Hardwicke Building

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FRANCHISING TEAM NEWSLETTER

Welcome to the first edition of Hardwicke Building's franchising newsletter. We are publishing this newsletter to compliment our highly successful annual seminar day, now in its 3rd year, and to demonstrate chambers' continuing expertise in this specialist area of business. It is aimed at both lawyers and non-lawyers alike. We hope it gives you a useful update on what's been happening in the cases that have been in front of the courts in the past few months, as well as some food for thought about the ways they may affect a franchise business. We hope you enjoy it.

Nigel Jones QC, Head of Chambers

Recently Reported Cases

Peart Stevenson Associates Ltd. v Holland [2008] EWHC 1868 (QB)

Michelle Stevens-Hoare represented the defendant franchisee in this claim by a franchisor.

The franchisor commenced proceedings seeking damages for repudiatory breach of the franchise agreement and damages for breach of the post termination restrictions in the agreement.

The franchisor faced a counterclaim for damages on the basis that the franchisee entered the franchise agreement in reliance on the fraudulent or negligent misrepresentations of the franchisor.

The franchisor denied the allegations of misrepresentation and sought to rely on the non-reliance clause in its standard franchise agreement.

A number of points to note highlighted by the case and three in particular:

First, the ease with which a franchisor can ensure any breach entitles them to terminate and claim all losses that flow from the termination. An express provision that time is of essence in relation to payment results in the right to terminate and claim damages flowing from the termination no matter how small the sum defaulted on.

Second, the vulnerability of a franchisor to claiming damage suffered by reason of any breach of post-termination clauses if the franchisor does not maintain any business activity in the area or actively try to recruit a new franchisee for the area.

Third, the limited protection given to franchisors by their standard non reliance clauses on the basis that they:

(i) may effectively seek to circumvent the Misrepresentation Act 1967 and therefore amount to an exclusion clause subject to the reasonableness test; and/or,

(ii) can only operate as an evidential estoppel so requiring the franchisor to establish that the franchisee intended them to act on his agreement to the non-reliance clause and the franchisor reasonably believed that the franchisee was not in fact placing any reliance on any representations.

Michelle Stevens-Hoare

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Chipsaway International Ltd. v Errol Kerr (2009) CA (Civ Div) 11/3/09

In this very recent decision, the Court of Appeal allowed the franchisor's appeal against a decision ([2008] EWHC 1887 (Ch)) that its former franchisee had not breached post-termination restrictive covenants contained in the franchise agreement.

The Court has thus restored the law on the upholding of post-termination restrictive covenants in franchising to

what had generally been understood to be the position, at least before last year.

The case concerned a classic situation. The franchise agreement included a restrictive covenant that for a period of 12 months following the termination the agreement, the former franchisee would not, without the franchisor's prior consent, be engaged in any capacity in any business which competed with the business as carried on at the date of termination within the territory. The franchise agreement ended. Despite the restrictive covenant, as is not infrequently the case, the former franchisee carried on business at the same premises, including the provision of services essentially the same or very similar to those of the franchisor (although not using the franchisor's products or name).

Important points to emerge are as follows:

On the Judge's construction of the clause, the former franchisee was restrained from engaging in any business only when a new franchisee was in the territory. The Court held that this construction was wrong.

An issue that had troubled the Judge was that the franchisor had not actually been taking any steps itself to try and protect its franchise in the territory by actively trying to recruit a new franchisee. The Court concluded that the fact that the franchisor did not look for a new franchisee was irrelevant. The meaning of the covenant was not dependent on there being a new franchisee in the territory.

The Court re-stated the following principles:

- The purpose of the covenant was to allow the franchisor breathing space for 12 months to allow it to find a new franchisee, (although it did not have to look for one, nor did there have to be one in the territory for the covenant to operate).
- The covenant was also in place to protect goodwill.
- There was no commercial purpose in denying protection during the period it was really needed.
- During the franchise goodwill was built up and when the franchise came to an end, the franchisor's interest was vulnerable to the former franchisee.
- The commercial purpose of the restrictive covenant was to stop the former franchisee from carrying on business which would allow the franchisor time to find a new franchisee.

The Court did add that the Judge was right to recognise that (on a literal interpretation of the clause) the restrictive covenant made no sense.

The decision has, so far, only been reported briefly online. A full transcript of the judgment is awaited for the detail of the case.

Alexander Goold

Recently we have been...

Graham Cunningham has been involved in an interesting case involving an injunction concerning the world of filling inkjet and laser cartridges, a world far more complex than you might suppose. This was a case of a former franchisee who, in the usual way, decided that, after the agreement came to an end, he would turn the signage boards around, trade under another name and continue with the previous activity of filling cartridges on site and obtaining them already filled from third parties.

The lessons from this case are all about precision…

The former franchisee contended that he was entitled to stock and sell refilled cartridges obtained from third parties. The franchisor said he was not: their supply formed part of the franchise "system". On a strict interpretation of the definition of the original "system" this was not in fact correct.

However, the third party refilled cartridge was an improvement to the system. It allowed the former franchisee access to a wider range of cartridges supplied to the franchisor's standards as to the ink by specific suppliers. The franchisor relied on launch materials to support this contention, as well as the fact that this type of refilled cartridge had been part of the starter kit at the commencement of the franchise.

One might have expected an improvement to the system to result in an updated Manual but it was not. Sound practical advice might suggest that all such improvements should always be recorded in the Manual to avoid the possibility of such issues arising.

The former franchisee decided that discretion was the better part of valour. He accepted that he would not sell

internally refilled or externally procured and refilled cartridges for the length of the restrictive covenant.

Discussions outside court then led to a settlement agreement – or at least it was thought they had, until detailed discussions about the contents of the settlement took place. At that point misconceptions and issues came out that engendered a certain amount of distrust between the parties. A settlement document was finally drafted and agreed at 9.30pm, the Judge having been told the parties had settled at around 2.15pm!

The morals of this particular part of the story being, (i) it is as well to make sure that everyone understands every aspect of the proposed settlement before it is tendered; (ii) if it all falls apart because of misunderstanding, adopting a mediation approach to sorting things out is the best way to go.

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Graham and Mark Engelman have been locking horns again. The franchisor ran a chemicals business. The franchisee became disenchanted and left the network. The agreement had actually ended in January 2008, although both parties had continued to trade as if it continued in existence. Then, in June 2008, the franchisee's solicitors calmly announced that the franchisee had decided not to renew and had finished in business as of 31 May.

The evidence provide otherwise. The franchisee had divulged to another franchisee that they intended to compete and renewed the agreement on their van, which was specially equipped to carry chemicals. Evidence also came from one customer that the franchisee was selling in competition.

Arguments ranged from the invalidity of the covenants, to uncertainty of terms.

However, the franchisor was prepared to compromise on the length of the remaining covenants, so they had only six months to run instead of nine months. Certain other rights were also forgiven, e.g. a claim for damages in default of notice. In return, the franchisor did gain the undertakings as to compliance with the restrictive covenants. So, settlement can work if the franchisor is prepared to be flexible and not insist on everything.

Graham Cunningham

Upcoming Seminars

The Annual Hardwicke Building Franchising Seminar Day 2nd June 2009 10.00 am – 3.30 pm, 9.15am Registration

Dunkirk or D-Day? Franchising in an Economic Downturn

Topics to include:

- Issues relating to Franchisor insolvency and the dangers of post-insolvency fall-out for you and your businesses with **Sarah McCann** and **Edward Rowntree**, Hardwicke Building
- Practicalities and solutions for assisting and dealing with struggling Franchisees with **Barney Laurence**, Sherrards Solicitors
- Issues relating to property ownership: where the Franchisor leases premises to the Franchisee; where the Franchisee owns the premises with **Sara Benbow** and **John de Waal,** Hardwicke Building
- Structuring franchise agreements to best protect you as the Franchisor with **John Pratt,** Hamilton Pratt
- Testing the boundaries of the franchising agreement. What issues may arise when Franchisees look to test the boundaries of the franchise agreement or seek to avoid further obligations under it. What Franchisors can do to respond with **Michelle Stevens-Hoare**, Hardwicke Building and **Russell Ford**, Owen White Solicitors
- Practical opportunities for streamlining your franchise business with **Alexander Goold**, Harwicke Building
- Plenary session addressing threats and opportunities for franchise businesses during the credit crunch with **Nigel Jones QC, John Pratt**, Hamilton Pratt, **Russell Ford**, Owen White Solicitors, **Barney Laurence**, Sherrards and a panel from Hardwicke Building

Cost:

This year we are offering the reduced price of £35 excl. of VAT (£40.25) in recognition of these difficult financial times.

If you or your colleague(s) would like to attend or if you have any questions please contact Marketing Manager Louise Poppelwell on 0207 242 2523 or email louise.poppelwell@hardwicke.co.uk

Any interesting news?

If you have any suggestions or ideas for our coming editions please contact Louise Poppelwell, Marketing Manager at Hardwicke Building on louise.poppelwell@hardwicke.co.uk or phone Louise on 020 7242 2523.

This newsletter was edited by Alexander Goold. For further information on the Hardwicke Franchising Team and the services we offer, please visit our website at www.hardwickebuilding.co.uk

The members of Hardwicke's Franchising Team have specialised skills and experience in a wide range of franchising law. We represent both franchisors and individuals and groups of franchisees.

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Nigel Jones QC	1976 (1999)	Sara Benbow	1990
Graham Cunningham	1976	Alexander Goold	1994
Michelle Stevens-Hoare	1986	Ian Silcock	1997
Mark Engelman	1987	Sarah McCann	2001
Madeleine Heal	1990	Michael Wheater	2003

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