and having a system of escalated levels of dispute resolution would go some way in keeping the franchisor-franchisee dynamics on an even keel. Providing for time for internal discussions to take place as a first level before taking the matter up a notch to non-binding mediation would enable parties to keep things civil before escalating even further.

Although not made compulsory by the Franchise Act, for a number of years now the Franchise Development Division has actively encouraged the inclusion of alternative dispute resolution through arbitration in franchise agreements. This could be resorted to if mediation fails, and would still leave the avenue of applying to the courts for any interlocutory injunctions that may be needed to preserve the status quo.

Q7. What systems do the best job of improving franchise relationships and what options are available to franchisor/franchisee if they are unable to resolve the dispute amicably?



Juan Carlos Uribe

Uribe: The parties can choose to resolve disputes through:

- Conciliation
- Mediation
- Arbitration
- Court

Parties can freely provide that the contract will be submitted to a court in the franchisor's country or to an international arbitration. In a domestic contract these clauses, if not individually negotiated, should be specifically approved in writing by the franchisee.

If the parties cannot reach an agreement through mediation or conciliation, arbitration typically provides a speedier resolution than court proceedings. In addition, some parties prefer arbitration because arbitrators often have specialised knowledge of the matters in question and because the proceeding remains confidential.

However, arbitration is not ideal in all circumstances as it is costlier, especially if an arbitration panel is appointed and because arbitrators cannot grant interim measures.

A relatively small number of disputes arising from franchise agreements are settled through arbitration, compared to the number of disputes submitted to the ordinary courts. International franchise agreements are usually settled through arbitration, which is considered more neutral, with respect to the parties.



Stewart Germann

Germann: Dispute resolution in relation to franchising really works, in my opinion. Because the relationship is very important between a franchisor and a franchisee, there needs to be a mechanism to sort out disagreements or disputes. Invariably in just about every franchise agreement I have seen there is a dispute resolution provision recommending either mediation or arbitration.

Mediation is very successful in New Zealand and I am a qualified mediator and have been involved in many mediations. Normally the clause starts off by saying that where a dispute arises between the parties, the complainant will set out the nature of the dispute in writing. Both parties will make every effort to resolve the dispute by mutual negotiation. However, in the event that the parties are unable to reach a resolution of the dispute within 21 days of the dispute first being raised by one party with the other, either party may issue a mediation notice in writing notifying the other party that it seeks to have the dispute resolved by mediation which must take place at a location to be agreed between the parties. A mechanism should be used determine the venue if both parties fail to agree on a location.

The next step is to appoint a mediator. The agreement should set out the mode of appointment and, if the parties cannot agree, then a mechanism for appointment of a mediator. In any mediation everything that occurs before the mediator will be in confidence and in closed session which is a huge advantage for mediation. Normally all discussions will be on a 'without prejudice' basis and any documents used at the mediation are destroyed afterwards. Each party to the mediation must be given proper opportunity to present its case and the mediator is required to act fairly, in good faith and without bias for the purpose of seeking a resolution of the dispute and to treat all matters in confidence. The mediator will have regard to the fairness and reasonableness of all matters relating to the dispute including the need for the franchisor to maintain the integrity of its name, image and the system and the reasonable interests of other franchisees of the system. The parties to a mediation must co-operate with a view to the mediation being determined as speedily as possible.

Normally the costs of the mediation will be borne equally by the parties unless otherwise agreed. Mediation is a voluntary process and the mediator assists the parties to reach a decision but does not impose it. On the other hand arbitration is a similar process which preserves confidentiality of the brand and the parties. However, the main difference is that the arbitrator will make a decision which is binding on the parties and can be enforced. That decision, known as an award, can only be challenged by any party if the arbitrator has made an error of law. It is important to note that the dispute resolution clause in a franchise agreement does not prevent a party from seeking injunctive relief from an appropriate court where failure to obtain such relief would cause irreparable damage to the party concerned or the franchise system.

Q8. What affect is the COVID-19 pandemic having on franchising opportunities?



Andrew Sherman

Sherman: The COVID-19 pandemic has affected franchising *both* positively and negatively and is likely to have a significant impact over the next 12-18 months.

On the positive side, certain franchise opportunities are thriving (as mentioned in answer 1 above), while many industries are suffering historic levels of pain in such areas as travel and tourism, business meetings and conventions, restaurant and bars, and most forms of specialty retail businesses.

Another example which seems to cut both ways is the record level of unemployment, which on one hand is significantly reducing consumer spending, but on the other hand, has now created a very large pool of highly qualified prospective franchisees, many of which have enough equity in their home and/or retirement savings to be able to afford the launch of a new business enterprise.

Finally, the commercial real estate market is another example of a double-edged sword in that, while many restaurant and retailers are struggling and could go out of business permanently, there will also be an opportunity for franchisors and their franchisees to take advantage of this trend in key venues and sites that would not have otherwise been available.



Juan Carlos Uribe

Uribe: It has been disastrous. Franchising as a commercial and social model has several economic and social effects, such as job creation, economic modernisation, and the development of entrepreneurship. The direct impacts on income, employment, and the achievement of social goals are most noticeable in emerging and developing markets as Colombia.

The negative effects of the pandemic in Colombia are worrying. One of the first consequences of the crisis has been the withdrawal of investment, since Colombia is considered as a country to be at greatest risk. In this context, Colombia is suffering from a drop in demand, the country is facing a massive decline in hospitality, restaurant and food service businesses.

As a second consequence, the social distancing measures are severely impacting the franchising, retail, and services sectors. Since the implementation of the COVID-19 emergency policies, approximately 90% of the franchising industry has not been operating in Colombia. Deliveries have become the primary source of income for the companies in Colombia.

In general, franchising opportunities were affected in a number of ways. Sales declined, supply chains were impacted as some products are sourced from countries that have closed their borders or that are among those most affected by the crisis.



Robert Toth

Toth: The whole Australian economy has been significantly affected and each State and Territory has had individual lockdown laws that have impacted on business. Many businesses are in hibernation with Landlords agreeing to provide rent relief to enable the franchisees to continue partial retail or online trade.

Many businesses have had to embrace going online within a matter of weeks rather than their plan to do so over the next 12 months. This has in fact been a positive as those businesses that were already online and offering click and collect and home delivery were ahead of their competition. Therefore, from such a negative there have been some positives and other business opportunities that have opened up in some sectors.

Q9. Can you outline the best practice for managing intellectual property issues in franchising?



Juan Carlos Uribe

Uribe: In a franchise agreement several intellectual property rights are exploited as trademarks, trade secrets, patents and copyrights. It is very important that necessary steps and measures are taken to better protect certain proprietary intangible rights from unauthorised uses and exploitation by franchisees. The franchisors have a general duty of brand reputation management of its franchise especially as it relates to the way the franchise business is run, the use of its trademark, inventions and confidential information, and the promotional materials utilised. Therefore, it is important that, within the user manual, the franchisor is clear about what he is delivering protected to the franchisee.

The following aspects are important steps to help avoid intellectual property issues in franchising:

Registration of primary and mains secondary trademarks as it prevents the unauthorised use of the trademark of the franchisor. However, apart from the registration of the franchisor's trademark in Colombia, there is a need for the franchisor to grant a right of use (the licence) to the franchisee to use its brand name and such licence must be recorded at the Colombian Trade Mark Registry to avoid objections by interested parties seeking a declaration of abandonment for non-use.

In the franchise agreement clearly define the franchisor's trade secret, require the franchisee to execute non-disclosure agreements with its employees who may become aware of the franchisors trade secret only on a need to know basis, prescribe confidentiality clauses that protect the trade secrets of the franchisor from unauthorised use both during the lifespan of the franchise agreement and post termination of the agreement.

It is pertinent for franchise agreements to contain clauses on the copyright ownership of creations of the franchisee or employers of the franchisee which were developed during the course of the franchise, including developments in other forms of intellectual property.



Robert Toth

Toth: Franchisors should ensure they do own or have evidence of their right to license their IP in granting master franchise or direct rights to franchisees. A thorough audit of their IP should be undertaken before they enter into another country and ensure their Trade Marks can be registered in Australia and that they will not be infringing any existing third parties' rights. Many overseas franchisors have been caught out by not registering their brand and having to rebrand from their recognised overseas brand due to an existing registered Trade Mark.



Dan Bjerg Geary

Geary: The licensing of IP as part of the franchise granted is not associated with any formalities or strict requirements. Nonetheless, a carefully drafted IP policy is important, both to managing the use of IP during the contract but also to prevent unauthorised use after. A point to be considered is whether a franchisee may at all register the franchisor's brand as part of the franchisee's corporate name, domain name, trademark, and social media profiles. A general prohibition of franchisee registration may save the franchisor from many complicated disputes post term.

In addition to the traditional type of intellectual property, franchisors have in recent years have increasingly become aware of the value consisting in trade secrets and know-how within the franchise concept. As a consequence many franchisors are more and more focused on protecting this and mitigate the risk of loss and misappropriation. This process is driven in part by a greater appreciation of know-how as an asset and in part by the EU trade secrets directive ("TSD") which was implemented in Danish law in June 2018. The legal position now requires the holder of a trade secret to demonstrate measures taken to curb trade secrets and prevent misappropriation.

Q10. How important is it for both the franchisor and franchisee to have an exit strategy?



Andrew Sherman

Sherman: In general terms, franchising is a long-term strategy and a highly interdependent relationship. Both franchisors and franchisees should assume that there is no easy exit strategy to the relationship once it has commenced. However, on the franchisor side, an increasing number of companies have been sold all or in part, to growing private equity firms in the United States, such as ROARK Capital, which now owns over 50-franchised systems.

At the franchisee level, an exit or succession plan has become critical as many franchisees who made their initial investment in the 1960s, 1970s and 1980s are ready for retirement and may now be facing health concerns. We are starting to see private equity play a role in the consolidation of franchise systems, driving operational efficiencies and financial returns. This trend has been expedited by the financial impact of COVID-19 and has caused many franchisees to turn to exit strategies earlier than they might have anticipated.



Juan Carlos Uribe

Uribe: We highly recommend that both parties have an exit strategy because as an investment, the franchisee one day would like to get out of the franchise. Considering the franchise is not an independent business that every franchisee can run any way he wants and that the franchisee does not own the trademark, the franchisor will have to approve and train whomever the franchisee wants to sell the franchise. Therefore, the best time to think about an exit strategy might be before the franchise is incorporated.



Stewart Germann

Germann: It is important to consider the ability to exit a franchise agreement before it is entered into. From the point of view of a franchisor, all franchise agreements – be they master franchise agreements or unit franchise agreements – must contain an assignment by franchisor clause. That clause will give the right to the franchisor at some future time to sell and exit the whole system without requiring the consent of either the master franchisee or the unit franchisee.

However, another aspect of exit for a franchisor's consideration is succession planning where the system is small and the franchisor may be a family-owned company. Over the years, I have found that this important aspect is often ignored. Whereas companies last forever, people do not so in a family-owned business the directors must have a succession plan in case death should suddenly intervene. For the franchise system to continue, someone will need to give support to the franchisee.

From a master franchisee or franchisee point of view, exit normally involves the right to assign or transfer the franchise to a third party in the future. Great care must be taken to check that the assignment clause in the agreement is appropriate and covers all aspects. A key consideration is always that the franchisor must provide its written consent to the proposed assignee or incoming franchisee of the franchise and the rationale is because the parties are in a relationship which requires consent.

The worst event for any franchisee is termination as that takes away the right of the franchisee to sell the business and recoup goodwill so although that will not be an exit strategy, it must be considered as a sudden death exit which either party will not want. In summary, exit strategies are often not considered and they should be.



Robert Toth

Toth: For a Franchisor there is usually a goal to be acquired down the track by a competitor or by a VC equity investor. The VC investor generally has an exit plan before they even acquire the business as they are seeking to maximise a return for their stakeholders.

Franchisees need to think about their exit strategy in the same way as they enter a franchise and seek expert advice on their exit costs if they sell the business. There is usually an assignment fee payable to the franchisor and they need to plan to exit while they still have some term left on their franchise agreement.



Adhuna Kamarul Ariffin

Ariffin: Given the symbiotic nature of the relationship between franchisor and franchisee, and the resulting goodwill that is liable to be generated, a well thought out exit strategy is essential. One of the safeguards built into the Franchise Act 1998 is the protection given to the franchisee where the franchise agreement is not renewed by the franchisor. The franchisee is then entitled to compensation, either through a repurchase or some other means at a price to be agreed between the parties. This will take into consideration the reduction in value of the franchised business caused by the expiration of the franchise.

Compensation is due when (A) the franchisee is stopped from conducting the same business under another mark in the same area, either (i) by the agreement, or (ii) by the franchisor's refusal to waive the non-competition provision of the agreement, at least six months before the expiration date of the agreement, or (B) the franchisor has not given the franchisee a written notice of the franchisor's intention not to renew at least six months before the expiration date of the agreement. Refusal to renew without compensation under those circumstances is an offence under the Act punishable with a fine on conviction.



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