

CORPO REVIEW #3

FRANCHISE

Draft amendments to the Civil Code –
introduction of the franchise agreement into
the statutory regulation

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PURPOSE OF THE REGULATION

Despite the significant and growing popularity of franchise networks in Poland, the franchise agreement has not been regulated in the Polish legal system so far. To a large extent, franchising has been used for the purpose of creating a network for distribution and sale of goods, and agreements concluded in this respect have been characterised by elements of a mandate or agency agreement as well as a licence agreement.

In the explanatory memorandum to the draft amendment, the project proponent points out that in Polish conditions the franchise agreement is the basis for conducting business in many industry sectors. According to various reports, the number of people involved in franchise networks in Poland exceeds half a million, and in 2020 there were more than 1,300 different franchise networks available.

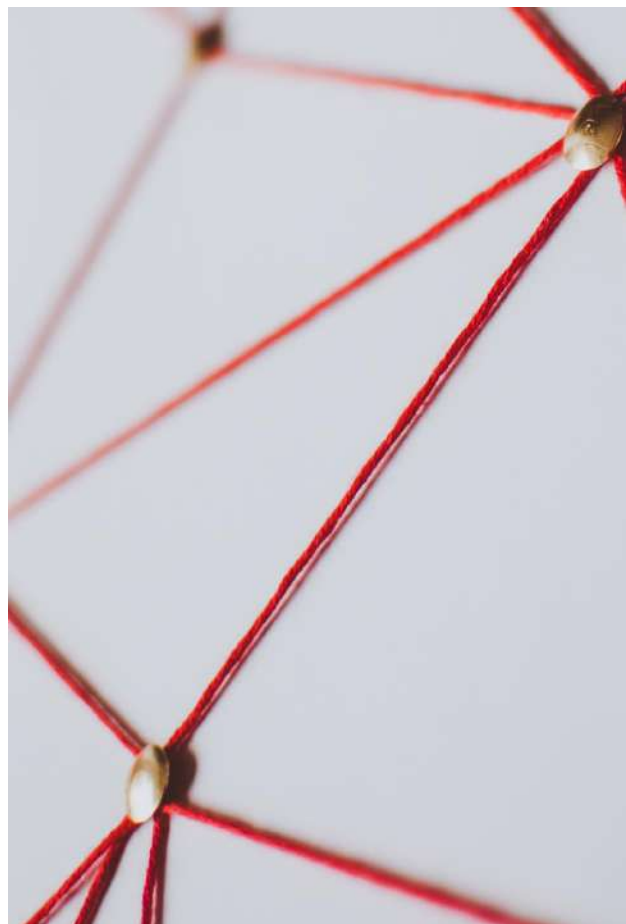
In the absence of statutory regulation, despite the theoretically equal contractual position of franchisee and franchisor, it is pointed out that the economic position of the franchisor and its capital advantage is incomparable to that of franchisees, who are most often micro and small entrepreneurs. Franchise agreements are practically agreements of accession (adhesion) and basically are not subject to any negotiation.

This has implications also in the legal sphere, for example in the event of litigation, the franchisee's position is less favourable than the position of the franchisor, which can lead to lengthy and complicated litigation involving significant legal costs.

The published reports referred to by the project proponent in the explanatory memorandum to the draft point to yet other problems arising from the lack of statutory regulation of the franchise relationship. For example, such issues may be pointed out:

- the problem of franchisors presenting unreliable information;
- imposing non-market purchase prices on the franchisor or its designees;
- imposing hidden fees by franchisors;
- difficulties in terminating franchise agreements, asymmetrical terms of termination.

Taking into account the problems and challenges indicated above, and given the ever-increasing popularity of franchise networks in the Polish market, a draft amending the Civil Code is currently being processed in Sejm (lower chamber of parliament), which is expected to lead to private law regulation of the franchise agreement, minimise the negative effects of the lack of such regulation in the future and ensure protection of franchisees..



PROPOSED AMENDMENTS - MAIN ASSUMPTIONS

In accordance with the latest draft of the act of November 28, 2023 (Council of Ministers draft number UD506), below we present the main principles of the proposed changes. However, we emphasise that they may still be modified in the course of parliamentary work. We will inform you of any changes on our [LinkedIn profile](#) - we encourage you to follow our posts.

Substance and form of the franchise agreement

A franchise agreement will be defined as an agreement concluded between two entities that are entrepreneurs within the meaning of the Civil Code - the franchisor, who undertakes to make a 'business concept or technique' available for use in return for payment, and the franchisee, who assumes the obligation to operate the business in its own name and on its own account in accordance with the concept made available, and to pay the agreed fee.

Conclusion of a franchise agreement must be done in writing otherwise being null and void.

Information document

No later than 14 days prior to the conclusion of the agreement, the franchisor will be obliged to provide the franchisee with an information document and a model franchise agreement. The information document should include:

- data identifying the franchisor,
- information on the mutual obligations of the parties,
- a description of the franchisor's activities, including in particular a listing of the business concept or technique made available for use and the activities to be carried out by the franchisee,
- information on the costs and expenditure to be borne by the franchisee,
- information on the means and extent of supervision by the franchisor of the performance of the franchise agreement,
- the duration of the franchise agreement and the time limits for its termination,
- rules and deadlines for non-competition obligations, etc.

Failure by the franchisor to provide an information document, or the inclusion of unreliable or untrue information in it, will allow the franchisee to terminate the agreement with immediate effect if there is a reasonable presumption that, had the franchisee been duly informed of them, the agreement would not have been concluded, and a period of thirty days has not elapsed since the franchisee became aware of this. This entitlement will expire six months after the conclusion of the agreement.

The franchisor will be obliged to submit the information document not only prior to the conclusion of the franchise agreement, but also prior to any amendment of the agreement.

Other mechanisms to protect the franchisee

The franchisee will have the possibility to terminate the agreement with immediate effect in the event that the franchisor blatantly violates material provisions of the agreement despite a prior written warning. The franchisee will also have the right to terminate the agreement immediately if the franchisee fails to provide the information document or provides false or unreliable information in it.

The franchisor's claim for payment of the contractual penalty will expire one year from the date on which the franchisor became aware, or by exercising due diligence could have become aware, of the non-performance or improper performance of an obligation under the franchise agreement by the franchisee, unless the franchisor has, within that period, called upon the franchisee to pay the contractual penalty.

With regard to the blank promissory note, the draft adopts the obligation to issue promissory notes without a 'not for order' or equivalent disclaimer. This basically comes down to establishing a prohibition on transferring the rights under the promissory note to third parties. If the franchisor, in order to fulfil or secure performance under the franchise agreement, accepted a blank promissory note that fails to meet the above requirement and assigned it to another person, the franchisor shall be obliged to compensate the issuer of the promissory note for the damage incurred by the indorser resulting from the franchisee's satisfaction of the indorser to the extent greater than if the franchisor had not indorsed the promissory note.

Prohibition of *subfranchising* and prohibition of in-kind contribution of franchises to a company

Unless otherwise agreed by the parties in the agreement, the franchisee may not transfer the rights under the franchise agreement to another person, nor may the franchisee contribute these rights to the company.

The proposed provision of Article 764¹⁴ of the Civil Code will apply in particular to cases of so-called *subfranchising* occurring in the trade, which consists in authorising a participant in the franchise network to conclude franchise agreements with third parties.

Franchisor's confidentiality protection

The franchisee is obliged to keep the know-how provided confidential without any limitation in time. However, it is possible and dependent on the will of the parties to regulate this issue differently in the agreement.

Time limits for termination of the franchise agreement

The franchisor will have the right to terminate an agreement concluded for an indefinite period six months in advance, and the parties have a contractual right to extend this period.

A franchise agreement concluded for an indefinite period will be terminable by the franchisee with three months' notice.

The cases, time limits and rules for termination by the franchisee of a fixed-term agreement will require appropriate contractual regulation.

Non-competition obligation

The proposed amendments provide for the possibility to contractually regulate a non-competition obligation following termination of the agreement. The non-competition obligation may consist only of an obligation on the franchisee not to create a competing franchise network for a maximum of one year from the date of termination of the agreement.

The term 'creation of a franchise network' should also be understood as its operation, i.e. the development of the network in terms of territory, volume, sector, product, service. In relation to the network, the term 'creation' also includes the meaning of managing and expanding.

Questions?

Contact us!



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The franchise agreement and antitrust law

Notwithstanding the above amendments, it should be noted that a franchise agreement is an agreement of entrepreneurs. Therefore, its provisions shall remain in compliance with the provisions on the prohibition of concluding competition restricting agreements.

A franchise agreement is a vertical agreement, i.e. concluded between entrepreneurs operating at two different levels of trade. The provisions of the franchise agreement should be in compliance with the provisions on vertical agreements, in particular the EU VBER Regulation and its Polish equivalent.

In particular, the franchisee and franchisor should avoid applying minimum and fixed sale prices. In the past, the President of the Office of Competition and Consumer Protection imposed a fine of almost half a million zlotys (PLN) on the organizer of the Sphinx franchise distribution system, i.e. Sfinks Polska S.A., for setting fixed sale prices for products offered in restaurants operating under the Sphinx brand (decision dated June 25, 2013, no. DOK-1/2013). This penalty was later reduced by the courts to the amount of PLN 50,000. What emerges from this case is the very restrictive position of the antitrust authority and the courts that even the desire to preserve the uniform image of a franchise chain does not justify completely free interference by the franchisor in the pricing policy of franchisees.

With the development of distribution systems, this approach has undergone some liberalization. The European Commission, in its guidelines to the VBER regulation, indicated that fixed sale prices may be necessary to organize a coordinated short-term low-price campaign (in most cases with a duration of 2 to 6 weeks), especially in a franchise system. The Commission indicated that such imposition of fixed sale prices could generally be considered as pro-competitive due to its temporary nature. However, each such situation should be evaluated on a case-by-case basis.

The proposed amendments will only cover franchise agreements concluded after the date of entry into force of the amendment. According to the draft presented to Sejm (lower chamber of parliament), the *vacatio legis* period will amount to 6 months from the date of announcement.