

Understanding Franchise Agreement Relationship & Termination Laws

BASED ON THE A SUMMARY OF FEDERAL AND STATE FRANCHISE RELATIONSHIP AND TERMINATION LAWS.

“This is a quick summary of the Relationship and Termination provisions of federal and state requirements. For an in-depth analysis of the specific requirements applicable to you, please contact Mohajerian Law Corp. at www.mohajerianlaw.com. This newsletter is not intended to be legal advice and is for informational purposes only.”

Franchise relationship and termination laws deal directly with conduct in the context of an existing franchise agreement. Generally agreed upon is the concern by legislatures regarding franchises being wrongfully terminated or dominated unfairly by large franchisors and distributors. The conduct of concern has been discrimination, franchisor competition, market encroachment, and dilution.

What do Termination, Cancellation, and Nonrenewal Really Mean?

The act of ending a franchise relationship is deemed a “termination,” “cancellation,” or “nonrenewal.” While “termination” and “cancellation” generally refer to ending a relationship during its intended term, “nonrenewal” generally means the end of a franchise agreement at expiration. Often times, the franchise agreement will outline the grounds for termination or cancellation. As well, the basis for renewal a signified in the franchise agreement.

Regardless of the terms set forth, the franchise relationship and termination laws set standards that franchisors must follow to avoid successful legal action on the part of a franchisee. It is important that careful consideration by franchisors be made to comply with law of their applicable jurisdiction.

How is Alteration Different?

In addition to termination, cancellation, and nonrenewal some franchise relationship and termination laws govern changes to franchise agreements otherwise known as alterations. For example, under Section 1 of the Indiana Deceptive Franchise Practices Law, it is unlawful for a franchise agreement to provide for or allow substantial modification of the franchise agreement

What Do Termination, Cancellation, and Nonrenewal Really Mean?

How is Alteration different?

Are There Standards of Conduct for Franchisors?

What is a Change of Competitive Circumstances?

by the franchisor without written consent of the franchisees. However, the change may have to be proven to be “substantial.” In *Wright-Moore Corp. v. Ricoch Corp.* a photocopier manufacturer’s unilateral change in credit terms for the sale of copiers to a distributor, as authorized by the distributorship agreements, was held not to be a substantial change due to the lack of resulting harm to the distributorship’s business.

Are There Standards of Conduct for Franchisors?

Under the franchise relationship and termination laws, a common requirement of conduct specifies that franchisors must act “fairly,” “justly,” or with “good cause.” These standards apply variously in attempts by franchisors at termination, cancellation, nonrenewal, alterations, and sometimes changes in competitive circumstances. For example, the “good cause” standard, in most states, applies to termination, cancellation, and nonrenewal. However, under Section 20 of the Illinois Franchise Disclosure Act of 1987, the “good cause” standard does not apply to nonrenewal. In other cases, the “good cause” is defined precisely, as with the Iowa Code, Title XX, Section 523H.7 which defines “good cause” to be:

“The failure of the franchisee to comply with a lawful requirement of the franchise agreement, provided that the termination by the franchisor is not arbitrary or capricious when compared to the actions of the franchisor in other similar circumstances. In addition, the burden of proof rests with the franchisee.”

What is a Change of Competitive Circumstances?

As noted the conduct of franchisors towards franchisees requires some level of “good cause” in connection with termination, cancellation, and nonrenewal. Some states require “good cause” for what is termed a “change in competitive circumstances.” For example, Wisconsin’s Fair Dealership Law makes this requirement.

However, the question of what constitutes a “change in competitive circumstances” has been the subject of considerable litigation. A variety of activities have been found to fall under the definition. These have included, for example, inadequate advertising, imposition of a discount for case program, change of distributorship to a non-exclusive basis, ineffective managements, installation of other distributorships in territory, bans on mail order sales, and withdrawal from the market.

Still in some cases, fairly substantial changes imposed by a franchisor have been held not to have substantially changed the franchisee’s competitive circumstances. In *Bresler’s 33Flavors Franchising Corp. v. Wokosin*, an ice cream franchisors imposition of a new standard agreement on a Wisconsin franchisee – requiring remodeling, advertising, and increased franchise fee – did not substantially change the franchisee’s competitive circumstances.

General Recommendations

Understanding and complying with the complex nature of franchise relationship and termination laws can be quite a challenge for most franchisors. The best advice you can receive is to make

sure you fully understand and comply with all applicable laws regarding your business. In most cases, review and counseling from an experienced franchise lawyer is the best way to ensure your compliance.

Mohajerian Law Corp. encourages you to contact our firm with questions or concerns regarding the franchise relationship and termination laws that are applicable to you. We proudly serve franchisors and franchisees in their quest for sound, prudent legal counseling.