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## The New EEC Block Exemption Regulation on Franchising

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# The New EEC Block Exemption Regulation on Franchising

Jean-Eric de Cockborne

## **Abstract**

This article discusses regulation of franchising within the European Community and its effect on competition policy. In part I the author gives a general presentation of the regulation, in part II the author discusses the scope of the regulation, in Part III the author discusses the substantive provisions of the regulation, and in the Conclusion the author suggests potential solutions.

# THE NEW EEC BLOCK EXEMPTION REGULATION ON FRANCHISING†

*Jean-Eric de Cockborne\**

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### INTRODUCTION

For Europe, 1992 is slowly but surely becoming a year as important as 1492 is for America: five hundred years after Columbus discovered America, Europe should be discovered by the Europeans as constituting a single entity, a great unified market. This is the current priority for Community action, the aim towards which all Community policies are directed. Competition policy is essential in this context, because competition will allow the complete opening up of the markets, thus yielding all the expected positive economic effects. Competition policy must guarantee that the physical, technical, and tax barriers that will disappear are not replaced by segmented markets resulting from restrictive business practices. It must also foster market integration in a positive way, by encouraging cooperation among undertakings capable of improving production or distribution and by promoting technical or economic progress.

Distribution is an area of major importance for market integration. Exclusive distribution agreements, for instance, enable manufacturers to enter new geographical markets because of the experience of exclusive importers that are already established in those markets. They also facilitate the promotion of sales of their products while at the same time rationalizing distribution.

Franchising, another form of distribution, helps to integrate the Common Market by making it easier for relatively small firms to develop cross-frontier distribution networks. The Community takes a generally positive view towards franchise agreements, because they allow franchisors to establish their networks with only limited investments, which may

assist the entry of new competitors in the market and, therefore, increase interbrand competition. They also allow independent traders to set up outlets more rapidly and with a higher chance of success than if they had to do so independently. Finally, they are favorable for consumers, because they combine the advantages of a uniform distribution network with the existence of traders that are personally involved in the efficient operation of their businesses. The favorable effect of franchising on interbrand competition will normally guarantee that a reasonable part of the resulting benefits will be passed on to the consumers.

Although the Commission's first decision concerning franchising was adopted in December 1986, the interest of the Commission in that form of agreement is not new. More than ten years ago, the Commission started to study, from the point of view of competition law, the different aspects of franchising as a new means of cooperation between enterprises in the Community. In 1978, it took part in the drawing up by the European Franchising Association of a European code of ethics for franchising.<sup>1</sup> In 1983, a seminar was organized jointly by the EEC Commission and the French authorities to examine the problems of franchising in relation to competition law.<sup>2</sup>

Several commentators<sup>3</sup> suggested that franchise agreements either did not fall under Article 85 or could benefit from the provisions of the block exemption regulation for exclusive dealing agreements.<sup>4</sup> However, the treatment of franchise agreements under EEC competition rules remained unclear.

In January 1986, the Court of Justice, in the *Pronuptia* case,

1. COMM'N OF THE EUROPEAN COMMUNITIES, EUROPEAN CODE OF ETHICS FOR FRANCHISING (1981).

2. See Schlieder, *Le Franchisage et le Droit de la Concurrence*, REVUE DE LA CONCURRENCE ET DE LA CONSOMMATION 43 (Supp. to No. 25, 1984).

3. See, e.g., Adams, *Franchising and Antitrust in the United Kingdom and European Community*, 26 ANTITRUST BULL. 815 (1981); Goebel, *The Uneasy Fate of Franchising Under EEC Antitrust Laws*, 10 EUR. L. REV. 87 (1985); Neumann, *Franchise-Verträge und EG-Kartellrecht*, 31 RECHT DER INTERNATIONALEN WIRTSCHAFT 612 (1985).

4. Comm'n Regulation No. 67/67, 10 J.O. L 67/849 (1967), O.J. Eng. Spec. Ed. 1967, at 10, Common Mkt. Rep. (CCH) ¶ 2727 [hereinafter Regulation 67/67] (on exclusive dealing agreements), replaced by Comm'n Regulation No. 1983/83, O.J. L 173/1 (1983), Common Mkt. Rep. (CCH) ¶ 2730 [hereinafter Regulation 1983/83] (on exclusive distribution agreements), and Comm'n Regulation No. 1984/83, O.J. L 173/5 (1983), Common Mkt. Rep. (CCH) ¶ 2733 [hereinafter Regulation 1984/83] (on exclusive purchasing agreements).

adopted its first position about franchising.<sup>5</sup> There, the Court considered that a distribution franchise agreement does not, in itself, interfere with competition.<sup>6</sup> It considered, in particular, that a non-competition obligation on the franchisees did not fall under Article 85(1), because it was indispensable for the proper functioning of a franchising system.

The *Pronuptia* judgment has been welcomed by many commentators as "finally" establishing the principle that vertical restrictions should be submitted to a rule-of-reason approach under Article 85(1).<sup>7</sup> Should this judgment, therefore, be hailed as the "European *Sylvania*"?<sup>8</sup> It is indeed a milestone for the application of Community competition rules to vertical restrictions; however, for the following reasons its scope should not be unduly widened.

First, *Pronuptia* does not involve a rule-of-reason analysis, as the Court of Justice did not refer to any market-power considerations.<sup>9</sup> Rather, it only considered that provisions that are essential for avoiding the possibility of the franchisor's know-how and assistance from benefiting its competitors do not constitute restrictions of competition for the purposes of

5. *Pronuptia*, Case 161/84, 1986 E.C.R. 353, Common Mkt. Rep. (CCH) ¶ 14,245.

6. *Id.* at 381, ¶ 15, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438.

7. See, e.g., Galan Corona, *Los Contratos de "Franchising" ante el Derecho Comunitario Protector de la Libre Competencia*, 13 REVISTA DE INSTITUCIONES EUROPEAS 687, 692 (1986); Goebel, *Pronuptia de Paris GmbH v. Pronuptia de Paris Irmgard Schillgalis*, 23 COMMON MKT. L. REV. 683 (1986) (case comment); Korah, *Pronuptia Franchising: The Marriage of Reason and the EEC Competition Rules*, 8 EUR. INTELL. PROP. REV. 99 (1986); Venit, *Pronuptia: Ancillary Restraints—or Unholy Alliances*, 11 EUROPEAN L. REV. 213 (1986); see also Waelbroeck, *The Pronuptia Judgment—a Critical Appraisal*, in 1986 FORDHAM CORP. L. INST. 211, 211 (B. Hawk ed. 1987) ("[T]he approach [the Court] adopted was largely based on the rule of reason. Unfortunately, however, the Court failed to carry its reasoning to its logical conclusion."). But see 2 B. Hawk, UNITED STATES, COMMON MARKET AND INTERNATIONAL ANTITRUST 426.3 (2d ed. 1987) ("analysis should not be confused with a U.S. rule of reason analysis").

8. The U.S. Supreme Court decision in *Continental T.V. v. GTE Sylvania*, 433 U.S. 36 (1977), established a rule-of-reason approach for non-price vertical restrictions, thereby reversing *United States v. Schwinn*, 388 U.S. 365 (1967), which had established that territorial, customer, and price restrictions imposed on dealers were *per se* infringements of the antitrust rules. *Id.* at 375-76; see 2 B. HAWK, UNITED STATES, COMMON MARKET AND INTERNATIONAL ANTITRUST 306 (2d ed. 1987).

9. Advocate General P. VerLoren van Themaat referred to *Sylvania* in his conclusions in the *Pronuptia* case to consider that the Court's assessment should be based on an examination of the market situation and in particular of interbrand competition. *Pronuptia*, 1986 E.C.R. at 361, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,446-47.

Article 85(1).<sup>10</sup> The same consideration was made for the measures that were necessary for maintaining the common identity and reputation of the franchised network.<sup>11</sup>

Second, *Pronuptia* does not constitute the major shift in Community case law that *Sylvania* did in the United States, because it applies the notion of ancillary restraints, which was already known and applied in Community law, in particular, for the sale of a business,<sup>12</sup> selective distribution,<sup>13</sup> and licenses of industrial property rights.<sup>14</sup>

Finally, care should be taken in extending the principles expressed in the *Pronuptia* judgment to other distribution agreements, because the Court of Justice stressed the importance of industrial property rights involved in franchising.<sup>15</sup>

The significance of the *Pronuptia* judgment lies in the fact that it applies the notion of ancillary restraint in a more extensive way than had been done before,<sup>16</sup> by combining principles developed in the fields of distribution and licenses of industrial property rights. In addition, it confirms the strict position taken from the start by the Commission and the Court of Jus-

10. Treaty Establishing the European Economic Community, Mar. 25, 1957, art. 85(1), 1973 Gr. Brit. T.S. No. 1 (Cmd. 5179-II) at 32 (official English version), 298 U.N.T.S. 11, 47-48 (1958) (unofficial English trans.) [hereinafter EEC Treaty].

11. *Pronuptia*, 1986 E.C.R. at 381-82, ¶¶ 16-17, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438-39.

12. The Court considers that a non-competition clause in an agreement for the sale of a business does not fall under Article 85(1) if it is necessary to the transfer of the enterprise concerned and its duration and scope are strictly limited to that purpose. *Remia v. Commission*, Case 42/84, 1985 E.C.R. 2545, 2571, ¶ 20, Common Mkt. Rep. (CCH) ¶ 14,217, at 16,301.

13. See, e.g., *Metro v. Commission*, Case 26/76, 1977 E.C.R. 1875, Common Mkt. Rep. (CCH) ¶ 8435; *Villeroy & Boch*, O.J. L 367/17 (1985), Common Mkt. Rep. (CCH) ¶ 10,758.

14. About the admissible territorial protection of the licensee, see *Erauw Jacquery v. La Hesbignonne*, Case 27/87, 1988 E.C.R. — (LEXIS, Eurcom library, Cases file); *Coditel v. Ciné-Vog Films (Coditel II)*, Case 262/81, 1982 E.C.R. 3381, Common Mkt. Rep. (CCH) ¶ 8865; *Nungesser v. Commission (Maize seed)*, Case 258/78, 1982 E.C.R. 2015, Common Mkt. Rep. (CCH) ¶ 8805.

15. See *Pronuptia*, 1986 E.C.R. at 381-82, ¶ 16, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438-39.

16. See Green, *Article 85 in Perspective: Stretching Jurisdiction, Narrowing the Concept of a Restriction and Plugging a Few Gaps*, 9 EUR. COMPETITION L. REV. 190 (1988). Green notes that the test used in *Remia* was stricter than in *Pronuptia*, because in the former case the Court examined whether the agreement as a whole was pro-competitive, whereas in the latter it was considered sufficient to observe that the agreement did not interfere with competition. In other words, it did not have either positive or negative effects on competition. *Id.* at 196-97.

tice towards certain basic principles of Community competition law, such as market partitioning and resale price maintenance. The consequence is that franchise agreements that appreciably affect intra-community trade are considered restrictive if they include, in particular, territorial protection for the franchisees.<sup>17</sup>

The Court of Justice found, furthermore, that franchise agreements falling under the prohibition of the Community competition rules could not benefit from any existing block exemption regulations.<sup>18</sup> In view of the considerable development of franchise agreements in the Community, where they now represent approximately ten percent of all retail sales,<sup>19</sup> the Commission considered it necessary to give priority to the examination of notified cases concerning franchising in order to acquire the necessary experience for the preparation of a block exemption regulation for franchise agreements.<sup>20</sup> A draft version of this regulation (the "Draft Regulation") was published in August 1987 in order to obtain the observations of interested parties.<sup>21</sup> More than forty responses were received by the Commission. After the required consultations of the Advisory Committee on Restrictive Practices and Monopolies, consisting of Member State experts, Commission Regulation No. 4087/88 (the "Regulation" or the "Franchising Regulation")<sup>22</sup> was adopted by the Commission on November 30,

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17. Except if the agreements are *de minimis*. See in that respect the Commission's Notice of 3 September 1986 on Agreements of Minor Importance, O.J. C 231/2 (1986), Common Mkt. Rep. (CCH) ¶ 2700 [hereinafter *De Minimis* Notice], which specifies that agreements are normally considered as not falling under Article 85(1) if the market share of the participating enterprises is not superior to five percent and their aggregate turnover (worldwide) does not exceed 200 million ECU. *Id.* at 2-3, ¶ 7, Common Mkt. Rep. (CCH) ¶ 2700, at 1853-3. The notice specifies that it does not apply where in a relevant market competition is restricted by the cumulative effect of parallel networks of similar agreements. *Id.* at 4, ¶ 16, Common Mkt. Rep. (CCH) ¶ 2700, at 1854.

18. *Pronuptia*, 1986 E.C.R. at 386-87, ¶ 32, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,441.

19. See Sutherland, *Franchise Agreements Under EEC Competition Rules*, Common Mkt. Rep. (CCH) ¶ 10,776, at 11,806 (address to Euro Conferences, Brussels, Mar. 25, 1986).

20. *Id.* at 11,808.

21. Draft Commission Regulation (EEC) on the Application of Article 85(3) of the Treaty to Categories of Franchise Agreements, O.J. C 229/3 (1987) [hereinafter *Draft Regulation*].

22. Comm'n Regulation No. 4087/88, On the Application of Article 85(3) of the

1988.

### I. GENERAL PRESENTATION OF THE REGULATION

The object of the Regulation is not to cover all aspects of franchising but only to specify which restrictions included in franchise agreements are compatible with EEC competition rules. The Regulation does not intend to give a general definition of "franchise agreement," but delimits a category of agreements that fall under Article 85(1) and normally fulfill the conditions for an exemption set out in Article 85(3).<sup>23</sup> First, it should be remembered that not all franchise agreements fall under Article 85(1); they only do so if they appreciably restrict competition within the Common Market and affect trade between Member States.<sup>24</sup> Second, agreements falling under 85(1) and not covered by the Franchising Regulation may still benefit from an individual exemption.<sup>25</sup>

#### A. Legal Basis

According to Article 87 of the Treaty, the Council is the competent authority to adopt regulations implementing the principles of Articles 85 and 86. Under the authority of this Article, the Council adopted Regulation 19/65,<sup>26</sup> which empowers the Commission to apply Article 85(3) to certain categories of exclusive agreements between two undertakings that fall within the scope of 85(1), when the agreement either has as its object the exclusive distribution or purchase of goods or includes restrictions imposed in relation to the assignment or use of industrial property rights.

Following the judgment of the Court in *Pronuptia*, the Commission believed that it was possible to define a category of agreements that could be deemed generally to meet the

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Treaty to Categories of Franchise Agreements, O.J. L 359/46 (1988) [hereinafter Franchising Regulation], reprinted in the appendix to this Article, *infra* pp. 297-310.

23. *Id.* recital 4, at 46, reprinted *infra* p. 298.

24. See EEC Treaty, *supra* note 10, art. 85(1), Gr. Brit. T.S. No. 1, at 32, 298 U.N.T.S. at 47-48; see Skaupy, *Pronuptia und die Folgen*, 36 WIRTSCHAFT UND WETTBEWERB [WuW] 445, 453 (1986).

25. See EEC Treaty, *supra* note 10, art. 85(3), Gr. Brit. T.S. No. 1, at 32-33, 298 U.N.T.S. at 48.

26. Council Regulation No. 19/65, 8 J.O. 533 (1965), O.J. Eng. Spec. Ed. 1965-66, at 35, Common Mkt. Rep. (CCH) ¶ 2717 [hereinafter Regulation 19/65].

conditions set up in Article 85(3) and, thus, benefit from an exemption from Article 85(1). The Commission considered that, essentially, such agreements could be defined as agreements on the exploitation of industrial or intellectual property rights, such as trademarks, trade names, and know-how, for the purpose of selling goods or providing services in premises of uniform appearance and with the same business methods. Franchise agreements, therefore, correspond to the second category of agreements envisaged by Regulation 19/65.<sup>27</sup> Where franchise agreements also include restrictions relating to the purchase or supply of certain goods, they also fall under the first category.<sup>28</sup> The question has been raised whether the arguments given by the Court of Justice in the *Pronuptia* case for rejecting the application of Regulation 67/67<sup>29</sup> to franchise agreements<sup>30</sup> should not apply equally to the competence of the Commission to adopt a block exemption regulation for franchise agreements on the basis of Regulation 19/65.<sup>31</sup> However, the four arguments given by the Court of Justice to refuse the application of Regulation 67/67 are based on the fact that this regulation refers only to exclusive distributorships,<sup>32</sup> while Regulation 19/65 also refers to restrictions im-

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27. See *id.* art. 1(1)(b), at 543, O.J. Eng. Spec. Ed. 1965-66, at 36, Common Mkt. Rep. (CCH) ¶ 2718, at 1872.

28. See *id.* art. 1(1)(a), at 543, O.J. Eng. Spec. Ed. 1965-66, at 36, Common Mkt. Rep. (CCH) ¶ 2718, at 1872.

29. See *supra* note 4.

30. See *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 387, ¶¶ 33-34, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,441.

31. See, Korah, *Franchising and the Draft Group Exemption*, 8 EUR. COMPETITION L. REV. 124, 127 (1987); see also Mendelsohn, *Consideration for a Block Exemption Regulation*, J. INT'L FRANCHISING & DISTRIBUTION L., Sept. 1986, at 9. Mendelsohn was of the opinion that the Commission did not have the power to adopt a block exemption under Regulation 19/65 for service franchise agreements. *Id.*

32. See *Pronuptia*, 1986 E.C.R. at 387, ¶ 33, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,441. The four arguments are as follows: (i) contracts benefiting from the exemption are defined by reference to exclusive supply and/or purchase and not by the characteristics of distribution franchising contracts, which include use of the same sign, the application of uniform commercial methods, and the payment of royalties; (ii) article 2 expressly applies to only agreements regarding exclusive dealing agreements, which are different in nature from distribution franchising contracts; (iii) the same article lists only restrictions and obligations that can be imposed on the distributor, without mentioning those that can be imposed on the other party to the contract, while in the case of distribution franchising the obligations assumed by the franchisor have a very special importance; and (iv) in article 2(2), the list of obligations that may be imposed on an exclusive distributor does not include the obligation

posed in relation to the assignment or use of industrial property rights.<sup>33</sup>

Regulation 19/65 provides that the Commission may adopt a block exemption regulation only when it has sufficient knowledge of the kinds of agreements in question.<sup>34</sup> Before drafting the Franchising Regulation, the Commission, therefore, gained experience in the field of franchising by examining a large number of contracts and adopting five decisions concerning franchising systems: *Pronuptia*,<sup>35</sup> *Yves Rocher*,<sup>36</sup> *Computerland*,<sup>37</sup> *ServiceMaster*,<sup>38</sup> and *Charles Jourdan*.<sup>39</sup> The amount of experience necessary before the Commission adopts a block exemption regulation based on Regulation 19/65 has varied; before the adoption of Regulation 67/67, several decisions concerning exclusive distribution had been

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to pay royalties or the obligations that are needed to preserve the identity and reputation of the network. *Id.*

It should be stressed that these arguments seem to be far from convincing, as article 2 of Regulation No. 67/67 specifically considers as non-restrictive obligations such as selling the contract goods under trademarks or packed and presented under the manufacturer's specifications, providing after-sale and guaranteed services, or employing staff having specialized or technical training. Regulation 67/67, *supra* note 4, art. 2(2), at 851, O.J. Eng. Spec. Ed. 1967, at 10, 11-12, Common Mkt. Rep. (CCH) ¶ 2727, at 1883. The same provisions exist in Regulation 1983/83, *supra* note 4, art. 2, at 2-3, Common Mkt. Rep. (CCH) ¶ 2730, at 1893. Furthermore, according to the Court of Justice, the obligations that would not be covered by Regulation 67/67 are considered by the same Court not to fall under Article 85(1). This point has been made by most commentators of the *Pronuptia* judgment. See, e.g., Demaret, *L'Arrêt Pronuptia et les Contrats de Franchise en Droit Européen de la Concurrence: Innovation et Tradition*, 48 LA SEMAINE JURIDIQUE 729, 737-38 (1986); Korah, *supra* note 7; Skaupy, *supra* note 24, at 445; Venit, *supra* note 7; Waelbroeck, *supra* note 7. *But see* Clement & Boutard-Labarde, *La Franchise et le Droit Européen de la Concurrence*, GAZETTE DU PALAIS, Apr. 6-8, 1986, at 11, 11-12 (finding the arguments of the Court of Justice satisfactory).

33. The Franchising Regulation refers to industrial or intellectual property rights to take into account the different terminology used in the various Member States. The concept of intellectual property rights is understood in most Member States as a wide notion including, in particular, trademarks, patents, know-how, signs, and copyrights; but in Spain and Portugal it does not include trademarks and patents.

34. Regulation 19/65, *supra* note 26, fourth whereas clause, at 533, O.J. Eng. Spec. Ed. 1965-66, at 35, Common Mkt. Rep. (CCH) ¶ 2717, at 1871.

35. *Pronuptia*, O.J. L 13/39 (1987), Common Mkt. Rep. (CCH) ¶ 10,854 (examining different agreements than those examined by the Court of Justice).

36. *Yves Rocher*, O.J. L 8/49 (1987), Common Mkt. Rep. (CCH) ¶ 10,855.

37. *Computerland*, O.J. L 222/12 (1987), Common Mkt. Rep. (CCH) ¶ 10,906.

38. *ServiceMaster*, O.J. L 332/38 (1988), Common Mkt. Rep. (CCH) ¶ 11,047.

39. *Charles Jourdan*, O.J. L 35/31 (1989).

made,<sup>40</sup> while only one decision<sup>41</sup> preceded Regulation 123/85.<sup>42</sup>

Regulation 19/65 involves another limitation, as it specifies that block exemptions adopted on its basis can only cover agreements between two undertakings.<sup>43</sup> However, agreements between several companies, in the case of a master franchise in particular, can be covered if they can be analyzed as a bundle of bilateral sets of obligations.

### B. *The Structure of the Regulation*

Article 1 of the Franchising Regulation includes the principle of the exemption and a set of definitions of terms that are used in the Regulation.<sup>44</sup> Article 2 states which restrictions are exempted.<sup>45</sup> Article 3 lists some obligations, normally not restrictive of competition, that may be included in an agreement, insofar as they are necessary to protect the franchisor's industrial or intellectual property rights; it also lists other obligations, normally not restrictive of competition, without qualification and specifies that should these obligations become restrictive of competition because of specific circumstances, they will also be covered by the exemption.<sup>46</sup> Article 4 stipulates which conditions must be fulfilled for the exemption to apply.<sup>47</sup> Article 5 is the "black list" of restrictions that prevent the application of the exemption.<sup>48</sup>

Article 6 provides for an "opposition procedure" pursuant to which the exemption may be extended to agreements that include obligations that are restrictive of competition and are not expressly allowed or excluded by the Regulation. The

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40. See, e.g., Junghans, O.J. L 30/10 (1977), Common Mkt. Rep. (CCH) ¶ 9912; Goodyear Italiana-Euram, O.J. L 38/10 (1975), Common Mkt. Rep. (CCH) ¶ 9708.

41. Bayerische Motoren Werke AG, O.J. L 29/1 (1975), Common Mkt. Rep. (CCH) ¶ 9701 [hereinafter Bayerische Motoren Werke].

42. Comm'n Regulation No. 123/85, on Motor Vehicle Distribution and Servicing Agreements, O.J. L 15/16 (1985), Common Mkt. Rep. (CCH) ¶ 2751 [hereinafter Regulation 123/85].

43. Regulation 19/65, *supra* note 26, art. 1(1), at 534, O.J. Eng. Spec. Ed. 1965-66, at 36, Common Mkt. Rep. (CCH) ¶ 2717, at 1872.

44. Franchising Regulation, *supra* note 22, art. 1, at 48-49, *reprinted infra* pp. 302-03.

45. *Id.* art. 2, at 49, *reprinted infra* p. 304.

46. *Id.* art. 3, at 49-50, *reprinted infra* pp. 304-06.

47. *Id.* art. 4, at 50, *reprinted infra* pp. 306-07.

48. *Id.* art. 5, at 50, *reprinted infra* pp. 307-08.

Commission must be notified of these agreements and express reference must be made to the opposition procedure concerned. If the Commission does not oppose such exemption within a period of six months, then the exemption is extended.<sup>49</sup> The presence of an opposition procedure gives more flexibility for the application of the Regulation.<sup>50</sup> It gives the Commission the possibility of examining whether certain obligations or combinations of obligations that may have been unknown to it when drafting the Regulation can nevertheless benefit from the block exemption. In addition, it gives companies legal security by allowing them to know within a short period of time whether or not their agreements are susceptible to problems being raised in relation to the Community competition rules.<sup>51</sup> Article 7 guarantees that information provided in notifications can be used only for the purposes of the Regulation,<sup>52</sup> in other words, for the application of Community competition rules to franchise agreements. This article, which exists in all block exemption regulations incorporating an opposition procedure, repeats the provisions on professional secrecy that appear in article 20 of Regulation 17.<sup>53</sup> This provision is necessary, because the legal basis for a notification referring to an opposition procedure is to be found in the relevant article of the block exemption regulation involved, here article 6, and not in Regulation 17.

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49. *Id.* art. 6, at 50-51, *reprinted infra* pp. 308-09.

50. See P. Sutherland, *Franchising: The European Community Context* 12 (address to the Twenty-Seventh Annual Convention of the International Franchise Association, Jan. 27, 1987) (available at the *Fordham International Law Journal* office); see also Comm'n, *Thirteenth Report on Competition Policy* ¶ 73 (1984). It should be noted that all block exemption regulations adopted since 1984 include an opposition procedure, with the only exception being Regulation 123/85, *supra* note 42.

51. For arguments in favor of the opposition procedure, see Vogelaar, *The Overall Policy of the Commission Concerning Distribution in the Light of Recent Developments: Some Capita Selecta*, in 1986 FORDHAM CORP. L. INST. 185, 192 (B. Hawk ed. 1987). Vogelaar deplores the lack of an opposition procedure in Regulations 1983/83 and 1984/83. On the effects of the opposition procedure, see, in particular, Siragusa, *Notifications of Agreements in the EEC—to Notify or not to Notify*, in 1986 FORDHAM CORP. L. INST. 243, 263 (B. Hawk ed. 1987); Venit, *The Commission's Opposition Procedure—Between the Scylla of Ultra Vires and the Charybdis of Perfume: Legal Consequences and Tactical Considerations*, 22 COMMON MKT. L. REV. 167 (1985).

52. See *Franchising Regulation*, *supra* note 22, art. 7, at 51, *reprinted infra* p. 309.

53. Commission Regulation 17 is the first regulation implementing Articles 85 and 86 of the Treaty. See Comm'n Regulation No. 17, art. 20, 5 J.O. 204, 211 (1962), O.J. Eng. Spec. Ed. 1959-62, at 87, 93, *Common Mkt. Rep. (CCH)* ¶ 2591, at 1794-95.

Article 8, in conformity with article 7 of Regulation 19/65,<sup>54</sup> recalls that the Commission may withdraw the benefit of the block exemption if it considers that an agreement covered by the Regulation nevertheless has certain effects incompatible with the conditions laid down in Article 85(3). It also provides a non-exhaustive list containing examples of situations that, on the basis of the Commission's experience, might lead to a withdrawal of the exemption.<sup>55</sup> The Commission makes an individual decision as to whether or not the exemption is withdrawn, by following proceedings under Regulation 17 and after giving the parties concerned an opportunity to make their views known. Such a decision cannot have a retroactive effect. It may be coupled with an individual exemption subject to conditions or obligations or subject to the finding of an infringement and an order to bring it to an end. The Commission has never adopted such a decision until now.<sup>56</sup>

Article 9 provides that the Regulation shall enter into force on February 1, 1989, and remain in force until December 31, 1999.<sup>57</sup> The obligation to fix a limit for the application of the block exemption is established in article 2(1) of Regulation 19/65.<sup>58</sup> It makes it possible for the Commission to revise the Regulation, if necessary, in light of the experience gained during its application. The duration of the block exemption is not intended to have an influence on the duration of the agreements involved, as block exemption regulations are normally renewed without or with only limited modifications.<sup>59</sup>

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54. See Regulation 19/65, *supra* note 26, art. 7, at 535, O.J. Eng. Spec. Ed. 1965-66, at 37, Common Mkt. Rep. (CCH) ¶ 2717, at 1874.

55. See Franchising Regulation, *supra* note 22, art. 8, at 51, *reprinted infra* pp. 309-10.

56. However, companies have in certain cases modified their agreements to avoid a withdrawal of the exemption. See Tetra Pak I, O.J. L 272/27, at 41-42, ¶ 53 (1988), Common Mkt. Rep. (CCH) ¶ 11,015, at 12,431-16, where the Commission indicated that it intended to withdraw the benefit of the exemption given to an exclusive patent license by Regulation 2349/84 on Patent Licensing, O.J. L 219/15 (1984), Common Mkt. Rep. (CCH) ¶ 2747 [hereinafter Regulation 2349/84]. The license did not include any restriction not covered by the Regulation, but the acquisition of the license was considered to constitute an abuse of a dominant position because of the structure of the market. The Commission did not need to withdraw formally the exemption, because the license was transformed into a non-exclusive license.

57. Franchising Regulation, *supra* note 22, art. 9, at 51, *reprinted infra* p. 310.

58. Regulation 19/65, *supra* note 26, art. 2(1), at 534, O.J. Eng. Spec. Ed. 1965-66, at 36, Common Mkt. Rep. (CCH) ¶ 2717, at 1872.

59. See Clough, *Franchising in Europe Since the Pronuptia Case*, 9 EUR. INTELL. PROP.

## II. SCOPE OF THE REGULATION

### A. *The Notion of Franchise Agreement*

The notion of franchise agreement varies considerably in Europe from one country to another. In none of the Member States of the European Community is there a legally binding definition of "franchise agreement," as no specific national legislation relating to franchising has been adopted until now. The only tentative definition can be found in codes of ethics adopted by franchisor associations,<sup>60</sup> non-compulsory standards,<sup>61</sup> or in the case law of national courts<sup>62</sup> or the Court of Justice of the European Communities.<sup>63</sup> Although all these definitions are different, the existence of certain common principles makes it possible to define a "European" notion of franchising. It can be defined briefly as a method of cooperation between independent companies based on the use of a common name and the exploitation of specific knowledge.

This concept is, therefore, narrower than the general notion of franchising in the United States, which includes, for example, automobile dealerships.<sup>64</sup> Under Community law, such

REV. 317, 318 (1987); *see, e.g.*, Comm'n Regulation No. 2779/72, 15 J.O. L 292/23 (1972), O.J. Eng. Spec. Ed. 1972 (28-30 Dec.), at 80, exempting specialization agreements, initially applicable until 1977, *extended* by Comm'n Regulation Nos. 2903/77, O.J. L 338/14 (1977) and 3604/82, O.J. L 376/33 (1982), *replaced* by Comm'n Regulation No. 417/85, O.J. L 53/1 (1985), Common Mkt. Rep. (CCH) ¶ 2743, which is applicable until December 31, 1997.

60. *See, in particular*, the definition adopted by the European Franchising Federation ("EFF") in 1980, quoted by Dubois, *Franchising Under EEC Competition Law: Implications of the Pronuptia Judgment and the Proposed Block Exemption*, in 1986 *FORDHAM CORP. L. INST.* 115, 116 (B. Hawk ed. 1987). It should be noted that most of the national franchising associations comprising the EFF have adopted their own definitions.

61. *See, e.g.*, L'ASSOCIATION FRANÇAISE DE NORMALISATION, *NORME FRANÇAISE: FRANCHISE, RELATIONS CONTRACTUELLES* (1987) (norms laying down minimum rules relating to negotiation and contents of franchise agreements).

62. *See, e.g.*, the definition given in Germany by the Bundesarbeitsgericht in its judgment of May 30, 1978, *ARBEITSRECHTLICHE PRAXIS* [AP] No. 9, § 60 HGB, at 265-66, *quoted in* Schaub, *Franchising und EG-Kartellrecht*, 37 *WuW* 607, 607 (1987).

63. *See* the definition of distribution franchise in *Pronuptia*, Case 161/84, 1986 *E.C.R.* 353, 381, ¶ 15, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438.

64. For a comparison of the European and U.S. concepts of franchising, *see* Dubois, *supra* note 60, at 117-18. Dubois makes a distinction between the first generation of franchising, including for instance truck dealers and gas service station, and the second generation concerning business format franchising. He considers, in agreement with Duncan Whitfield, President of the EFF, that the European notion of franchising "emphasises the existence of a partnership between the franchisor and

agreements would be considered as selective distribution while franchising would be limited to the U.S. notion of business format franchising.<sup>65</sup>

The Regulation is not intended to give a general definition of all possible kinds of franchise agreements, instead it attempts to determine a category that is sufficiently homogeneous to make it possible to assume that agreements corresponding to that definition, and fulfilling the other conditions set out in the Regulation, will normally meet the conditions of application of Article 85(3).

The Regulation defines "franchise" as a "package of industrial or intellectual property rights relating to trade marks, trade names, shop signs, utility models, designs, copyrights, know-how or patents, to be exploited for the resale of goods or the provision of services to end users."<sup>66</sup> It specifies that to be covered by the Regulation, a franchise agreement shall include, at least, the following obligations: (i) "the use of a common name or shop sign and a uniform presentation of contract premises and/or means of transport";<sup>67</sup> (ii) "the communication by the franchisor to the franchisee of know-how";<sup>68</sup> and (iii) "the continuing provision by the franchisor to the franchisee of commercial or technical assistance during the life of the agreement."<sup>69</sup> It is important to stress that all three elements must be present; the exemption would not apply, for example, in the case of a franchise based only on the use of a common name, without communication of know-how.<sup>70</sup>

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each of the franchisees," while the U.S. definition "insists on the franchisor's obligation to be the boss in the shop." *Id.*

65. For a discussion of U.S. business format franchising, see Strasser, *Big Macs and Radio Shacks: Antitrust Policy for Business Format Franchise*, 27 ARIZ. L. REV. 341 (1985). According to Konigsberg, *A Compendium of Franchising Terms*, J. INT'L FRANCHISING & DISTRIBUTION L., Dec. 1987, at 58, the U.S. Department of Commerce has defined business format franchising as being "characterized by an ongoing business relationship between Franchisor and Franchisee that includes not only the product, service and trade mark, but the entire business format itself—a marketing strategy and plan, operating manuals and standards, quality control, and continued two-way communic[a]tions." *Id.* at 60.

66. Franchising Regulation, *supra* note 22, art. 1(3)(a), at 48, *reprinted infra* p. 302.

67. *Id.* art. 1(3)(b), at 48, *reprinted infra* p. 302.

68. *Id.*

69. *Id.*

70. Korah considers that "[t]here seems to be no reason why the exemption should not apply where the value of the franchise may be the reputation of the net-

The Regulation further defines "know-how" as a body of "non-patented practical information, resulting from experience and testing by the franchisor, which is secret, substantial and identified."<sup>71</sup> This definition is almost identical to the one adopted in the block exemption for know-how licensing agreements (the "Know-How Regulation").<sup>72</sup> In the same way as the Know-How Regulation, the Franchising Regulation defines successively the concepts of secret, substantial, and identified. "Secret" is taken in the broad sense, so that the way in which the different elements constituting the know-how are combined must not be "generally known or easily accessible."<sup>73</sup> Each element does not have to be secret or original.

The substantiality of the know-how is also defined in a relative way: it must be assessed by reference to its usefulness for the franchisee, that is to say, it should be "capable, at the date of conclusion of the agreement, of improving the competitive position of the franchisee . . ."<sup>74</sup> With respect to the previous situation of the franchisee, the know-how must either help it enter a new market or, if it is already present in that market, improve its performance.<sup>75</sup> The know-how must be of importance for selling goods or for providing services to end-users. It should relate, in particular, to "the presentation of goods for sale, the processing of goods in connection [with] the provision of services, methods of dealing with customers, and administration and financial management."<sup>76</sup> The know-how in-

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work, rather than substantial know-how." Korah, *supra* note 31, at 129. This view is not reconcilable with the Pronuptia judgment, which reasons that the basis for the difference of treatment between selective distribution agreements and franchise agreements is the importance of the know-how involved for the latter and the necessity to protect it. Korah notes that where "the know-how is of little value, territorial protection from others in the network is unlikely to be important." *Id.* Agreements that do not include such protection shall normally not fall under Article 85(1) and have, therefore, no need for an exemption. See *infra* notes 120-28 and accompanying text on the question of differentiation between distribution and franchise agreements.

71. Franchising Regulation, *supra* note 22, art. 1(3)(f), at 48, *reprinted infra* p. 303.

72. Comm'n Regulation No. 556/89, O.J. L 66/1 (1989) [hereinafter Know-How Regulation] (on the application of Article 85(3) of the Treaty to certain categories of know-how licensing agreements).

73. Franchising Regulation, *supra* note 22, art. 1(3)(g), at 48, *reprinted infra* p. 303.

74. *Id.* art 1(3)(h), at 49, *reprinted infra* p. 303.

75. *Id.*

76. *Id.*

volved is not necessarily only commercial but may also be technical, especially in the case of service franchising.<sup>77</sup> The definition of the purposes of the know-how is one of the criteria that helps to determine whether an agreement is covered either by the Franchising Regulation or the Know-How Regulation. Recital 5 of the Franchising Regulation refers more specifically to the processing or adaptation of goods to fit the specific needs of customers. This does not cover industrial fabrication but covers, for example, such operations as key reproduction or assembly of prefabricated elements to form a door or window of a determined size.

Finally, the know-how must be recorded in an appropriate form.<sup>78</sup> For franchise agreements, this record usually takes the form of a "bible," which describes in detail all the necessary information for the functioning of the franchised outlets. It may also be recorded in any kind of computer storage or data base. This condition is set up to make it possible to check, *a posteriori*, the secrecy and substantiality of the know-how in case of contestation.<sup>79</sup> The Regulation does not specify the conditions of disclosure of the know-how, as it is not considered to be a problem of competition law.<sup>80</sup>

The Regulation also gives a specific definition of the "franchisor's goods," which include only the goods manufactured "by the franchisor or according to its instructions, and/or bearing the franchisor's name or trade mark."<sup>81</sup> This category is intended to cover either goods manufactured by the franchisor or its subcontractors, or third parties to which it has granted a manufacturing license; these goods do not have to carry the franchisor's brand, which may be technically im-

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77. In *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 381, ¶ 15, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438, the Court of Justice only refers to business methods, but only with respect to distribution franchises.

78. Franchising Regulation, *supra* note 22, art. 1(3)(i), at 49, *reprinted infra* p. 303.

79. *Id.*

80. A disclosure obligation is usually contained in the code of ethics adopted by franchising associations; see, for example, article 4 of the code of ethics of the British Franchise Association, which provides that "[f]ull and accurate written disclosure of all information material to the franchise relationship shall be given to the prospective franchisees within a reasonable time prior to the execution of any binding document." BFA Code of Ethics, *reprinted in* M. MENDELSON, *THE ETHICS OF FRANCHISING: A BRITISH FRANCHISE ASSOCIATION GUIDE* 37 app. (1987).

81. Franchising Regulation, *supra* note 22, art. 1(3)(d), at 48, *reprinted infra* p. 303.

possible for certain products. It also covers products manufactured by third parties and selected by the franchisor, which affixes its name on them (distribution trademark). The feature common to these products is that the franchisor has an exclusive right to market them and, therefore, may identify the franchised network with these products. The distinction between the franchisor's products, as defined above, and other products is used in the Regulation to determine which purchasing restrictions may be imposed on the franchisees.<sup>82</sup>

The definition of "contract premises" makes a distinction between fixed and mobile franchises.<sup>83</sup> For the second category, the services are not provided at the franchisee's premises; they may be provided at the customer's premises (e.g., for cleaning services) or in any other place (e.g., for car repair services). In that case, a distinction is made between two concepts: the contract premises and the contract means of transport. The contract premises is the base from which the franchisee operates, i.e., where he keeps his stock and materials, where his customers can contact him, and where his accounts can be checked. The contract means of transport, on the other hand, refers to the van or truck that the franchisee uses to provide the services and to which the franchisor's standards concerning appearance and equipment are applied.

The Franchising Regulation, therefore, only concerns agreements in which the franchisor grants the franchisee the right to use certain signs and know-how and undertakes to provide continuing assistance to the franchisee during the life of the agreement.<sup>84</sup> According to the Court of Justice, these provisions do not by themselves restrict competition<sup>85</sup> and, therefore, do not need an exemption. The Franchising Regulation applies to agreements that combine these provisions with restrictions on competition, such as territorial protection or exclusive dealing.<sup>86</sup>

The Regulation applies only to franchise agreements that

82. See *infra* notes 157-82 and accompanying text.

83. See Franchising Regulation, *supra* note 22, art. 1(3)(e), at 48, *reprinted infra* p. 303.

84. *Id.* art. 1(3)(b), at 48, *reprinted infra* p. 302.

85. Pronuptia, Case 161/84, 1986 E.C.R. 353, 381, ¶ 15, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438.

86. Franchising Regulation, *supra* note 22, recital 9, at 47, *reprinted infra* p. 299.

include conditions to ensure that consumers receive a fair share of the benefits resulting from the exempted agreements. It provides that franchisees are obligated to indicate that they are independent enterprises, so that consumers know that they are not dealing with a branch of a large company. This indication can be made by any appropriate means that does not jeopardize the common identity of the network, for example, a mention in the business papers or a card in the shop-window.<sup>87</sup> Where franchisees must honor a guarantee for the franchisor's products, it is also a condition for the application of the Regulation that this obligation will apply to goods supplied by another member of the franchise network that honors a similar guarantee.<sup>88</sup> This position is in conformity with the Commission's position regarding the application of a European-wide guarantee.<sup>89</sup> This obligation does not, however, prevent the possibility of setting up a parallel network that would offer a less extensive guarantee.<sup>90</sup>

The payment by the franchisee of financial consideration to the franchisor is also considered as a condition for the application of the Regulation, since it is included in the definition of the franchise agreement for the purposes of the Regulation.<sup>91</sup> It is provided that the financial consideration may be direct or indirect, which takes into account that there are not always royalties or an initial payment, in particular, when the franchise concerns the franchisor's products. The payment, therefore, may be included in the price of the goods supplied by the franchisor, as long as it is identifiable.

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87. *Id.* art. 4(c), at 50, *reprinted infra* p. 307; *see, e.g., Computerland, supra* note 37, at 19, ¶ 24(iii), *Common Mkt. Rep. (CCH)* ¶ 10,906, at 12,173.

88. *Franchising Regulation, supra* note 22, art. 4(b), at 50, *reprinted infra* pp. 306-07.

89. *See, e.g., Comm'n, Sixteenth Report on Competition Policy* ¶ 56 (1987) (Commission restating its consistent position that "guarantees offered as part of after-sales service by manufacturers of consumer durables must be valid throughout the Community regardless of the Member State in which the product is purchased"); *see also* *ETA v. DK Investment (Swatch)*, Case 31/85, 1985 E.C.R. 3933, 3943-44, ¶¶ 10-14, *Common Mkt. Rep. (CCH)* ¶ 14,276, at 16,688; *Regulation 123/85, supra* note 42, recital 12, at 18, *Common Mkt. Rep. (CCH)* ¶ 2751, at 1971.

90. *See Hasselblad v. Commission*, Case 86/82, 1984 E.C.R. 883, *Common Mkt. Rep. (CCH)* ¶ 14,014.

91. *Franchising Regulation, supra* note 22, art. 1(3)(b), at 48, *reprinted infra* p. 302.

### B. *Different Kinds of Franchising Systems*

The definition of franchise agreement given in the Regulation can be seen as comprising two parts: first, the general definition is given, and second, the scope of the Regulation is limited to certain kinds of franchising systems, i.e., distribution and service franchises for end-users. It is necessary, therefore, to examine the different kinds of franchises and determine why certain franchises are not covered by the Regulation.

#### 1. Industrial Franchises

An industrial franchise usually consists of an agreement by which one producer grants another producer the right to manufacture certain goods and market them under its trademark. It can be analyzed as a trademark license combined with a manufacturing license based on patents or know-how. This kind of agreement is not covered by the Franchising Regulation, because it raises different issues than are raised by product or service franchises.<sup>92</sup> An industrial franchise normally relates to a horizontal relationship between potentially competitive producers, while the Franchising Regulation covers agreements involving a vertical relationship between a producer or distributor and a retailer.

Industrial franchise agreements should often be able to benefit from the patent-licensing regulation<sup>93</sup> or the Know-How Regulation<sup>94</sup> if they fulfill the necessary conditions for the application of these regulations and, in particular, if substantial industrial property rights are involved. Where the distributor or franchisee only performs additional operations to improve the quality, durability, appearance, or taste of the product, the agreement may also be covered by Regulation 1983/83,<sup>95</sup> as it is interpreted by the relevant Commission's notice.<sup>96</sup>

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92. *Id.* recital 4, at 46, reprinted *infra* p. 298.

93. Comm'n Regulation No. 2349/84, O.J. L 219/15 (1984), Common Mkt. Rep. (CCH) ¶ 2747 (on patent licensing).

94. Know-How Regulation, *supra* note 72.

95. *See supra* note 4.

96. *See* Commission Notice on Regulations 1983/83 and 1984/83, O.J. C 101/2, at 3, ¶ 10 (1984), Common Mkt. Rep. (CCH) ¶ 10,583, at 11,368 [hereinafter Commission Notice]. The notice gives such examples as "rustproofing of metals, sterilization of food or the addition of colouring matter or flavouring to drugs" and specifies that the Commission's position as to the applicability of the Regulation will depend on how much value adds to the goods:

Industrial franchise agreements can also be the object of individual exemption, under the principles of the Commission's administrative practice relating to licensing agreements. The only decision concerning an industrial franchise is the *Campari* decision of December 23, 1977, concerning licensing agreements for the manufacture and sale of spirits under the Campari trademark.<sup>97</sup> This decision exempts, in particular, the obligation on the licensees not to deal in competing products and not to actively market the licensed products outside their territory. It considers as non-restrictive an obligation on the licensees to follow the instructions of the licensor and buy exclusively from him certain secret ingredients; the same applies to an obligation to carry out advertising, not to disclose the licensed know-how, and not to assign their rights without the licensor's consent.<sup>98</sup>

## 2. Distribution and Service Franchises

The Franchising Regulation applies equally to franchising systems relating to the distribution of goods or the provision of services. Although the *Pronuptia* judgment only concerned distribution franchises,<sup>99</sup> the Commission found that the principles expressed in that judgment could apply to service franchises.

The examination of existing systems actually shows that distribution and service franchises do not constitute two clearly distinct categories, but that most systems include both types of franchises in varying proportions. Pure distribution franchises, without provisions for any service, are quite rare, because the resale of goods is usually accompanied by at least some customer services. The practice of the Commission shows this mix in, for example, the *Computerland* decision, where the franchisees provided sales advice, after-sale services,

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Only a slight addition in value can be taken not to change the economic identity of the goods. . . . The Commission applies the same principles to agreements under which the reseller is supplied with a concentrated extract for a drink which he has to dilute with water, pure alcohol or another liquid and to bottle before reselling.

*Id.*

97. *Campari*, O.J. L 70/69 (1978), Common Mkt. Rep. (CCH) ¶ 10,035.

98. *Id.* at 74, Common Mkt. Rep. (CCH) ¶ 10,035, at 10,203.

99. See *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 380-81, ¶ 13, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438.

and training courses,<sup>100</sup> and the *Yves Rocher* decision, where the franchisees undertook to give beauty treatments.<sup>101</sup>

In the case of service franchises, there is also usually a product that results from the service, for instance, keys in key reproduction franchises or soles in shoe repair franchises. Even for service franchises where no product is sold to the customers, such as car rentals or hotels, products are used for the provision of the services and competition restrictions can be involved with respect to the supply of these products. In the Commission's *ServiceMaster* decision, which concerned the notified agreement of a franchise for cleaning services, it is specified that the franchisees must use the franchisor's cleaning products and can resell them to their customers.<sup>102</sup> However, this reselling activity is only collateral to their main activity as providers of services.

Therefore, from the point of view of competition law, there does not appear to be a difference in nature between distribution and service franchises that should justify a difference of treatment. The Regulation takes into account the peculiarities of service franchises in dealing with the obligations that may be imposed on the franchisees but applies the same principles to all franchise agreements, particularly those regarding territorial protection.<sup>103</sup>

### 3. Wholesale and Retail Franchises

The Regulation covers only the selling of products or provision of services to end-users. End-users include professional users as long as they do not buy only to resell to third parties, but instead use the goods sold by the franchisees to sell other goods or provide services.<sup>104</sup> Furthermore, the franchisees must be free to sell products that are the subject of the

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100. See *Computerland*, *supra* note 37, at 12, ¶ 2, Common Mkt. Rep. (CCH) ¶ 10,906, at 12,166-67. The decision concludes, however, that the system constituted a distribution franchise, because the services were only accessories to the resale of goods. *Id.* at 16, ¶ 21, Common Mkt. Rep. (CCH) ¶ 10,906, at 12,170-71.

101. See *Yves Rocher*, *supra* note 36, at 51, ¶ 15, Common Mkt. Rep. (CCH) ¶ 10,855, at 12,049. The same paragraph specifies that these treatments only account for a small proportion of their turnover. *Id.*

102. See *ServiceMaster*, *supra* note 38, at 38-39, ¶ 5, Common Mkt. Rep. (CCH) ¶ 11,047, at 12,546.

103. See *infra* notes 137-56 and accompanying text.

104. It is specified in the *Computerland* decision that most of the franchisees' cus-

franchise to other franchisees or sell to resellers within other channels of distribution supplied by the manufacturer of these goods or with its consent.<sup>105</sup> This provision only aims at avoiding market partitioning and does not contradict the fact that the franchisees must concentrate their activity on retailing.

The Regulation, therefore, does not cover wholesale franchises, i.e., systems where the franchisees act as wholesalers. This is due to the fact that such systems raise different competition problems than retail franchises, in particular in relation to parallel imports. The small number of agreements of this nature known by the Commission seems to indicate that there is no mass problem that would justify a block exemption regulation; furthermore, in that field the Commission would lack the necessary experience required by Regulation 19/65 to prepare a block exemption regulation.<sup>106</sup> This does not mean that such agreements are incompatible with Article 85, but if they fall under paragraph 1 of this Article, they would have to be exempted under Article 85(3) by individual decisions.

#### 4. Master Franchises

Unlike wholesale franchises, the Regulation expressly covers master franchise agreements, that is, two-tiered franchises where the franchisor grants a master franchisee the right to enter into agreements with other parties, the franchisees, to give them the right to exploit the franchise in a given territory.<sup>107</sup> The Regulation indicates that, "[w]here applicable, [its provisions] concerning the relationship between franchisor and franchisee shall apply *mutatis mutandis* to the relationship between franchisor and master franchisee and between master franchisee and franchisee."<sup>108</sup> The Regulation also specifically exempts an obligation on the master franchisee not to conclude franchise agreements with franchisees outside its contract territory.<sup>109</sup> Master franchise agreements are particularly

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tomers are business users. *Computerland*, *supra* note 37, at 12, ¶ 2, Common Mkt. Rep. (CCH) ¶ 10,906, at 12,166-67.

105. See *infra* notes 214-18 and accompanying text.

106. See *supra* notes 34-42 and accompanying text.

107. See LELOUP, *DROIT ET PRATIQUE DE LA FRANCHISE* B29 (1983); Konigsberg, *Agreements Commonly in Use in International Franchise Arrangements, Part One: Master Franchise Agreements*, J. INT'L FRANCHISING & DISTRIBUTION L., June 1987, at 162.

108. Franchising Regulation, *supra* note 22, art. 1(2), at 48, *reprinted infra* p. 302.

109. See *infra* notes 137-56 and accompanying text.

important for international franchisors, who can rely on one single company to develop the franchise in a large territory, usually a whole country.<sup>110</sup> Another form of market penetration for international franchisors is the area development agreement, where a franchisee, or area developer, undertakes to open a certain number of franchises in a given territory, during a given time. The difference between the master franchisee and the area developer is that the latter does not have the right to sub-franchise and is obliged to open all franchised outlets itself.<sup>111</sup> It has been argued that the Regulation should include specific provisions for development agreements.<sup>112</sup> This, however, does not seem to be necessary. Although the Regulation does not mention such agreements, they are also covered by the block exemption, because article 2(c) exempts an obligation on the franchisee to exploit the franchise only from the contract premises.<sup>113</sup> It does not limit the number of premises that should be used by the franchisee to exploit the franchise in its territory.<sup>114</sup>

### C. Sectoral Field of Application of the Block Exemption

#### 1. Reason for Application to All Economic Sectors

The existence of specific block exemption regulations for vertical agreements in the sectors of motor vehicles,<sup>115</sup> service stations,<sup>116</sup> and beer supply<sup>117</sup> raises the problem of the relationship among these different regulations. Two options were

110. See Zeidman, *Pronuptia—the International Perspective*, J. INT'L FRANCHISING & DISTRIBUTION L., Sept. 1986, at 5, 5-6.

111. See Konigsberg, *Agreements Commonly in Use in International Franchise Arrangements, Part Two: Development Agreements and Multiple Unit Franchise Agreements*, J. INT'L FRANCHISING & DISTRIBUTION L., Sept. 1987, at 7. In the case of multiple unit franchise agreement, a franchisee has the right to open more than one franchise outlet in a given area but without exclusivity; each new outlet is subject to the franchisor's approval. See *id.* at 12-13.

112. See Zeidman & Renz, *Will Master Franchise Agreements be Covered by the Proposed Block Exemption Regulation for Franchising Agreements?*, J. INT'L FRANCHISING & DISTRIBUTION L., Dec. 1987, at 84.

113. Franchising Regulation, *supra* note 22, art. 2(c), at 49, *reprinted infra* p. 304.

114. In *Computerland*, *supra* note 37, at 22, ¶ 36, Common Mkt. Rep. (CCH) ¶ 10,906, at 12,176, the exemption was granted *mutatis mutandis* to the area development agreements involved.

115. Regulation 123/85, *supra* note 42.

116. Comm'n Regulation No. 1984/83, tit. III, O.J. L 173/5, at 10 (1983), Common Mkt. Rep. (CCH) ¶ 2733, at 1912-13.

117. *Id.* tit. II, at 9-10, Common Mkt. Rep. (CCH) ¶ 2733, at 1910-12.

conceivable: either decide that the Franchising Regulation would not apply in sectors where specific regulations had already been adopted, or decide that agreements fulfilling the conditions set out in the Franchising Regulation could not also benefit from another block exemption, whatever the sector concerned.

The first approach would have been based on the consideration that there are only limited differences between franchising and other distribution systems, primarily selective distribution and exclusive purchasing agreements. The reasoning followed by the Commission in adopting specific provisions concerning distribution in the sectors of motor vehicles, service stations, and beer is because of the particularities of their economic structure.<sup>118</sup> This reasoning should, therefore, also be applied to exclude the application of the Franchising Regulation to such sectors. The Regulation would then have included a provision stating that it did not apply to agreements concluded in sectors where a specific block exemption for exclusive distribution or purchasing agreements had been adopted.

The Commission did not retain that approach but stipulated, to the contrary, the following:

Agreements may benefit from the provisions either of [the Franchising Regulation] or of another Regulation, according to their particular nature and provided that they fulfil the necessary conditions of application. They may not benefit from a combination of the provisions of [the Franchising Regulation] with those of another block exemption Regulation.<sup>119</sup>

This means that only franchise agreements that have all restrictions covered by the Franchising Regulation are deemed to be automatically exempted and that franchise agreements that include restrictions that are not covered by it are not automatically exempted, even if these restrictions were covered by another block exemption. This condition results from the fact that the Regulation is based on a global assessment of the re-

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118. See Regulation 123/85, *supra* note 42, recital 3, at 16, Common Mkt. Rep. (CCH) ¶ 2751, at 1970; Regulation 1984/83, *supra* note 4, recital 12, at 6, Common Mkt. Rep. (CCH) ¶ 2733, at 1906.

119. Franchising Regulation, *supra* note 22, recital 17, at 48, *reprinted infra* p. 301.

strictions and other obligations that are necessary to reach the advantages brought about by the franchise agreements. The addition of other restrictions that may be considered acceptable in the framework of other agreements would destroy that balance. However, agreements that satisfy the conditions set out in article 4 and do not include any provision listed in the "black list" of article 5 may benefit naturally from the opposition procedure.

## 2. Differences Between Franchise and Other Agreements

The refusal to exclude the application of the Franchising Regulation in certain sectors results from the consideration, expressed by the Court of Justice, that franchise agreements are different in nature from distribution and exclusive purchasing agreements.<sup>120</sup> The Court of Justice considered that franchise agreements enable the franchisor to exploit its knowledge without risking its own capital, provide franchisees without any substantial experience access to the franchisor's methods, and enable franchisees to benefit from the reputation of the franchisor's sign.<sup>121</sup> It concluded that distribution franchise agreements differ from exclusive dealing or selective distribution agreements, because these do not include the utilization of the same shop sign, the application of uniform commercial methods, and the payment of royalties.<sup>122</sup> In the Regulation, the Commission considers that the application of uniform commercial methods results from the communication of know-how and the provision of continuing assistance. Four main differences, therefore, can be emphasized.

The first relates to the use of a common name or shop sign, which gives the network its uniform appearance.<sup>123</sup> Only the name of the franchisor appears on the shop front, and the

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120. See *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 387, ¶ 33, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,441.

121. *Id.* Demaret reasonably remarks that these conditions are not always met, as the franchisor sometimes supplies the premises used by the franchisee, thereby investing some capital, and that the franchisee may already have some experience. More than criteria, these are characteristics often found in franchise agreements. Demaret, *supra* note 32, at 731.

122. See *Pronuptia*, 1986 E.C.R. at 381, ¶ 15, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438.

123. See Franchising Regulation, *supra* note 22, art. 1(3)(b), at 48, *reprinted infra* p. 302.

franchisee is obliged not to develop a separate goodwill attached to its name. This should not prevent the possibility of indicating that the franchisee is an independent undertaking, thus avoiding the possibility of giving a misleading impression to consumers. However, this indication must be made in a way that does not jeopardize the uniformity of the network.<sup>124</sup> The fact that the satisfaction or dissatisfaction of consumers is directly linked to the name of the franchisor justifies, in particular, the franchisor exercising a tighter control on the franchisees to maintain the reputation of its network. In the case of automobile or beer distribution agreements, the trademark of the car manufacturer or brewer is also displayed on the shop sign, but it is always in conjunction with either the dealer's trade name or the name of the premises. The consumer, therefore, will link the name of the manufacturer with the product and the name of the dealer or of the premises with the service he received.

The second element is the communication of substantial know-how devised and experienced by the franchisor.<sup>125</sup> This reveals a different, and even opposed, strategy for the expansion of a selective distribution network as compared with franchising. In the first case, the manufacturer relies mainly on the know-how of traders that are already established and have experience in the sector. The franchisor, on the contrary, usually looks for candidates that either are not yet established as independent traders or were active in a different sector. The main criterion for selection is, apart from having the necessary capital, the aptitude to apply the methods developed by the franchisor.<sup>126</sup> Franchising, therefore, may be a way for a new entrant in a market to develop a network independent from existing distributors, who are already linked to other manufacturers.

The third factor is a consequence of the former: because of the relative inexperience of the franchisees, the successful application of the franchisor's methods cannot be limited to the initial communication of know-how by the franchisor but

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124. *Id.* recital 12, at 47, *reprinted infra* p. 300.

125. *See Pronuptia*, 1986 E.C.R. at 381-82, ¶ 16, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438-39.

126. *See* M. MENDELSON, *THE GUIDE TO FRANCHISING* 66-67 (4th ed. 1985).

must be supported by an updating of that know-how by the franchisor's continuing assistance.<sup>127</sup> Even if such assistance is present in certain cases of selective distribution, its importance is more limited because of the pre-existing experience of the dealers.

Finally, franchise agreements are characterized by the payment of a financial consideration. This characteristic, which does not exist in selective distribution or exclusive purchasing agreements, results from the communication of industrial property rights and the fact that the franchisees do not necessarily buy products from the franchisor. This is, however, a criterion that is more difficult to assess, because the compensation may be made in different forms.<sup>128</sup>

### 3. Consequence of the Differences

The consequence of the differences examined above is that agreements presently covered by Regulations 1984/84 or 123/85 will not benefit from the Franchising Regulation, because they do not fulfill the conditions for its application. However, the fact that the Commission has exempted certain kinds of agreements for these sectors does not mean that only agreements of that nature may be concluded.<sup>129</sup> On the contrary, the coexistence of agreements of different natures in a given sector favors competition, and the exclusion of certain sectors from the block exemption would have created discrimination against those undertakings. It will, therefore, be possible to create new networks by concluding franchise agreements covered by the Franchising Regulation.

In addition, it will be possible to replace existing selective distribution or exclusive purchasing agreements by franchise agreements covered by the Franchising Regulation. This, of course, will not imply just changing the name of the agree-

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127. Franchising Regulation, *supra* note 22, art. 1(3)(b), at 48, *reprinted infra* p. 302.

128. *See supra* note 91 and accompanying text.

129. *See, e.g.,* V.A.G. France v. Etablissements Magne, Case 10/86, 1986 E.C.R. —, Common Mkt. Rep. (CCH) ¶ 14,390. In *V.A.G. France*, the Court of Justice specifically considered that Regulation 123/85, *supra* note 42, exempting motor car distribution agreements, does not set up provisions directly affecting the validity of agreements or oblige the contracting parties to adapt the contents of their contracts to its provisions. *V.A.G. France*, 1986 E.C.R. at —, Common Mkt. Rep. (CCH) ¶ 14,390, at 17,607.

ments but concluding new agreements satisfying all the conditions set out by the Franchising Regulation. The condition relating to the uniformity of the network will be easy to verify. The premises, or vehicles, in the case of mobile franchises, should be identical or closely similar and carry only the name of the franchisor. The communication of substantial know-how would seem to be more difficult to assess.<sup>130</sup> However, in the *Pronuptia* case, the Court of Justice gave some guidance.<sup>131</sup> In deciding that a non-competition clause, even for a reasonable period after termination of the contract, does not fall under Article 85, the Court stressed the necessity of protecting the franchisor's know-how.<sup>132</sup> The definition of substantiality in article 1(3)(h) of the Regulation clarifies how this assessment should be made: the know-how should be "capable, at the date of conclusion of the agreement, of improving the competitive position of the franchisee, in particular, by improving the franchisee's performance or helping it to enter a new market."<sup>133</sup> In a network where the franchisees are mainly new entrants without experience, the know-how communicated by the franchisor could be quite basic. However, if the franchisor wants to deal with undertakings already present in the market, such as car dealers, it will be necessary to demonstrate that the franchisor's know-how represents a substantial improvement over the know-how previously obtained by the franchisee.

#### D. Market Considerations

The Franchising Regulation will not apply if it appears from the position of the parties to an agreement that it could lead to market partitioning. Article 5(a), therefore, excludes the application of the Regulation to agreements between competitors.<sup>134</sup> This situation could arise mainly in connection with master franchise agreements.

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130. See Demaret, *Selective Distribution and EEC Law After the Ford, Pronuptia and Metro II Judgments*, in 1986 FORDHAM CORP. L. INST. 149, 182 (B. Hawk ed. 1987) (car dealerships would probably pass the test but not service station agreements).

131. *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 381-82, ¶ 16, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438-39.

132. *Id.*; see *infra* notes 232-40 and accompanying text.

133. Franchising Regulation, *supra* note 22, art. 1(3)(h), at 49, *reprinted infra* p. 303.

134. *Id.* art. 5(a), at 50, *reprinted infra* p. 307.

The Regulation also provides that the Commission may withdraw the benefit of the exemption where competition or access to the market is restricted because of the cumulative effect of parallel networks of similar agreements. In that case, because of the rigidity of the market, even agreements fulfilling all the conditions of the Regulation might have effects incompatible with the conditions laid down in Article 85(3).<sup>135</sup> The same applies in cases where, in a substantial part of the Common Market, the goods or services that are the subject of the franchise do not face effective competition from the identical or similar goods or services.<sup>136</sup>

### III. SUBSTANTIVE PROVISIONS OF THE REGULATION

#### A. Territorial Protection

The Regulation exempts the practice of protecting the franchisee against direct competition from the franchisor, who may itself not undertake either to exploit the franchise in the contract territory or to sell directly the "franchisor's products"<sup>137</sup> to resellers or end-users in that territory.<sup>138</sup> This obligation is similar to what is exempted by articles 1 and 2(1) of Regulation 1983/83<sup>139</sup> and should be interpreted in the same way. This would not prohibit the manufacturer from supplying its goods to other resellers, who may afterwards sell them in the contract territory, if it supplies the goods only at the reseller's request and the goods are handed over outside the territory.<sup>140</sup>

The franchisee may also be protected from active competi-

135. See *id.* art. 8(a), at 51, *reprinted infra* p. 310. A similar concept is mentioned in the *De Minimis* Notice, *supra* note 17, at 4, ¶ 16, Common Mkt. Rep. (CCH) ¶ 2700, at 1854.

136. See Franchising Regulation, *supra* note 22, art. 8(c), at 51, *reprinted infra* p. xxx; similar provisions are included in Regulation 123/85, *supra* note 42, art. 10(1), at 23, Common Mkt. Rep. (CCH) ¶ 2751, at 1979; Regulation 2349/84, *supra* note 56, art. 9(2), at 23, Common Mkt. Rep. (CCH) ¶ 2747, at 1961; Regulation 1984/83, *supra* note 4, art. 14(a), at 10, Common Mkt. Rep. (CCH) ¶ 2733, at 1913; Regulation 1983/83, *supra* note 4, art. 6(a), at 4, Common Mkt. Rep. (CCH) ¶ 2730, at 1895.

137. As defined in Franchising Regulation, *supra* note 22, art. 1(3)(d), at 48, *reprinted infra* p. 303; see *supra* notes 81-82 and accompanying text.

138. Franchising Regulation, *supra* note 22, art. 2(a), at 49, *reprinted infra* p. 304.

139. See Regulation 1983/83, *supra* note 4, arts. 1, 2(1), at 2-3, Common Mkt. Rep. (CCH) ¶ 2730, at 1893.

140. See Commission Notice, *supra* note 96, at 5, ¶ 27, Common Mkt. Rep. (CCH) ¶ 10,583, at 11,370-71.

tion by other franchisees, as the franchisor may decide that no other company will be granted the right to exploit the franchise in the contract territory. This, however, can never amount to absolute territorial protection, as the franchisor may only impose on the franchisees an obligation not to seek customers outside their territory.<sup>141</sup> A "location clause," or an obligation on the franchisee to exploit the franchise only from the contract premises, is also exempted. In the case of mobile service franchises this obligation relates to the base from which the franchisee exploits the franchise.<sup>142</sup>

The obligations relating to territorial protection constitute one of the main subjects of the Regulation. According to the Court of Justice, provisions organizing a sharing of markets between the franchisor and franchisees or among the franchisees fall under the prohibition of Article 85(1).<sup>143</sup> This is the case when a provision obliging the franchisee to sell only from the contract premises (location clause) is combined with provisions granting the franchisee exclusivity in a given territory for the use of the licensed sign. The Court of Justice considers, however, that this territorial protection of the franchisee might be necessary to ensure a minimum profitability of the franchised outlet, thereby justifying an exemption under Article 85(3).<sup>144</sup> In its reasoning in *Pronuptia*, the Court makes a reference to the *Grundig* judgment<sup>145</sup> and seems to limit the applicability of Article 85(1) to agreements concerning a trademark whose use is already widespread.<sup>146</sup> However, this limitation is not repeated in the operative part of the judgment and its object seems only to recall that Article 85(1) will not apply to agreements that are not capable of affecting trade between Member States.<sup>147</sup>

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141. See Franchising Regulation, *supra* note 22, art. 2(d), at 49, *reprinted infra* p. 304.

142. See *id.* arts. 1(3)(e), 2(c), at 48, 49, *reprinted infra* pp. 303-04.

143. *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 385, ¶ 27, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,442.

144. See *id.* at 383-84, ¶¶ 23-24, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,439-40.

145. *Consten and Grundig v. Commission*, Joined Cases 56 & 58/64, 1966 E.C.R. 299, Common Mkt. Rep. (CCH) ¶ 8046.

146. See *Pronuptia*, 1986 E.C.R. at 384, ¶ 24, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,439-40.

147. This point has been the object of several comments. See Dubois, *supra* note 60, at 132. Venit, *supra* note 7, at 218, considers that territorial restrictions would

It could be argued that the Regulation is more restrictive than the Court of Justice, as it analyzes the territorial protection and the location clause as two separate restrictions,<sup>148</sup> while the Court indicated that their combination led to a sharing of markets prohibited by Article 85(1).<sup>149</sup> Until now, the Commission adopted the same position in its individual decisions.<sup>150</sup> However, it appears that an obligation to carry on the exploitation of the franchise only from the premises described in the contract is a restriction of competition, as it prevents the franchisee from opening a second outlet. On the other hand, the fact that the franchisee can exploit the franchise only from premises approved by the franchisor is not a restriction of competition and is covered by article 3(2)(i) of the Regulation.<sup>151</sup>

The Regulation would not apply if the franchisees were obliged not to supply within the territory goods or services that are the subject of the franchise to end-users because of their place of residence.<sup>152</sup> The block exemption could be withdrawn if in practice the agreement were applied in such a way that the users were prevented, because of their place of residence, from obtaining the goods or services that are the

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have to be assessed under Article 85(3) only in the case of a widespread trademark, while it could be done under Article 85(1) in the case of a new entrant on the market. Green, *supra* note 16, at 197, remarks that although it can be argued that the Court alluded to the fact that a franchise incorporating a new name might not fall under Article 85(1), one cannot make this assertion with absolute confidence, since it was made by the Court in a very backhanded manner. Waelbroeck, *supra* note 7, at 219, rightly remarks that the analogy made by the Court with the *Grundig* judgment seems misplaced, since that case concerned a situation where wholesalers and distributors were prohibited from exporting, while such obligation did not exist in the *Pronuptia* case.

148. See Franchising Regulation, *supra* note 22, arts. 2(c), 3(1)(c), at 49, reprinted *infra* pp. 304-05.

149. See *Grundig*, 1966 E.C.R. at 343, Common Mkt. Rep. (CCH) ¶ 8046, at 7653.

150. See, e.g., *Computerland*, *supra* note 37, at 19, ¶ 25, Common Mkt. Rep. (CCH) ¶ 10,906, at 12,174; *Yves Rocher*, *supra* note 36, at 56, ¶ 54, Common Mkt. Rep. (CCH) ¶ 10,855, at 12,055; *Pronuptia*, *supra* note 35, at 45, ¶ 28, Common Mkt. Rep. (CCH) ¶ 10,854, at 12,044. The last decision even specifies that the obligation to carry on the franchised business from the premises approved by the franchisor does not fall within Article 85(1). *Id.* at 43-44, ¶ 25(ii), Common Mkt. Rep. (CCH) ¶ 10,854, at 12,043.

151. See Franchising Regulation, *supra* note 22, art. 3(2)(i), at 50, reprinted *infra* p. 306.

152. See *id.* art. 5(g), at 50, reprinted *infra* p. 308.

subject of the franchise or if the agreement uses different Member States' specifications in order to isolate markets.<sup>153</sup> This means that the franchisees are only protected against active competition from other franchisees.

This approach is in line with the consistent positions of the Commission and the Court of Justice in relation to exclusive or selective distribution,<sup>154</sup> according to which there would be no absolute territorial protection for distributors, so that parallel imports always remain possible.

The Regulation also exempts an obligation on the master franchisee not to conclude agreements with franchisees outside its territory.<sup>155</sup> This obligation restricts competition, as it is also a partitioning of the market. However, it may be considered necessary to guarantee that the master franchisee concentrates its efforts to develop the franchise in its territory. A similar reasoning has been adopted in connection with motor vehicle distribution.<sup>156</sup>

### B. *Exclusive Dealing and Non-Competition Obligations*

The Regulation makes an important distinction between the franchisor's goods, defined as goods manufactured by the franchisor or according to its instructions and/or bearing the franchisor's brands,<sup>157</sup> and other goods.

#### 1. Franchisor's Goods

As regards the franchisor's goods, the Regulation exempts an exclusive dealing obligation: the franchisee may be obliged not to manufacture, distribute, or use in the process of providing services goods competing with the franchisor's goods that form the subject of the franchise. However, this obligation cannot be imposed for accessories or spare parts for those

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153. See *id.* art. 8(c), (e), at 51, *reprinted infra* p. 310.

154. See, e.g., *Metro v. Commission*, Case 26/76, 1977 E.C.R. 1875, 1907-08, Common Mkt. Rep. (CCH) ¶ 8435, at 7851-52; *Consten and Grundig v. Commission*, Joined Cases 56 & 58/64, 1966 E.C.R. 299, 345, Common Mkt. Rep. (CCH) ¶ 8046, at 7654; *Grundig*, O.J. L 233/1, at 6 (1985), Common Mkt. Rep. (CCH) ¶ 10,701, at 11,639-8.

155. Franchising Regulation, *supra* note 22, art. 2(b), at 49, *reprinted infra* p. 304.

156. See Regulation 123/85, *supra* note 42, recital 9, art. 3(9), at 17, 20, Common Mkt. Rep. (CCH) ¶ 2751, at 1971, 1974.

157. See *supra* notes 81-82 and accompanying text.

goods. These accessories or spare parts are subject to the same provisions as products other than the franchisor's products.<sup>158</sup>

For both categories of products, the Regulation refers not only to the products sold but also to those used in the process of the provision of services. This expression covers both products "consumed" for the provision of services (such as soles for shoe repair franchises) and machines or equipment necessary to provide the services.<sup>159</sup>

Neither of these provisions amounts to allowing an exclusive purchasing obligation, since the franchisee must be free to obtain from other franchisees or distributors the goods that are the subject of the franchise, if those goods are also distributed through other channels by their manufacturer or with its consent.<sup>160</sup> This condition has been emphasized by the Court of Justice<sup>161</sup> and is in line with previous case law concerning distribution agreements.<sup>162</sup>

The distinction between franchisor's products and other products was not made by the Court of Justice in *Pronuptia*. The Court considered as non-restrictive only an obligation on the franchisee to deal exclusively with the products of the franchisor, or producers designated by it, when it was impracticable to formulate objective quality criteria or too expensive to ensure that those criteria are observed.<sup>163</sup> The basis for the distinction made by the Commission is that where the franchisor markets products under its trademark, the franchise formula is used by it to sell the largest possible quantities of its products.<sup>164</sup> The nature of such a franchise is, therefore, dif-

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158. Franchising Regulation, *supra* note 22, art. 3(1)(a)-(b), at 49, *reprinted infra* pp. 304-05.

159. See *ServiceMaster*, *supra* note 38, at 40, ¶ 17, Common Mkt. Rep. (CCH) ¶ 11,047, at 12,547-48.

160. See Franchising Regulation, *supra* note 22, art. 4(a), at 50, *reprinted infra* p. 306.

161. See *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 383, ¶ 21, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,439.

162. See, e.g., *Metro v. Commission*, Case 26/76, 1977 E.C.R. 1875, Common Mkt. Rep. (CCH) ¶ 8435.

163. *Pronuptia*, 1986 E.C.R. at 383, ¶ 21, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,439. Goebel notes that it seems unfortunate that the ruling gives the impression that exclusive supply obligations are generally to be regarded as compatible with Article 85(1). Goebel, *supra* note 7, at 697.

164. The Draft Regulation made a distinction between "producer franchise"

ferent from the one identified by the Court of Justice, as it is, indeed, mainly a mode of distribution.<sup>165</sup>

In *Yves Rocher*, the Commission accepted an exclusive dealing obligation on the grounds that the retailing of products bearing trademarks other than that of the franchisor would expose it to the risk of the use of its know-how for the benefit of competing producers and would detract from the identity of the network, which is symbolized by the franchisor's sign.<sup>166</sup> The franchisees were, however, free to sell accessories not bearing the franchisor's trademark, under the condition that the accessories were previously approved by the franchisor. On the basis of its examination of the relevant facts and, in particular, the structure of the market,<sup>167</sup> the Commission considered that these obligations did not fall under Article 85(1), as they were inherent to the very nature of the Yves Rocher distribution formula.<sup>168</sup>

The Regulation confirms that an exclusive dealing provision relating to the franchisor's goods is acceptable, but on the basis of a different rationale. It was considered impossible to generalize the position taken in *Yves Rocher*, that such an obligation was inherent to the nature of the franchising formula. The Regulation, therefore, considers that an exclusive dealing provision constitutes a restriction of competition under Article 85(1), as it prevents the franchisees from selling competing products even if they are of the same quality.<sup>169</sup> However, this

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and "distributor franchise." Draft Regulation, *supra* note 21, recital 5, at 4; see *Pronuptia*, 1986 E.C.R. at 380-81, ¶ 13, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438. This distinction emphasizes the fact that in one case the franchisor is a producer whose first aim is to sell its goods, while in a "multibrand" franchise, such as Computerland or a supermarket, the franchisor uses its trademark and know-how to sell the products of third parties. This terminology was abandoned, because in a large number of cases the franchisees sell both the franchisor's products and other products. It was replaced by the distinction between the kind of purchasing restrictions admissible in relation with either category of products. Franchising Regulation, *supra* note 22, recital 3, at 46, *reprinted infra* p. 297; see Korah, *supra* note 7, at 99.

165. Whereas the Court of Justice considered that the franchise system of *Pronuptia* was more a way of exploiting knowledge and reputation. *Pronuptia*, 1986 E.C.R. at 381, ¶ 15, Common Mkt. Rep. (CCH) ¶ 10,855, at 12,053.

166. *Yves Rocher*, *supra* note 36, at 55, ¶ 45, Common Mkt. Rep. (CCH) ¶ 10,855, at 12,053.

167. *Id.* at 50, ¶ 7, Common Mkt. Rep. (CCH) ¶ 10,855, at 12,048.

168. *Id.* at 57, ¶ 63, Common Mkt. Rep. (CCH) ¶ 10,855, at 12,056.

169. See Franchising Regulation, *supra* note 22, art. 2(e), at 49, *reprinted infra* p. 304.

restriction is compatible with the objectives of Article 85(3), because it guarantees that the franchisor's know-how is used only to promote the sale of the franchisor's products and permits a complete identification between the trademark of the products sold and the sign on the shop.<sup>170</sup>

The Regulation, therefore, allows the franchisor to establish a network of outlets bearing its trademark and selling only goods bearing that trademark, as long as they form the essential object of the franchise. Where the object of the franchise is, at the same time, to sell certain products and their accessories or spare parts, the franchisee must be free to sell competing accessories or spare parts of matching quality or, if no specification of quality is practicable, such products made by manufacturers agreed to by the franchisor.<sup>171</sup> An exclusive dealing obligation for these accessories or spare parts cannot generally be considered indispensable to the achievement of positive results from the franchise agreements, because the sale of such products will not normally jeopardize the uniform appearance of the network or prevent the franchisee from concentrating its efforts on the marketing of the franchisor's goods or services. Similar reasoning is seen in the motor vehicle distribution regulation.<sup>172</sup> An agreement that includes an exclusive dealing obligation with a wider scope would be included in the "black list" and, therefore, could not benefit from the opposition procedure.<sup>173</sup>

## 2. Other Goods

For products other than the franchisor's products, the Regulation considers as non-restrictive an obligation to deal only with goods meeting minimum objective quality specifications laid down by the franchisor, insofar as it is necessary to protect the franchisor's know-how or maintain the common identity of the network. If the quality specifications were imposed on other grounds, the agreement should be submitted to the opposition procedure. If, however, the franchisees were

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170. *See id.* recital 9, at 47, *reprinted infra* p. 299.

171. *Id.*

172. *See* Regulation 123/85, *supra* note 42, recital 8, at 17, Common Mkt. Rep. (CCH) ¶ 2751, at 1970.

173. Franchising Regulation, *supra* note 22, art. 5(b)-(c), at 50, *reprinted infra* p. 307.

prevented from obtaining supplies of goods of equivalent quality to those proposed by the franchisor, the Regulation would not apply, as it is specified that it does not apply if the franchisee is prevented from obtaining goods of equivalent quality to those proposed by the franchisor.<sup>174</sup>

If it is impracticable to formulate such criteria, the franchisees may be obliged to deal only in goods manufactured by the franchisor or other producers designated by it. This condition finds its origin in the *Pronuptia* judgment, where the Court gave two examples of such impracticability: the nature of the products (in that case, fashion products) or the large number of franchisees.<sup>175</sup> The term "impracticable" must be interpreted to cover cases where it is theoretically possible, but too expensive, to apply such criteria. The Commission referred only to the nature of the products, because the large number of franchisees was considered to be too subjective a criterion for a block exemption regulation. Agreements including an exclusive dealing obligation where the nature of the products makes it practicable to define objective quality criteria may benefit from the opposition procedure insofar as it is possible for the franchisee to obtain supplies of goods of equivalent quality to those offered by the franchisor. On the other hand, the exemption does not apply if the franchisor refuses to designate as authorized manufacturers, third parties proposed by the franchisees for reasons other than protecting the franchisor's industrial property rights or maintaining the common identity and reputation of the network.<sup>176</sup> The franchisor must prove that the proposed manufacturers are not suitable.

The Community approach towards exclusive dealing obligations is quite different from the U.S. approach. In the United States, *Martino v. McDonald's*<sup>177</sup> held that an obligation imposed by a franchisor on a franchisee to buy and use one brand of cola does not constitute a *per se* illegal tie-in contrary to section 1 of the Sherman Act<sup>178</sup> where the economic benefit

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174. *Id.* art. 5(b), at 50, *reprinted infra* p. 307.

175. *See* *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 383, ¶ 21, *Common Mkt. Rep.* (CCH) ¶ 14,245, at 16,439.

176. *Franchising Regulation*, *supra* note 22, art. 5(c), at 50, *reprinted infra* p. 307.

177. 625 F. Supp. 356 (N.D. Ill. 1985).

178. 15 U.S.C. § 1 (1982).

to the franchisor is general.<sup>179</sup> It also does not violate the Sherman Act under a rule-of-reason analysis, where the franchisor has no economic interest in the sale of the brand chosen but, rather, an interest in the linkage of the franchise with a product that is well perceived by the consumers.<sup>180</sup> The criterion to decide whether a tying arrangement is an exclusive dealing obligation that constitutes a *per se* violation is whether or not the franchisor has a "direct economic interest in the tied product . . . ."<sup>181</sup> This criterion seems to be rather formalistic as there may be indirect interests, such as special discounts to the franchisees, which will not always be identifiable. On the other hand, the Commission's position is based on the consideration that an exclusive dealing obligation constitutes a tie-in that restricts competition, because it prevents competing manufacturers from selling through the franchise network, and this obligation is not indispensable for the proper functioning of the network if other products of equivalent quality exist.<sup>182</sup>

### 3. Non-Competition Obligation During the Term of the Agreement

For the franchisor's goods, it should be stressed that an exclusive dealing obligation that is exempted by the Regulation makes it possible to oblige the franchisee not to manufacture or sell goods competing with the franchisor's goods, with the exception of spare parts or accessories for those goods.<sup>183</sup>

For other goods, the Regulation considers as not restrictive, insofar as it is necessary to protect the franchisor's know-how or to maintain the identity of the network, an obligation not to engage directly or indirectly in a similar business, in a territory where it would compete with a member of the franchised network.<sup>184</sup> This limitation was used by the Court of Justice in the *Pronuptia* judgment,<sup>185</sup> and the Regulation confirms it with the specification that "member of the franchised

179. *Martino*, 625 F. Supp. at 362.

180. *Id.* at 363.

181. *Id.* at 362. *But see* Robert's Waikiki U-Drive v. Budget Rent-A-Car, 732 F.2d 1403, 1407-08 (9th Cir. 1984) (interest need not be so direct).

182. Franchising Regulation, *supra* note 22, art. 5(b), at 50, *reprinted infra* p. 307.

183. *See id.* art. 2(e), at 49, *reprinted infra* p. 304.

184. *Id.* art. 3(1)(c), at 49, *reprinted infra* p. 305.

185. *See Pronuptia*, Case 161/84, 1986 E.C.R. 353, 381-82, ¶ 16, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438-39.

network" includes the franchisor. The ground for this territorial limitation is that for such products, the franchisor's revenue results from the royalties paid; it does not depend on which products are sold but on the amount of business done by its franchisees. As a consequence, there are no grounds to protect the franchisor from the franchisee's competition where the franchised network is not established. It should be noted that an obligation on the franchisee not to use the franchisor's know-how for purposes other than the exploitation of the franchise applies without territorial limitation.<sup>186</sup> Furthermore, in cases where the franchisee is an individual, an obligation to use its best endeavors to exploit the franchise,<sup>187</sup> which is considered as non-restrictive, may practically amount to an obligation not to engage in any other business.

A non-competition obligation should not extend as far as a complete prohibition on the franchisee from investing in any competing business. The only restrictions that may be imposed on the franchisee's freedom of investment must be justified by the need to avoid circumvention of a non-competition obligation by investments of the franchisee. This would be the case, in particular, if the franchisee were personally involved in a competing company. The Regulation, therefore, considers as non-restrictive an obligation on the franchisee not to acquire a financial interest in a competing undertaking to an extent where the power to influence the economic conduct of that undertaking would be present.<sup>188</sup>

Agreements including more restrictive provisions, such as a complete prohibition on investment in competing companies or the prohibition of such investments that do not give the franchisee a power to influence the conduct of the competing enterprise, will have to be submitted to the opposition procedure. The Commission, in its individual decisions, stressed that franchisees were free to acquire financial interests in enterprises competing with the franchisor as long as it did not involve them personally carrying on competing activities, or it requested the franchisors to modify their agreements so that

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186. See Franchising Regulation, *supra* note 22, art. 3(2)(d), at 50, *reprinted infra* p. 306.

187. *Id.* art. 3(1)(f), at 49, *reprinted infra* p. 305.

188. See *id.* art. 3(1)(d), at 49, *reprinted infra* p. 305.

this possibility could exist.<sup>189</sup> In *ServiceMaster*, the Commission observed:

Although the prohibition against acquiring non-controlling financial interest in the capital of a competing publicly-quoted company can be a restriction of competition falling within Article 85(1), in this particular case it is not considered to be an appreciable restriction because the franchisees are generally small undertakings for which the prohibition against acquiring more than 5% of a publicly-quoted company does not normally constitute a real hindrance in the development of their own activities.<sup>190</sup>

#### 4. Post-Term Ban

The Regulation also considers as non-restrictive an obligation not to engage in any similar business after termination of the agreement, if the obligation is for a reasonable period, not exceeding one year, and only applies in the territory where the franchise was exploited.<sup>191</sup> The Court of Justice only made a reference to a reasonable period<sup>192</sup> and the Commission has never accepted a period greater than one year in its decisions. In *Pronuptia*, the Commission specified that the post-term ban provision of the agreement did not apply if the franchisee had exploited the franchise for more than ten years, had fulfilled its obligation, and did not join a competing network.<sup>193</sup> In *Charles Jourdan*<sup>194</sup> there was no post-term ban, and it was specified that because most of the franchisees already had some experience in that sector before becoming franchisees, a post-term ban would probably not have been accepted.<sup>195</sup> Regarding the ter-

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189. See, e.g., *ServiceMaster*, *supra* note 38, at 39-40, ¶ 10, Common Mkt. Rep. (CCH) ¶ 11,047, at 12,547 (franchisee was free to acquire financial interests of up to five percent of capital of a publicly-quoted company); *Computerland*, *supra* note 37, at 17, ¶ 22(ii), Common Mkt. Rep. (CCH) ¶ 10,906, at 12,171; *Yves Rocher*, *supra* note 36, at 52, ¶ 26, Common Mkt. Rep. (CCH) ¶ 10,855, at 12,051.

190. *ServiceMaster*, *supra* note 38, at 39-40, ¶ 10, Common Mkt. Rep. (CCH) ¶ 11,047, at 12,547.

191. Franchising Regulation, *supra* note 22, art. 3(1)(c), at 49, *reprinted infra* p. 305.

192. See *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 381-82, ¶ 16, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,438-39.

193. See *Pronuptia*, *supra* note 35, at 41, ¶ 11, Common Mkt. Rep. (CCH) ¶ 10,854, at 12,041.

194. See *Charles Jourdan*, *supra* note 39.

195. *Id.* at 36, ¶ 27.

ritory where a non-competition obligation may apply, the Court of Justice made no distinction between the period during the validity of the agreement and the period following its termination. In the Commission's decisions, apart from *Pronuptia*, a post-term competition ban was stipulated only for the territory where the franchisee had been exploiting the franchise or for a smaller territory.<sup>196</sup>

The rationale given by the Court of Justice for considering this obligation as non-restrictive is not entirely convincing. The protection of the franchisor's know-how is already ensured by the obligations not to use the know-how after termination of the agreement and not to disclose the know-how to third parties. The non-competition clause may be considered useful, however, because it is usually difficult for the franchisor to prove an unauthorized use of its know-how. It may also be necessary to protect the goodwill of the franchise, which results from the franchisor's sign and commercial methods and from the way in which they have been applied by the franchisee.<sup>197</sup> If the franchisee were allowed to go on with a similar business at the same place where it once exploited the franchise, the mere fact that the franchisor's brand would be removed and the appearance of the outlet modified would not avoid the risk of the former franchisee keeping the largest part of its customers and could prevent the franchisor from profitably setting-up a new franchised outlet in that area. The post-term ban is, therefore, justified only in the area where the franchisee has exploited the franchise.

However, the franchisee should not completely be prevented from pursuing a similar business and from keeping some of its customers. Furthermore, the territories are usually such that the franchisee would be prevented from opening new premises in the same town or in the main shopping area of the same town. This is why the duration of the post-term ban should be reasonable and should, in any case, not exceed one

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196. See, e.g., *ServiceMaster*, *supra* note 38, at 39-40, ¶ 10, Common Mkt. Rep. (CCH) ¶ 11,047, at 12,547.

197. Galan Corona notes that the post-term ban raises major problems but considers that it is an application of the principles established in relation to the sale of a business. Galan Corona, *supra* note 7, at 697.

year,<sup>198</sup> which in almost all cases will be sufficient to allow the franchisee to set up new premises. A shorter period should often be considered as reasonable where the franchisee was already active in that sector before joining the franchised network, because it had already developed a know-how distinct from the franchisor's, or where the franchise concerns franchisor's products that are not distributed through other channels, as the risk of confusion for the customers is then very limited or non-existent.

Obligations on the franchisee after termination of the contract that are less restrictive than a non-competition obligation, for example, a prohibition of solicitation of former customers,<sup>199</sup> are also considered as not falling under Article 85(1). On the other hand, agreements that include a post-term competition ban for a period that cannot be considered as reasonable or exceed one year must be submitted to the opposition procedure.<sup>200</sup>

### C. Price Restrictions

Two provisions relate to prices:<sup>201</sup> article 5(e) stipulates that the Regulation does not apply when the franchisee is restricted in the determination of its sale prices, but this does not prevent the franchisor from recommending such prices.<sup>202</sup> This means that in the case of a concerted practice between the franchisor and its franchisees to maintain resale prices, the Regulation will not apply and any national court could declare the agreement contrary to Article 85 and, consequently, void. Furthermore, article 8(d) specifies that the Commission may withdraw the benefit of the block exemption when franchisees engage in concerted practices among themselves relating to the sale prices of the goods or services that are the object of the franchise.<sup>203</sup> In that case, a decision of the Commission is

198. See Franchising Regulation, *supra* note 22, art. 3(1)(c), at 49, *reprinted infra* p. 305.

199. See, e.g., *ServiceMaster*, *supra* note 38, at 40, ¶ 11, Common Mkt. Rep. (CCH) ¶ 11,047, at 12,547.

200. See Franchising Regulation, *supra* note 22, art. 6(1), at 50, *reprinted infra* p. 308.

201. *Id.* arts. 5(e), 8(d), at 50-51, *reprinted infra* pp. 307, 310.

202. *Id.* art. 5(e), at 50, *reprinted infra* p. 307.

203. *Id.* art. 8(d), at 51, *reprinted infra* p. 310.

necessary to withdraw the benefit of the Regulation.<sup>204</sup>

These provisions are closely related to the considerations of the Court of Justice in the *Pronuptia* case, according to which, the communication of recommended prices was not restrictive of competition as long as there was no accompanying concerted practice.<sup>205</sup> This position has been followed by the Commission in its individual decisions,<sup>206</sup> and the Regulation confirms that the communication of recommended prices is not a restriction, since it is not included among the exempted restrictions but only mentioned as not preventing the application of the Regulation.

Resale price maintenance, on the other hand, is prohibited by Article 85(1), because it suppresses all intrabrand price competition. The broad formulation used by the Regulation covers not only fixed prices but also minimum or maximum prices; the negative effect of minimum prices is self-evident, and the Commission considers that maximum prices could have the same effect as fixed prices in bringing consumer prices to a uniform level.<sup>207</sup> This is in line with the case law of the Court of Justice concerning selective distribution, according to which, even if some limitation in price competition is inherent in selective distribution systems, this competition should never be eliminated.<sup>208</sup> It is only in the sector of newspapers that the Court has considered that resale price maintenance might be exempted under Article 85(3) if it were the only means for the publisher to finance the practice of taking back unsold copies and the only means to offer a wide range of press products to the public.<sup>209</sup>

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204. See *supra* notes 54-56 and accompanying text.

205. See *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 384, ¶ 25, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,440.

206. See *Pronuptia*, *supra* note 35, at 44, ¶ 26, Common Mkt. Rep. (CCH) ¶ 10,854, at 12,043-44; *Yves Rocher*, *supra* note 36, at 56, ¶ 51, Common Mkt. Rep. (CCH) ¶ 10,855, at 12,054-55.

207. See, e.g., *Yves Rocher*, *supra* note 36, at 53, ¶ 34, Common Mkt. Rep. (CCH) ¶ 10,855, at 12,052. The Commission mentions that before granting the exemption, it requested Yves Rocher to avoid any reference in its circulars to the notion of maximum price and to issue a circular to its franchisees stressing that the recommended prices were purely guidelines. *Id.*

208. See, e.g., *Ford v. Commission*, Joined Cases 25 & 26/84, 1985 E.C.R. 2725, Common Mkt. Rep. (CCH) ¶ 14,144; *Metro v. Commission*, Case 26/76, 1977 E.C.R. 1875, 1904-05, ¶ 21, Common Mkt. Rep. (CCH) ¶ 8435, at 7850.

209. See *Binon v. AMP*, Case 243/83, 1985 E.C.R. 2015, 2046, ¶ 46, Common

It has been argued that the application of the concept of concerted practices to resale price maintenance is ambiguous, since the Court of Justice has defined concerted practices as any direct or indirect contact between economic operators, having as its object or effect either to influence the conduct of a competitor or to inform it about the conduct that one intends to adopt.<sup>210</sup> This could be interpreted as meaning that the mere fact that a price recommendation is followed by franchisees could be deemed to amount to a concerted practice.<sup>211</sup> However, it should be stressed that this definition of concerted practice has been used by the Court of Justice only in the context of horizontal agreements and actually refers to contacts between competitors. The same reasoning cannot be transposed to the relationship between manufacturer and distributor. The practice of the Commission and the case law of the Court of Justice shows that in the case of vertical agreements, recommended prices are condemned only if actions are taken to implement them in a compulsory way.<sup>212</sup> Indirect price fixing, such as an obligation on a franchisee not to harm the brand image of the franchisor by its pricing level, has also been considered unacceptable.<sup>213</sup>

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Mkt. Rep. (CCH) 14,218, at 16,327. On June 23, 1987, the Commission published its intention to make a favorable decision in that case, subject to the condition that resale price maintenance should not apply to parallel imports of newspapers. Notice Pursuant to Article 19(3) of Regulation No. 17 Concerning Case IV/31.609—Agence et Messageries de la Presse, O.J. C 164/2, at 3-4, ¶ 18 (1987).

210. See, e.g., *Suiker Unie and Others v. Commission*, Joined Cases 40-48, 50, 54-56, 111, 113 & 114/73, 1975 E.C.R. 1663, 1942, ¶ 174, Common Mkt. Rep. (CCH) ¶ 8334, at 8179.

211. See Schroedermier, *Die Pronuptia Entscheidung des EuGH*, 36 WuW 670, 675 (Sept. 1986); Waelbroeck, *supra* note 7, at 221. But see Harris, *Franchisees and 'Concerted Practices'*, J. INT'L FRANCHISING & DISTRIBUTION L., Dec. 1986, at 70, 71 (little likelihood of breach of competition rules by following recommended prices).

212. See, e.g., *Hasselblad*, O.J. L 161/18, at 29, 32, ¶¶ 65-66, 76 (1982), Common Mkt. Rep. (CCH) ¶ 10,401, at 10,843, 10,846; *AEG-Telefunken*, O.J. L 117/15, at 26, ¶ 68 (1982), Common Mkt. Rep. (CCH) ¶ 10,366, at 10,787-16, *aff'd*, *AEG v. Commission*, Case 107/82, 1983 E.C.R. 3151, Common Mkt. Rep. (CCH) ¶ 14,018; see Goebel, *supra* note 7, at 698-99.

213. See *Pronuptia*, *supra* note 35, at 41, ¶ 12(c), Common Mkt. Rep. (CCH) ¶ 10,854, at 12,041. In *Pronuptia*, the Commission specified that a clause to this effect had to be abolished before the Commission could grant an exemption. See *id.* In the field of exclusive distribution, the Commission considered that the argument of maintaining the brand image of a producer of luxury products (cognac) may not justify its intervention in its exclusive distributor's pricing policy. See *Hennessy-Henkell*, O.J. L 383/11, at 16-17, ¶¶ 32-33 (1980), Common Mkt. Rep. (CCH) ¶ 10,283, at

#### D. Customer Restrictions

The Regulation considers as non-restrictive an obligation on the franchisees to sell the products that are the subject of the franchise only to end-users or to other members of the network. When these products are also sold to other resellers outside the network with the manufacturer's consent, the franchisee can also supply such resellers.<sup>214</sup> This obligation has already been considered as non-restrictive in the case of selective distribution<sup>215</sup> and in several decisions concerning franchising.<sup>216</sup> In *Computerland*, it was specified that an obligation on the franchisees not to supply resellers outside the network is considered non-restrictive when the franchisees sell products bearing the franchisor's name or trademark; this obligation is, on the other hand, considered as restrictive when the franchisees sell products from other manufacturers and are prevented from supplying other qualified resellers.<sup>217</sup> The Regulation is consistent with this position by accepting an obligation to sell solely within the franchised network only if the manufacturer of the goods does not market them through other channels.<sup>218</sup> On the other hand, if it also supplies agreed dealers within a selective distribution system or any resellers, the franchisees should be free to supply these dealers or resellers.

#### E. Other Obligations Relating to the Control of the Network

Under the same qualification that applies to an obligation to sell only products of a certain quality,<sup>219</sup> the Regulation considers as non-restrictive an obligation on the franchisee to of-

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10,657-7 to 10,657-8. On the other hand, the Commission has accepted that a manufacturer could prohibit dealers within a selective distribution system from advertising that they were selling at "cash and carry" prices. Grundig, O.J. L 233/1, at 4 (1985), Common Mkt. Rep. (CCH) ¶ 10,701, at 11,639-6.

214. Franchising Regulation, *supra* note 22, art. 3(1)(e), at 49, *reprinted infra* p. 305.

215. See, e.g., Metro v. Commission, Case 26/76, 1977 E.C.R. 1875, 1907-08, ¶¶ 26-27, Common Mkt. Rep. (CCH) ¶ 8435, at 7851-52.

216. See, e.g., *Yves Rocher*, *supra* note 36, at 55, ¶ 46, Common Mkt. Rep. (CCH) ¶ 10,855, at 12,053-54.

217. *Computerland*, *supra* note 37, at 19-20, ¶ 26, Common Mkt. Rep. (CCH) ¶ 10,906, at 12,173-74.

218. See Franchising Regulation, *supra* note 22, art. 2(a), (c), at 49, *reprinted infra* p. 304.

219. *Id.* art. 3(1)(a), at 49, *reprinted infra* p. 304.

fer for sale a minimum range of products, to keep minimum stocks, to achieve a minimum turnover, to plan its orders in advance, to provide warranty services, and to use its best endeavors to sell the goods or services that are the subject of the franchise.<sup>220</sup> These obligations, which would be considered as restrictive of competition in a selective distribution system,<sup>221</sup> are considered as not falling under Article 85(1) because of the particular nature of the franchise agreement and, in particular, because of the importance of the industrial property rights licensed by the franchisor.<sup>222</sup> However, these obligations should be applied only to preserve the identity and reputation of the network. This means, in particular, that they should be applied in a non-discriminatory way to the franchisees.

The Regulation considers as non-restrictive certain obligations on the franchisee relating to advertising, only insofar as they are necessary to protect the franchisor's industrial property rights or maintain the common identity and reputation of the network. The franchisee may be obliged to participate financially in the advertising done by the franchisor and obtain the franchisor's approval for any advertising carried out by the franchisee itself.<sup>223</sup> The Regulation would, therefore, not exempt an obligation that would allow the franchisor to influence the pricing policy of the franchisees through control of their advertising.<sup>224</sup>

In conformity with the *Pronuptia* judgments, the Regulation lists as non-restrictive the other obligations necessary to maintain the identity and the reputation of the network. These include an obligation to attend any training courses offered by the franchisor,<sup>225</sup> apply its methods,<sup>226</sup> comply with the franchisor's standards for equipment and presentation of the premises,<sup>227</sup> and not to change the location of the premises<sup>228</sup>

220. *Id.* art. 3(1)(d), at 49, *reprinted infra* p. 305.

221. *See, e.g.*, *Metro v. Commission*, Case 26/76, 1977 E.C.R. 1875, 1913, ¶ 37, *Common Mkt. Rep. (CCH)* ¶ 8435, at 7854.

222. *See Pronuptia*, *supra* note 35, at 44-45, ¶ 27, *Common Mkt. Rep. (CCH)* ¶ 10,854, at 12,044.

223. *Franchising Regulation*, *supra* note 22, art. 3(1)(g), at 49, *reprinted infra* p. 305.

224. *Id.* art. 5(e), at 50, *reprinted infra* p. 307.

225. *Id.* art. 3(2)(e), at 50, *reprinted infra* p. 306.

226. *Id.* art. 3(2)(f), at 50, *reprinted infra* p. 306.

227. *Id.* art. 3(2)(g), at 50, *reprinted infra* p. 306.

or assign its rights and obligations under the franchise agreement without the franchisor's approval.<sup>229</sup> An obligation on the franchisee to allow the franchisor to carry out checks on the contract premises and of the contract vehicles, inventory, and accounts of the franchisee is also considered as non-restrictive.<sup>230</sup> The franchisor must be able, in particular, to verify that the goods sold or the services provided by the franchisees are up to the standards of the network. The Regulation specifies, however, that the Commission may withdraw the benefit of the exemption when these checks on the franchisee are used for different purposes.<sup>231</sup> This is in order to prevent the franchisor from using these checks to isolate markets by making it difficult for franchisees to supply other franchisees or meet unsolicited orders from customers outside the contract territory.

#### F. Know-How and Other Industrial Property Rights

It is essential for the protection of the franchisor's know-how that the franchisee be obliged not to disclose it to third parties. This obligation is, therefore, not restrictive of competition and may be imposed even after termination of the agreement. The franchisee must also use the know-how and the other industrial property rights licensed by the franchisor only for the exploitation of the franchise and according to the instructions of the franchisor.<sup>232</sup> This may include, in particular, an obligation to use a trademark only in a particular way.<sup>233</sup> For the know-how, this obligation may apply after termination of the contract, as long as the know-how has not fallen into the public domain. If the know-how has become publicly known, the franchisees must be free to use it without limitation, otherwise they would be placed at an unjustified competitive disadvantage vis-à-vis third parties. However, if the know-how enters the public domain because of the actions of a franchisee,

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228. *Id.* art. 3(2)(i), at 50, *reprinted infra* p. 306.

229. *Id.* art. 3(2)(j), at 50, *reprinted infra* p. 306.

230. *Id.* art. 3(2)(h), at 50, *reprinted infra* p. 306.

231. *Id.* art. 8(e), at 51, *reprinted infra* p. 310.

232. *Id.* art. 3(2)(a), (d), (f), at 49-50, *reprinted infra* pp. 305-06.

233. See *Pronuptia*, *supra* note 35, at 44, ¶ 26, Common Mkt. Rep. (CCH) ¶ 10,854, at 12,043 (provision prohibiting franchisee from using Pronuptia trademark other than in combination with its own business name and followed by words "Franchisee of Pronuptia de Paris" did not fall within Art. 85(1)).

that franchisee may not use the know-how after the termination of the agreement.<sup>234</sup>

Certain positive obligations of collaboration imposed on the franchisee are also considered to be non-restrictive. This is the case for a grantback obligation, i.e., an obligation to communicate to the franchisor any experience gained in the process of exploiting the franchise and to grant the franchisor and the other franchisees a non-exclusive license for any know-how resulting from that experience.<sup>235</sup> An obligation to assist the franchisor in the case of an infringement of the licensed industrial property rights is also considered to be outside the scope of Article 85(1).<sup>236</sup> On the other hand, an obligation on the franchisee not to challenge the validity of the licensed industrial property rights would prevent the application of the Regulation.<sup>237</sup> This does not refer to an obligation on the franchisee to recognize the validity of the industrial property rights at the moment of signature of the contract but only to an obligation not to challenge them during the life of the agreement. Such a no-challenge obligation would place the franchisees at a disadvantage in comparison to their competitors and without justification if some of these rights appeared to be ill-founded, for example, if the franchisor's trademark had become descriptive or generic or if anterior rights exist in the case of a patent. The franchisor must be free to terminate the contract in such a case. Article 3(3) provides that if, because of particular circumstances, the obligations listed in article 3(2) become restrictive of competition, they will also be covered by the block exemption.<sup>238</sup> On these different points, the Franchising Regulation closely parallels the patent-licensing regulation.<sup>239</sup>

The recent *Bayer* judgment<sup>240</sup> does not, in my view, question the fact that a no-challenge obligation normally infringes

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234. Franchising Regulation, *supra* note 22, art. 5(d), at 50, *reprinted infra* p. 307.

235. *Id.* art. 3(2)(b), at 49, *reprinted infra* p. 305.

236. *Id.* art. 3(2)(c), at 50, *reprinted infra* pp. 305-06.

237. *Id.* art. 5(1), at 50, *reprinted infra* pp. 307-08.

238. *Id.* art. 3(3), at 50, *reprinted infra* p. 306.

239. See Comm'n Regulation No. 2349/84 on Patent Licensing, arts. 2(1)(8), 2(1)(10), 3(1), O.J. L 219/15, at 20 (1984), Common Mkt. Rep. (CCH) ¶ 2747, at 1956-57.

240. *La Société Bayer AG v. Süllhöfer*, Case 65/86, 1988 E.C.R. \_\_\_; see Korah, *No Duty to License Independent Repairers to Make Spare Parts: The Renault, Volvo and Bayer*

Article 85(1); it is only in two exceptional circumstances—the granting of a free license or the granting of a license concerning an obsolete technology not used by the licensee—that the Court of Justice has considered that a no-challenge clause was not restrictive of competition. Neither of these situations is likely to occur in the case of franchising.

### CONCLUSION

The adoption of the Franchising Regulation certainly marks a change in the treatment of vertical restrictions under EEC antitrust law. This new approach, however, is consistent with the previous policy. It is interesting, in this respect, to examine the differences among the various existing block exemption regulations and what could be the main consequences, from the point of view of the application of the EEC competition rules, of the transformation of distribution or selective purchasing agreements into franchise agreements, assuming that all the conditions of the Franchising Regulation would be met. The consequences would vary according to the type of pre-existing agreements.

#### A. Exclusive Distribution and Purchasing

The Franchising Regulation would not apply to non-reciprocal agreements between competitors, contrary to Regulations 1983/83 and 1984/83;<sup>241</sup> it would apply without limitation as to the maximum duration of the agreements, contrary to Regulation 1984/83.<sup>242</sup>

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<sup>241</sup> *See Hennecke Cases*, 10 EUR. INTELL. PROP. REV. 381, 384-86 (1988) (very critical of the *Bayer* judgment).

<sup>241</sup>. See Regulation 1983/83, *supra* note 4, art. 3(b), at 3, Common Mkt. Rep. (CCH) ¶ 2730, at 1894. Regulation 1983/83 provides that the block exemption applies to non-reciprocal exclusive distribution agreements between competitors, where at least one of the parties has a total turnover of no more than 100 million ECU. *Id.*; see Regulation 1984/83, *supra* note 4, art. 3(b), at 8, Common Mkt. Rep. (CCH) ¶ 2733, at 1909. Regulation 1984/83 includes the same provision for non-reciprocal exclusive purchasing agreements. The Franchising Regulation, Regulation 1983/83, and Regulation 1984/83 do not apply to reciprocal agreements between competitors.

<sup>242</sup>. See Regulation 1984/83, *supra* note 4, art. 3(d), at 8, Common Mkt. Rep. (CCH) ¶ 2733, at 1909. Article 3(d) provides that it does not apply to agreements concluded for an indefinite duration or for a period of more than five years; in the case of beer supply agreements, article 8(1)(d) stipulates that the maximum period can be 10 years. *Id.* art. 8(1)(d), at 9, Common Mkt. Rep. (CCH) ¶ 2733, at 1911.

The territorial protection granted to the reseller would be similar to what is provided in Regulation 1983/83<sup>243</sup> but more extensive than in Regulation 1984/83.<sup>244</sup> The range of products covered by the exclusive dealing clause would be narrower than in Regulation 1983/83 and similar to what is provided in Regulation 1984/83 in either the general part or the sections relating to beer supply and service stations agreements.<sup>245</sup> The Franchising Regulation allows for a non-competition clause for a period of up to one year after termination of the contract, while both Regulations 1983/83 and 1984/83 exempt a non-competition covenant only during the validity of

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According to article 8(2)(a), where the agreement relates to premises let to the reseller by the supplier, the exemption applies for the whole period for which the reseller operates the premises. *Id.* art. 8(2)(a), at 9, Common Mkt. Rep. (CCH) ¶ 2733, at 1911. Articles 12(1)(c) and 12(2) establish similar provisions for service stations. *Id.* art. 12(1)(c), (2), at 10, Common Mkt. Rep. (CCH) ¶ 2733, at 1912-13.

243. See Regulation 1983/83, *supra* note 4, art. 2(1), at 2-3, Common Mkt. Rep. (CCH) ¶ 2730, at 1893.

244. Regulation 1984/83, *supra* note 4, art. 2(1), at 8, Common Mkt. Rep. (CCH) ¶ 2733, at 1909. No contract territory can be stipulated under Regulation 1984/83. Article 2(1) provides only that the supplier may be obliged not to undertake to distribute the contract products "in the reseller's principal sales area and at the reseller's level of distribution"; this means that the supplier is entitled to supply other resellers in the same area. Regulation 1984/83, *supra* note 4, art. 2(1), at 8, Common Mkt. Rep. (CCH) ¶ 2733, at 1909. On the differences between the territorial protection allowed under Regulations 1983/83 and 1984/84, see Commission Notice, *supra* note 96, at 2, ¶ 4, Common Mkt. Rep. (CCH) ¶ 10,583, at 11,367-68; Schröter, *The Application of Article 85 of the EEC Treaty to Distribution Agreements—Principles and Recent Developments*, in 1984 FORDHAM CORP. L. INST. 375, 416 (B. Hawk ed. 1985).

245. Article 2(e) of the Franchising Regulation exempts an obligation on the franchisee not to manufacture or distribute goods competing with the franchisor's goods that form the essential object of the franchise, with the exception of accessories or spare parts thereof. Franchising Regulation, *supra* note 22, art. 2(e), at 49, *reprinted infra* p. 304. Article 2(2)(a) of Regulation 1983/83 exempts the obligation on the reseller not to manufacture or distribute goods competing with the contract goods, without any limitation as to the range of these products. Regulation 1983/83, *supra* note 4, art. 2(2)(a), at 3, Common Mkt. Rep. (CCH) ¶ 2730, at 1893. Article 2(2) of Regulation 1984/83 exempts a similar restriction, but article 3(c) of the same Regulation excludes the application of the block exemption when the exclusive purchasing obligation relates to several products that are not linked together either by their nature or according to commercial use, while articles 6(1)(a) and 11(a) respectively exempt the obligation not to sell beer or other drinks in one case and motor vehicle fuel and other fuels in the other, i.e., the main products covered by the agreement, which are supplied by other undertakings. Regulation 1984/83, *supra* note 4, arts. 2(2), 3(c), 6(1), 11(a), at 8-10, Common Mkt. Rep. (CCH) ¶ 2733, at 1909-10, 1912.

the agreement.<sup>246</sup> However, it should be stressed that the Franchising Regulation does not cover an exclusive purchasing obligation that is exempted by Regulation 1983/83<sup>247</sup> and forms the main object of agreements covered by Regulation 1984/83,<sup>248</sup> as the franchisees should always be free to purchase from other franchisees or other distributors within other channels of distribution supplied by the manufacturer or with its consent.

### B. *Selective Distribution*

Restrictions resulting from selective distribution systems are only acceptable for certain products. According to the Court of Justice, it is necessary to examine whether the properties of the product require a selective distribution system to preserve the product's quality and ensure that it is used correctly.<sup>249</sup> The Commission has, for instance, refused to exempt agreements concerning plumbing fittings, noting that the characteristics of these products do not require a selective distribution system.<sup>250</sup> The Court of Justice did not establish a similar condition for franchise agreements in the *Pronuptia* case<sup>251</sup> and the Franchising Regulation does not include any limitation of that nature.

Until now, it has been accepted only for motor vehicle distribution that selective distribution agreements could be based

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246. Compare Franchising Regulation, *supra* note 22, art. 3(1)(c), at 49, *reprinted infra* p. 305 with Regulation 1983/83, *supra* note 4, art. 2(2)(a), at 3, Common Mkt. Rep. (CCH) ¶ 2730, at 1893 and Regulation 1984/83, *supra* note 4, arts. 2(2), 7(1)(a), 11(a), at 8-10, Common Mkt. Rep. (CCH) ¶ 2733, at 1909-12.

247. Regulation 1983/83, *supra* note 4, art. 2(2)(b), at 3, Common Mkt. Rep. (CCH) ¶ 2730, at 1893 (providing that supplier impose on distributor "the obligation to obtain the contract goods for resale only from the other party . . .").

248. See Regulation 1984/83, *supra* note 4, arts. 1, 6, 10, at 7, 9-10, Common Mkt. Rep. (CCH) ¶ 2733, at 1908, 1910, 1912.

249. See, e.g., *Lancôme v. Etos*, Case 99/79, 1980 E.C.R. 2511, 2536, ¶ 20, Common Mkt. Rep. (CCH) ¶ 8714, at 8593.

250. See *Ideal Standard*, O.J. L 20/38, at 41-42, ¶ 15 (1985), Common Mkt. Rep. (CCH) ¶ 10,662, at 11,574-75; *Grohe*, O.J. L 19/17, at 20-21, ¶ 15 (1985), Common Mkt. Rep. (CCH) ¶ 10,661, at 11,565-66. Demaret considers that these cases present "intriguing horizontal aspects," as two leading manufacturers adopted the same marketing policy. However, the motivation of the two decisions does not address that question. Demaret, *supra* note 130, at 173.

251. The Court considered only that the characteristics of certain products might justify exclusive dealing obligations. *Pronuptia*, Case 161/84, 1986 E.C.R. 353, 387, ¶ 33, Common Mkt. Rep. (CCH) ¶ 14,245, at 16,441.

on a quantitative selection of the dealers<sup>252</sup> and include an obligation to deal exclusively in the manufacturer's products.<sup>253</sup> For other sectors, selective distribution agreements have been considered as acceptable only if they were based on qualitative selection criteria: agreements based on simple objective qualitative criteria do not fall under Article 85(1),<sup>254</sup> while agreements including additional restrictions, such as a minimum turnover requirement, may obtain exemptions if they are applied in a non-discriminatory manner.<sup>255</sup>

In sectors other than motor vehicle distribution, the transformation to franchise agreements would permit a quantitative selection of the franchisees, because the Regulation exempts an obligation on the franchisor to appoint only one franchisee in a given territory;<sup>256</sup> it also makes it possible to give a territorial protection to the franchisees<sup>257</sup> and to impose exclusive dealing and non-competition obligations.<sup>258</sup>

### C. Motor Vehicle Distribution

In the area of motor vehicle distribution, contrary to Regulation 123/85, the Franchising Regulation does not impose conditions relating to the protection of the dealers, such as a minimum duration of the agreements<sup>259</sup> or specific rules for the calculation of discounts.<sup>260</sup> As far as the interests of the users are concerned, the Franchising Regulation does not in-

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252. See, e.g., *Bayerische Motoren Werke*, *supra* note 41, at 4-5, 6-7, ¶¶ 13, 24, Common Mkt. Rep. (CCH) ¶ 9701, at 9539-7 to 9539-10 (specifying that quantitative selection was only accepted, because motor cars are products of considerable value, utilization of which can jeopardize life, health, and material goods and affect the environment); see also Regulation 123/85, *supra* note 42, art. 1, at 19-20, Common Mkt. Rep. (CCH) ¶ 2751, at 1973.

253. See *Bayerische Motoren Werke*, *supra* note 41, at 5, 7, ¶¶ 18, 28, Common Mkt. Rep. (CCH) ¶ 9701, at 9539-8, 9539-11; see also Regulation 123/85, *supra* note 42, recitals 7, 8, arts. 3(3), 5(2), at 17, 20-21, Common Mkt. Rep. (CCH) ¶ 2751, at 1970, 1974, 1976-77.

254. See, e.g., *Metro v. Commission*, Case 26/76, 1977 E.C.R. 1875, 1904, ¶ 20, Common Mkt. Rep. (CCH) ¶ 8435, at 7850.

255. See, e.g., *id.* at 1913, ¶ 37, Common Mkt. Rep. (CCH) ¶ 8435, at 7854.

256. See Franchising Regulation, *supra* note 22, art. 2(a), at 49, *reprinted infra* p. 304.

257. See *id.* art. 2(d), at 49, *reprinted infra* p. 304.

258. See *id.* arts. 2(a), 2(e), 3(1)(c), at 49, *reprinted infra* pp. 304-305.

259. See Regulation 123/85, *supra* note 42, art. 5(2)(2), at 22, Common Mkt. Rep. (CCH) ¶ 2751, at 1977.

260. See *id.* art. 5(1)(2)(c), at 21, Common Mkt. Rep. (CCH) ¶ 2751, at 1976.

clude a condition relating to an obligation on the franchisee to honor guarantees and to perform free servicing,<sup>261</sup> but it does provide that where such a guarantee exists, it must be applied in a non-discriminatory way.<sup>262</sup> The practical result is the same, however, because all motor vehicle manufacturers grant a manufacturer's guarantee for their products. The Franchising Regulation also does not include as a condition an obligation on the manufacturer (franchisor) to supply a distributor (franchisee), following a customer's request, with goods corresponding to the norms applicable where the customer intends to use the goods.<sup>263</sup> However, the Franchising Regulation does not apply when the franchisees are obliged not to supply the goods or services that are the subject of the franchise to end-users because of their place of residence.<sup>264</sup> It is also provided that the benefit of the exemption can be withdrawn when the parties prevent the end-users from obtaining the goods that are the subject of the franchise because of their place of residence or if they use the differences in specifications concerning these goods or services in different Member States to isolate markets.<sup>265</sup> Unlike Regulation 123/85, the Franchising Regulation does not stipulate that an intermediary acting on behalf of an end-user should comply with specific formalities such as obtaining a prior written authority from the user.<sup>266</sup> The franchisees must be free to sell to end-users, whether they act through intermediaries or not.

The scope of the admissible exclusive dealing clause during the duration of the contract is similar in both Regulations. The motor vehicle regulation refers to an obligation not to sell new motor vehicles other than those within the contract program<sup>267</sup> and not to sell or use competing spare parts that do

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261. Regulation 123/85 does, however, include such a provision. *Id.* art. 5(1)(1)(a), at 21, Common Mkt. Rep. (CCH) ¶ 2751, at 1976.

262. Franchising Regulation, *supra* note 22, art. 4(b), at 50, *reprinted infra* pp. 306-07.

263. See Regulation 123/85, *supra* note 42, art. 5(1)(2)(d), at 21, Common Mkt. Rep. (CCH) ¶ 2751, at 1976.

264. See Franchising Regulation, *supra* note 22, art. 5(g), at 50, *reprinted infra* p. 308.

265. *Id.* art. 8(c), at 51, *reprinted infra* p. 310.

266. See Regulation 123/85, *supra* note 42, art. 3(11), at 20, Common Mkt. Rep. (CCH) ¶ 2751, at 1974-75.

267. See *id.* art. 5(2), at 21-22, Common Mkt. Rep. (CCH) ¶ 2751, at 1976-77. This assumes that the dealer has accepted the obligations for the improvement of

not match the quality of the contract goods.<sup>268</sup> The corresponding provisions of the Franchising Regulation refer to goods competing with the franchisor's goods that are the subject of the franchise, with the exception of accessories or spare parts for which only an obligation to match minimum objective quality specifications laid down by the franchisor could be imposed.<sup>269</sup>

The Franchising Regulation also considers as non-restrictive a non-competition provision that applies after the termination of the agreement for a reasonable period not exceeding one year.<sup>270</sup> This is an important difference from Regulation 123/85, which only exempts, for a maximum period of one year after termination of the agreement, obligations relating to the contract goods, such as obligations not to modify the goods or sell them to resellers outside the distribution system.<sup>271</sup> However, the notion of "reasonable period" depends on the value of the know-how to be protected and can be quite short if the dealer was already experienced before concluding the franchise agreement. Therefore, in the case of car dealers that were already established in that sector before they became franchisees, it is likely that a post-term competition ban would be considered as reasonable only for a period of two to three months.

Because the differences between the franchising block exemption and other block exemptions result from the different natures of the agreements in question, the transformation of certain distribution networks into franchises should not have any negative effect on overall competition. This might be different if in certain sectors nearly all manufacturers were to adopt similar franchising systems. It should be remembered that the Commission may withdraw the benefit of the exemption where an agreement covered by the Regulation, nevertheless, has effects incompatible with Article 85(3) of the Treaty.

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distribution and servicing structures stipulated in article 4(1), which are similar to what is normally found in a franchise agreement. *See id.* art. 4(1), at 20, Common Mkt. Rep. (CCH) ¶ 2751, at 1975.

268. *Id.* art. 3(4), at 20, Common Mkt. Rep. (CCH) ¶ 2751, at 1974.

269. Franchising Regulation, *supra* note 22, arts. 2(e), 3(1)(a), at 49, *reprinted infra* p. 304.

270. *Id.* art. 3(1)(c), at 49, *reprinted infra* p. 305.

271. *See* Regulation 123/85, *supra* note 42, art. 3(12), at 20, Common Mkt. Rep. (CCH) ¶ 2751, at 1975.

Article 8(a) of the Regulation specifically refers, in that respect, to a situation where competition or access to the market is restricted because of the cumulative effect of parallel networks of similar agreements.<sup>272</sup>

The new Franchising Regulation will give greater legal certainty to enterprises, because they will know what provisions they can or cannot insert in their franchise contracts, without the need to notify the Commission. In case of doubt, the opposition procedure will make it possible for undertakings to have a rapid answer as to the validity of their agreements. The Regulation should, therefore, favor the development of franchising agreements in the Community, which would result in considerable economic benefits, in particular for small- and medium-sized enterprises. Its adoption coincides with the adoption of the block exemption regulation on know-how agreements.<sup>273</sup> Together with the other block exemptions already adopted, they form a coherent body of legislation aimed at giving more legal certainty.

The Community approach of adopting block exemption regulations has sometimes been criticized as being too rigid and artificial. It has been argued that it would be preferable to apply, as in the United States, a rule-of-reason analysis to vertical restrictions. It is true that the block exemption method is somewhat Procrustean, but it has the merit of clarity. It should not be overlooked that the aims of antitrust policy are not the same in the United States as in Europe, where the goal of market integration is an important aspect of competition policy. Furthermore, the consequence of the particular structure of Article 85 is that a rule-of-reason type analysis can only be made under paragraph 3 of that Article after notification to the Commission.<sup>274</sup> It is interesting, in that respect, to note that Professor Hawk, in his treatise on United States and Common Market antitrust, argues that in U.S. law, vertical restrictions should be given a rebuttable presumption of illegality in a way similar to Article 85, where such agreements are presumed to violate Article 85(1) and may be exempted under Article 85(3)

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272. Franchising Regulation, *supra* note 22, art. 8(a), at 51, *reprinted infra* p. 310.

273. Know-How Regulation, *supra* note 72.

274. For a comparison of the analysis under Article 85(3) with a rule-of-reason analysis under section 1 of the Sherman Act, see 2 B. HAWK, UNITED STATES, COMMON MARKET AND INTERNATIONAL ANTITRUST 109-12 (2d ed. 1987).

only upon a showing of increased efficiency.<sup>275</sup> Block exemption regulations avoid the need for notification and individual exemptions and also avoid the burdensome litigation involved in the application of the rule of reason. For agreements fulfilling the conditions set out in a block exemption regulation, it is only where, because of particular circumstances, the positive effects on competition are not present, that an individual examination must be made in order to withdraw the benefit of the exemption.

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275. *See id.* at 311.