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Foreign Competition Laws and Their Effect On Transnational Franchise Relationships

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I. INTRODUCTION

Most U.S. based franchise attorneys know that competition law has a long-standing relationship with franchise legislation and litigation in the United States, and there is a treasure trove of case law from the U.S. common law framework to analyze, compare and contrast alleged anti-competitive conduct against the law and its various interpretations. However, international competition law comes in many forms, and when U.S. franchisors enter into foreign markets, they are sometimes surprised to find that foreign competition laws can vary widely from competition law the United States in terms of coverage, application, practical relevance and enforcement, especially where the scope of coverage of some competition laws can be extremely broad and the availability of practical guidance extremely limited.

This paper provides an overview of key foreign competition law across a broad swath of territory, specifically, Europe, North America and Latin America (including Brazil and Mexico), and Asia, the Pacific and the Mid-East (including Australia, China, the Gulf Cooperation Council countries and several other key jurisdictions). For each geographic area, the paper provides a general overview of the competition law itself and then focuses on three key areas of competition law, namely retail price maintenance, sourcing restrictions and exclusivity/non-competition covenants. While the paper provides an overview of the specific competition law tenets in the covered jurisdictions, the goal is to discuss the practical application and realistic business and legal options that must be analyzed when considering how these laws apply to franchise transactions as well as the requirements for compliance with these laws and the practical consequences and enforcement realities of noncompliance.

II. EUROPE

A. European Union Competition Law

The European Union (EU) is an economic and political union of 28 member states that are located primarily in Europe. To be expected, the regulation of competition among and within the members states has been a primary source of contention, and competition law dates back to the original Treaty of Rome that was a precursor to the founding of the EU.

Today, competition law within the European Union is mainly governed by the Treaty on the Functioning of the European Union (TFEU). Article 101 of the TFEU broadly prohibits agreements and other concerted practices, which have as their object or effect the prevention, restriction or distortion of competition. Article 102 of the TFEU prohibits the abuse of a

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2 We use the phrase ‘competition law’ throughout this paper to cover what in some jurisdictions may be more commonly known as antitrust law, anti-monopoly law, consumer protection law or other similar nomenclature.

3 As of July 2013, the European Union consists of: Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and United Kingdom. An updated list of all Member States is available at: http://europa.eu/about-eu/countries/index_en.htm. Each website cited in this paper was last visited between May and July of 2013.

4 Treaty establishing the European Economic Community (Rome, 25, March 1957).


6 Id. art. 101.
dominant position within the internal market.\textsuperscript{7} The focus in this paper is on Article 101(1) of the TFEU.

Article 101(1) of the TFEU prohibits all agreements between undertakings,\textsuperscript{8} decisions by associations of undertakings and concerted practices which may affect trade between member states and which have as their object or effect the prevention, restriction or distortion of competition within the internal market.\textsuperscript{9} Article 101(1) of the TFEU seeks to ensure that undertakings independently determine their business’s policy on the Internal Market.\textsuperscript{10} Prohibited activities include price fixing, territorial restrictions and market allocations.

Agreements or decisions that are made in violation of Article 101(1) of the TFEU are deemed to be automatically void pursuant to Article 101(2) of the TFEU. Article 101(3) of the TFEU, in conjunction with Article 1(2) Regulation 1/2003, provides an opportunity for exemption from the prohibition of Article 101(1) of the TFEU. An agreement is exempted if the following requirements are fulfilled:

(a) the agreement must contribute to the improvement of the production or distribution of goods or to promoting technical or economic progress,

(b) the agreement must allow consumers a fair share of the resulting benefit,

(c) the agreement may not impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives,

(d) the agreement may not afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.\textsuperscript{11}

Importantly, the Commission has adopted Block Exemption Regulations\textsuperscript{12} to facilitate the assessment of agreements that may run afoul of the express prohibitions under the TFEU. If an agreement falls within the scope of a Block Exemption Regulation (BER), it is deemed to satisfy the requirements of Article 101(3) of the TFEU. If no BER is applicable, the undertaking has to assess whether the requirements of Article 101(3) of the TFEU are satisfied on an individual basis. It is the undertaking’s duty to self-assess if its conduct meets either the requirements of a BER or of Article 101(3) of the TFEU. A prior decision by the Commission to that effect is not required (Article 1(2) Regulation 1/2003). Decisions by the Commission concerning franchise systems are, therefore, rare. Such decisions were mostly decided in the late 1980’s, when it was possible to obtain a decision of negative clearance or exemption.\textsuperscript{13}

A franchise agreement’s compliance with European Union Competition law thus needs to be assessed in two steps:

\textsuperscript{7} Id. art. 102.

\textsuperscript{8} An “undertaking” is an entity or person (i.e., a contracting party) under European Union parlance.

\textsuperscript{9} TFEU, supra note 5 at art. 101.

\textsuperscript{10} TFEU, supra note 5 at art. 101(3).

\textsuperscript{11} The BER relevant to franchising is the Commission Regulation 330/2010 of 20 April 2010 on the application of Article 101(3) of the TFEU to categories of vertical agreements and concerted practices, which is discussed below.

(1) Does the franchise agreement restrict competition?

(2) Is it exempt from the prohibition of Article 101(1) of the TFEU, because it fulfills the criteria of a BER or Article 101(3) of the TFEU itself?

The burden of proof that the agreement restricts competition (step 1) is on the agency or party claiming that the franchise agreement violates Article 101(1) of the TFEU, whereas the burden of proof for the claim that the criteria of a BER or Article 101(3) (step 2) are fulfilled lies with the party claiming that the agreement is valid.

1. European Union Structure

The TFEU is applicable to all member states of the European Union, and applicability is neither conditioned upon the adoption of these provisions into national laws nor a prior decision by a competition authority (Articles 1 and 3(1) Regulation 1/2003). Therefore, the competition authorities of the member states are to directly apply the provisions of the TFEU.

The Agreement on the European Economic Area (EEA) contains identical provisions in its Articles 53-54. Therefore the legislative regime is comparable in Iceland, Liechtenstein and Norway. Switzerland which has not ratified the EEA Agreement has also signed a similar agreement.

Article 3(2) Regulation 1/2003 prevents the application of national competition laws in cases in which it would lead to the prohibition of agreements, decisions by associations of undertakings or concerted practices, which may affect trade between member states but do not violate Article 101 of the TFEU, either because they do not restrict competition or because they are exempt from Article 101(1) of the TFEU as they fulfill the conditions of Article 101(3) of the TFEU. Article 101 thus takes precedence over national competition laws, if the agreement may affect trade within the EEA.

Trade is not limited to the exchange of goods and services but also encompasses agreements which merely affect the competitive structure of the market. Such competitive structure may be affected, if a sufficient degree of probability leads to the assumption of an appreciable influence on the pattern of trade between member states. The capability to affect trade is sufficient. The European Court of Justice (E.C.J.) has therefore held that franchise agreements that allocate markets are "in any event liable to affect trade between Member States, even if they are entered into by undertakings established in the same Member State, in so far as they prevent franchisees from establishing themselves in another Member State."

Therefore, with regard to franchise agreements that may affect trade within the EEA, it is only necessary to evaluate whether the franchise agreements comply with the requirements set forth in Article 101 of the TFEU (or Article 53 EEA-Agreement respectively). An assessment according to national competition laws is only necessary if the franchise agreement may not

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14 Agreement between the European Economic Community and the Swiss Confederation, 1972 O.J.SPEC.ED. (L 300) 191-282 (hereinafter "EEC Swiss Agreement").
15 These are the so called EFTA States, Art. 2(b) EEA-Agreement.
16 EEC Swiss Agreement, cited supra note 14. As of July 2013, the conclusion of a cooperation agreement is pending.
18 See further id. at para 19-57.
19 Id. at para 26.
affect trade between Member States or EEA states. The allocation of cases between the European Commission and the EFTA Surveillance Authority is governed by Article 56 EEA-Agreement. As a rule of thumb, the EFTA Surveillance Authority decides those cases which mainly or solely affect the trade between the EFTA states.21

2. Pronuptia and Vertical Restraints Block Exemption Regulations

The E.C.J. has held in its landmark case, Pronuptia, that provisions that are essential for the functioning of a franchise system do not constitute restrictions on competition for the purposes of Article 101(1) of the TFEU.22 In this case the franchisor, Pronuptia de Paris GmbH, which distributes wedding dresses, claimed outstanding license fees from the franchisee, Mrs. Schillgalis, who operated a franchised store in Hamburg, Germany. Mrs. Schillgalis defended herself against the claim stating that the franchise contracts were void, because they violated competition law. The Federal Court of Justice of Germany asked the E.C.J. for a preliminary ruling on the applicability of Article 101(1) of the TFEU.23 The E.C.J. denied the applicability of Article 101(1) of the TFEU to those provisions which are essential for the functioning of a franchise system. It considered two categories of provisions essential for the functioning of a system that therefore do not constitute restrictions of competition for the purposes of Article 101(1) of the TFEU:

(a) First, those provisions that ensure that a franchisor can communicate know-how and provide assistance without running the risk that such know-how or assistance benefits competitors.24

(b) Second, measures taken by the franchisor which are necessary to maintain the identity and reputation of the network.25

Provisions essential to secure that know-how does not benefit competitors include non-compete clauses and provisions requiring the franchisor’s consent prior to the transfer of the franchisee’s undertaking to a third party.26

Essential provisions with regard to maintaining the identity and reputation of a franchise system include the franchisee’s obligation to use the know-how provided and business method developed by the franchisor as well as restrictions imposed on the location and design of the franchisee’s unit.27 The E.C.J. also deems clauses that ensure the franchisor’s right to freely choose its franchisees to be necessary to maintain the reputation of the franchise system.28 Clauses prohibiting the franchisees from sourcing products or services from unapproved suppliers and limiting advertising opportunities may be essential in certain cases as well.29

If a franchise agreement falls within the scope of Article 101(1) of the TFEU, it may still comply with competition law. When assessing franchise agreements, special consideration has to be given to the Vertical Agreements Block Exemption Regulation (VA-BER).30 The VA-BER is applicable to different types of vertical agreements such as agency, selective distribution and

21 See art. 56 EEA Agreement for details on the case allocation.
22 Pronuptia supra note 13 at para 16-27.
23 Id. at para 8.
24 Id. at para 16.
25 Id. at para 17.
26 Id. at para 16.
27 Id. at para 18-19.
28 Pronuptia supra note 13 at para 20.
29 Id. at para 21-22.
exclusive distribution. It replaced the Franchise Block Exemption Regulation, which franchise practitioners may remember was the applicable regulation for a number of years. Vertical agreements are exempt from the prohibition of Article 101(1) of the TFEU if the market shares of the parties to the agreement do not exceed 30% and if the agreement does not contain any so called “hardcore-restrictions.” The VA-BER thus creates a “safe harbor” for all agreements that fall within its scope.

A “Vertical Agreement” is defined as “an agreement or concerted practice entered into between two or more undertakings each of which operates, for the purposes of the agreement or the concerted practice, at a different level of the production or distribution chain, and relating to the conditions under which the parties may purchase, sell or resell certain goods or services.” Different types of franchise agreements – especially commercial and distribution agreements – may benefit from the VA-BER. Industrial franchise agreements (i.e., franchises relating to the manufacturing of goods), however, do not necessarily qualify for the exemption. If the agreement’s primary objective is to assign or grant access to intellectual property rights, it may, however, fall in the scope of a different BER, namely the Technology Transfer BER (TT-BER).

To help assess compliance with the VA-BER, and avoid repercussions under the TFEU, the European Commission has set forth certain obligations in its Guidelines on Vertical Restraints that it deems necessary to protect the franchisor’s intellectual property rights and which therefore fall under the block exemption and can be contained in agreements. These are:

- **(a)** an obligation on the franchisee not to engage, directly or indirectly, in any similar business;
- **(b)** an obligation on the franchisee not to acquire financial interests in the capital of a competing undertaking such as would give the franchisee the power to influence the economic conduct of such undertaking;
- **(c)** an obligation on the franchisee not to disclose to third parties the know-how provided by the franchisor as long as this know-how is not in the public domain;
- **(d)** an obligation on the franchisee to communicate to the franchisor any experience gained in exploiting the franchise and to grant the franchisor, and other franchisees, a non-exclusive license for the know-how resulting from that experience;

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32 VA-BER, supra note 30 at art. 2(1).
33 Id. at art. 3(1).
34 Id. at art. 4. Note that a hard core restriction leads to the nullification of the entire franchise agreement. See Commission Notice: Guidelines on Vertical Restraints, 2010 O.J. (C 130) 1, para 70 (hereinafter “Vertical Guidelines”).
35 Id. at para 23.
36 Id. at art. 1(1).
37 Id. at para 45; Franck Wijckmans & Filip Tuyschaever, Vertical Agreements in EU Competition Law, (2d ed. 2011), para 6.75 (hereinafter “Wijckmans”).
40 Vertical Guidelines supra note 34 at para 45.
(e) an obligation on the franchisee to inform the franchisor of infringements of licensed intellectual property rights, to take legal action against infringers or to assist the franchisor in any legal actions against infringers;

(f) an obligation on the franchisee not to use know-how licensed by the franchisor for purposes other than the exploitation of the franchise;

(g) an obligation on the franchisee not to assign the rights and obligations under the franchise agreement without the franchisor’s consent.41

3. Resale Price Maintenance

Resale price maintenance constitutes a hardcore restriction pursuant to Article 4(a) of the VA-BER, which states that the exemption will not apply to “[t]he restriction of the buyer’s ability to determine its sale price, without prejudice to the possibility of the supplier to impose a maximum sale price or recommend a sale price, provided that they do not amount to a fixed or minimum sale price as a result of pressure from, or incentives offered by, any of the parties.”

The Commission defines resale price maintenance as measures which directly or indirectly intend to establish a fixed or minimum resale price or resale price level.42 Agreements that contain resale price maintenance measures are presumed to infringe Article 101(1) of the TFEU and do not fall within the scope of the VA-BER.43 The Commission also considers an individual exemption to be unlikely, it does however identify three situations in which resale price maintenance may be permissible while fulfilling the criteria of Article 101(3) of the TFEU,44 namely:

(a) Efficiencies may firstly arise with the launch of a new product. Fixed prices can provide the distributors with the means to increase sales efforts and can thus serve as an incentive to increase demand for the product, which will ultimately benefit consumers.45 It is, however, necessary that the increase in demand cannot be accomplished by imposing effective promotion requirements on the distributors.46

(b) Fixed prices may secondly also benefit the consumers if they are set for a coordinated short term low price campaign. The Commission explicitly mentions franchise systems as potential beneficiaries of this possibility and considers two to six weeks as an appropriate time frame for most cases.47

(c) Finally, resale price maintenance may help to prevent free-riding at the distribution level. It is necessary that the distributors benefiting from guaranteed prices use their (additional) margins to improve their service; the Commission, therefore, does not deem it sufficient to demonstrate the possibility of improved services but states that it is necessary to demonstrate an incentive to do so.48 Free-rider issues mainly arise with expensive and complex

41 Id. at para 45(a)-(g).
42 Vertical Guidelines supra note 34 at para 223; for examples see id. at para 48.
43 Id. at para 223.
44 Id. at para 223-229.
45 Id. at para 225.
46 Id. at para 225 note 1.
47 Id. at para 225.
48 Vertical Guidelines supra note 34 at para 225.
products. The exemption, therefore, will not be applicable in markets whose products neither require prior consultation nor other customer services.

Resale price recommendations are not per se a form of resale price maintenance. The E.C.J. has held in Pronuptia that price guidelines do not restrict competition, “so long as there is no concerted practice between the franchisor and the franchisees or between the franchisees themselves for the actual application of such prices.” Price recommendations and maximum resale prices do not raise competition concerns as long as they do not have the same effect as fixed prices. A combination of recommendations with threats – e.g. termination of contract – or incentives – such as rebates – to ensure that franchisees follow these recommendations may therefore violate Article 101(1) of the TFEU.

The European Courts affirmed these considerations in later decisions. For example, in JCB Service v. Commission, the setting of a price scale had been found not to violate Article 101(1) of the TFEU. The price scale had not been binding and it has not been proven that the price scale had a coercing effect. In the Volkswagen case, the Commission fined the company for sending several circular letters to its German dealers, urging them not to sell the new “Passat” car model at a price considerably below the recommended resale price and/or to limit or not to grant discounts to customers.

4. Exclusivity, Territories and Non-Competition

Many franchise agreements provide for certain exclusive rights for franchisees and certain retained or exclusive rights for the franchisor. This exclusivity can take the form of exclusive supply rights where the franchisor is obligated only or mainly to sell the contract goods to a single or limited number of franchisees. These type of exclusive supply provisions fall within the scope of the VA-BER and are thus exempt from Article 101(1) of the TFEU, but only if neither party’s market share exceeds 30 percent. The reverse obligation (i.e., the franchisees' obligation to exclusively purchase goods from the franchisor or a specified supplier) is discussed below under “Product Sourcing”.

The E.C.J. has considered provisions within franchise agreements that lead to an allocation of markets to fall within the scope of Article 101(1) of the TFEU even though it recognizes that they may lead to efficiencies as they may create an incentive to invest. Territorial restrictions, therefore, need to be assessed by evaluating whether such restrictions fall within the scope of a BER or if they fulfill the criteria of Article 101(3) of the TFEU on an individual basis. Territorial restrictions generally constitute a hardcore restriction (Article 4(b)

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49 Cf. id. at para 225.
50 Pronuptia supra note 13 para 25.
51 Vertical Guidelines supra note 34 at para 48.
53 JCB Service supra note 52.
54 Id. at para 130.
55 Commission Decision of 26 June 2001 relating to a proceeding under Article 81 of the EC Treaty (Case COMP/F-2/36.693 – Volkswagen) 2001 O.J. L262/14 (this decision was later overturned since the Commission did not sufficiently prove that an agreement was concluded in Case No. T-208/01, Volkswagen v. Commission, 2003 E.C.R. II-5141 (C.F.I.).
56 Id. at para 192; Wijckmans supra note 37 at para 6.97.
57 Vertical Guidelines supra note 34 at para 152.
VA-BER). They can, however, still benefit from the VA-BER, if they fulfill the criteria of one of the exceptions enumerated in Article 4(b) of the VA-BER.\(^{58}\)

Since the VA-BER does not contain franchise-specific provisions, territorial restrictions in franchise agreements must be evaluated according to the type of distribution system used by the respective franchise system. Franchise systems need to be categorized into exclusive/non-exclusive and selective/non-selective systems to assess compliance with the VA-BER.\(^{59}\)

Territorial restrictions in selective franchise systems (i.e., systems where goods and services are sold to specific franchises and/or specific customers based on identifiable criteria) are not exempt by the VA-BER. Franchisees may therefore need to remain free to actively and passively\(^{60}\) sell to end users and other franchisees regardless of the customer’s or franchisees’ location.\(^{61}\) The franchisor can, however, prevent the franchisees from operating out of an unauthorized location.\(^{62}\)

Exclusive distribution agreements generally fall within the scope of the VA-BER, if neither party’s market share exceeds 30 percent.\(^{63}\) Franchise agreements based on exclusivity may limit the franchisee’s ability to actively sell into territories reserved for other franchisees or the franchisor.\(^{64}\) This limitation may not restrict the resale of the products by the franchisee’s customers.\(^{65}\)

In the case of a combination of selective and exclusive distribution, members of the system must be able to actively sell into non-exclusive territories.\(^{66}\) It must be noted that such a combination cannot be agreed upon for the same territory as it would lead to a hardcore restriction.\(^{67}\) The assessment of combinations of exclusive and non-exclusive distribution agreements is similar to that of combinations of exclusive and selective distribution. In these cases active sales can only be prohibited for those territories in which an exclusive distribution system is used. Territorial restrictions can, therefore, only be imposed if the franchise system’s approach to exclusivity differs,\(^{68}\) for example, an exclusive system in one member state of the European Union and a non-exclusive system in another. In this case, the franchisees in the non-exclusive member state may be prevented from actively selling into the areas reserved for exclusive distribution. The franchisees in the territories with exclusive distribution remain free to actively and passively sell into the non-exclusive territories.

In recent years territorial restrictions became more and more relevant as they also relate to bans of online sales. Online distribution enables suppliers to offer their products to more consumers and creates a lucrative option to increase their sales. The E.C.J. decided de facto limits of online sales in its Pierre-Fabre decision\(^{69}\). Even though the decision itself relates to selective distribution systems, its conclusions can also be applied to franchise systems as

\(^{58}\) See VA-BER, supra note 30 at art. 4(b) (i)-(iv).
\(^{59}\) Wijckmans supra note 37 at para 6.91.
\(^{60}\) 'Active’ sales are sales initiated by the distributor and have to be differentiated from ‘Passive’ sales which are unsolicited requests from individual customers, see Vertical Guidelines supra note 34 at para 51.
\(^{61}\) See art. 4 (c) and (d) VA-BER.
\(^{62}\) VA-BER, supra note 30 at art. 4(c).
\(^{63}\) Vertical Guidelines supra note 34 at para 152.
\(^{64}\) VA-BER, supra note 30 at art. 4(b) (i).
\(^{65}\) See further Vertical Guidelines supra note 34 at paras 51-55.
\(^{66}\) Id. at para 152.
\(^{67}\) Id. at 57.
\(^{68}\) Wijckmans supra note 37 at para 6.39 in conjunction with 6.91.
restrictions of online sales not only constitute a restriction of active sales in selective distribution systems but also restrict passive sales in territories which have not been allocated to the respective distributor.\(^{70}\)

In *Pierre-Fabre*, a pharmaceutical and cosmetics company, had required its distributors to sell its products only from outlets at which there is at least one person present, who is “specially trained to: [inter alia] acquire a thorough knowledge of the technical and scientific characteristics of the products..., necessary for the proper fulfillment of the obligations of professional practice... In order to do this, the person in question must have a degree in pharmacy awarded or recognized in France.”\(^{71}\) The E.C.J. held that clauses limiting the opportunity of a distributor to sell via the internet *de facto* restrict that distributor’s ability to sell outside its contractual territory and thus constitute a restriction of competition.\(^{72}\)

5. **Non-Competition**

Franchise systems receive special treatment with respect to non-competition provisions.\(^{73}\) While Article 5 of the VA-BER generally limits the duration of non-competition provisions to five years, E.C.J. deems non-competition provisions in franchise agreements essential to protect the know-how of the franchisor. It has, therefore, held that these clauses do not infringe Article 101(1) of the TFEU so long as the provisions are limited to the period of validity of the agreement or for a reasonable period after its expiration.\(^{74}\) The Commission also has declared that non-competition provisions may be necessary to maintain the common identity and reputation of the franchised network. Therefore, many practitioners believe a non-competition provision will fall outside the scope of Article 101(1) of the TFEU so long as it does not exceed the duration of the franchise agreement itself.\(^{75}\) However, other practitioners take the position that longer term franchise agreements should be reduced to a series of auto-renewable five year agreements to ensure compliance with Article 5 of the VA-BER. In either case, the duration of non-competition clauses should, therefore, be based on and tied to the underlying justification for their existence – protection of the franchisor’s know-how or reputation.

Post-termination non-competition provisions may also benefit from protection under the VA-BER if they fall within the scope of Article 101(1) of the TFEU. Article 5(3) of the VA-BER permits post-termination non-competition clauses if the following four criteria are met:

(a) the obligation relates to goods or services which compete with the contract goods or services;

(b) the obligation is limited to the premises and land from which the buyer has operated during the contract period;

\(^{70}\) The Commission states in its Vertical Guidelines (*supra* note 34 at para 52), that “in principle, every distributor must be allowed to use the internet to sell products.”

\(^{71}\) *Id.* at para 13.

\(^{72}\) *Id.* at para 47.

\(^{73}\) Pursuant to Article 1(d) of the VA-BER “‘non-compete obligation’ means any direct or indirect obligation causing the buyer not to manufacture, purchase, sell or resell goods or services which compete with the contract goods or services, or any direct or indirect obligation on the buyer to purchase from the supplier or from another undertaking designated by the supplier more than 80% of the buyer’s total purchases of the contract goods or services and their substitutes on the relevant market, calculated on the basis of the value or, where such is standard industry practice, the volume of its purchases in the preceding calendar year.” VA-BER, *supra* note 30 at art. 1(d).

\(^{74}\) *Pronuptia* *supra* note 13 at para 25.

\(^{75}\) Vertical Guidelines *supra* note 34 at para 190(b).
(c) the obligation is indispensable to protect know-how transferred by the supplier to the buyer; and

(d) the duration of the obligation is limited to a period of one year after termination of the agreement.

With respect to confidentiality, if the know-how remains confidential and has not entered the public domain, the use and disclosure of that know-how can be prohibited without a time limit. Even though the text of the VA-BER does not expressly mention franchise systems and its applicability is not limited to them, they are the most likely distribution systems to benefit from the exemption.76

It should also be noted that a non-competition clause, that does not fall within the scope of the block examination, does not lead to the nullification of the complete franchise agreement. The nullification is instead limited to the non-competition clause itself.77

6. **Product Sourcing**

Obligations to source the contract goods from a specified supplier also need to be assessed by the abovementioned two step system. Such obligations do not fall within the scope of Article 101(1) of the TFEU if they are necessary for the protection of the network's reputation.78 This may be the case if the prohibition on obtaining goods from unapproved suppliers is the only way to effectively guarantee the quality of goods offered by the franchisees. Other methods may be ineffective if it is either impractical to provide objective quality specifications or if the monitoring of these specifications is too expensive.79 Recognized examples of exclusive purchasing obligations that do not infringe Article 101(1) of the TFEU are the distribution of fashion articles80 and a wide product range.81 In the Computerland case the franchise system’s portfolio contained more than 3000 products. The Commission concluded that due to "the wide product range...and the very rapid technological evolution in this product market, it would be impracticable to ensure the necessary quality control by establishing objective quality specifications which franchisees could apply themselves."82

The necessity of an exclusive purchase obligation was denied in the Body Shop decision by the Higher Regional Court of Düsseldorf, Germany.83 The franchise agreement used until 2003 allowed the franchisees to source 35% of their goods from outside suppliers. According to the new franchise agreement, which was for a term of 7 years, the franchisee had to obtain 100% of the products, which were cosmetics items, personal hygiene items and appropriate ancillary products, from the franchisor or from authorized suppliers. The Higher Regional Court first established that the exclusive purchase obligation was not necessary in order to protect know-how. It further held that the exclusive purchase obligation was not necessary in order to protect the identity or reputation of the franchise system since the franchisor permitted the purchase of up to 35% of products from outside suppliers until the introduction of the new franchise agreement. It was not clear to the Court why a 100% purchase

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76 See also Goyder supra note 39 at 195 and Wijckmans supra note 37 at para 6.95.
77 See VA-BER, supra note 30 at art. 5 and Vertical Guidelines supra note 34 at para 65 and 71.
78 Pronuptia supra note 13 at para 21.
79 Goyder supra note 39 at at 187-188.
80 Pronuptia supra note 13 at para 21.
81 Computerland supra note 13 at para 23(vi) (in this case the franchise system’s portfolio contained more than 3,000 products).
82 Id.
83 Oberlandesgericht [OLG] [Higher Regional Court ] Düsseldorf, Apr. 11 2007, Case VI-U (Kart) 13/06, available at: http://www.justiz.nrw.de/nrwe/olgs/duesseldorf/j2007/VI_U__Kart__13_06urteil20070411.html (Ger.).
obligation should now be essential in order to protect the identity and reputation of “The Body Shop” franchise system. The Court pointed out that these goals could be reached by alternative means such as objective quality requirements or a purchasing obligation limited to a certain range of goods.\textsuperscript{84}

If obligations to source the contract goods from a specified source fall within the scope of Article 101(1) of the TFEU, they need to be assessed by the general provisions, especially Article 5 VA-BER.\textsuperscript{85} A provision which requires the franchisee to purchase more than 80% of its total purchases from a source specified by the franchisor constitutes a non-competition clause. If the obligation to purchase a certain quota of products from the franchisor or a specified source, does not exceed the 80% threshold it is exempt by the VA-BER. The agreement is also exempt, if the threshold is met and the purchase obligation is either limited to five years or the duration of the non-competition clause can be extended, for example, to protect the franchisor’s know-how.\textsuperscript{86}

In selective franchise systems the franchisees must, however, also be able to source from each other, \textit{i.e.}. cross supplies may not be prohibited (Article 4(d) VA-BER).

\begin{itemize}
  \item \textbf{B. Eastern European Competition Law}
  
  Competition law in Russia is mostly contained in the Law on the Protection of Competition\textsuperscript{87} (RLPC) that came into effect in October 2006. In July 2009 the Russian Competition Law was significantly amended. On January 6, 2012, the “third antimonopoly package” of laws amending the Russian Competition Law and a number of other federal laws – including the Criminal Code, the Code of Administrative Offenses and the Land Code – entered into force. The Russian Competition Law deviates in certain noteworthy aspects from the regulations of the EEA and Switzerland.

  The main source of Ukrainian competition law is the Law of Ukraine on Economic Competition Production (ULPC).\textsuperscript{88} ULPC’s Article 6 prohibits inter alia concerted practices in relation to price fixing, quota agreements and market allocation. Article 9 provides an exemption for agreements through which intellectual property rights are transferred or which deal with granting the right to use this intellectual property. The exception is limited to the legitimate rights of the subject of intellectual property right. Franchise agreements rarely cause competition concerns.\textsuperscript{89}

  \begin{itemize}
    \item \textbf{1. Resale Price Maintenance}
    
    As a general rule, the Russian legislative regime prohibits resale price maintenance except for fixing a maximum resale price for the buyer. Such prohibition on resale price maintenance does not apply, however, if the parties to an agreement either have an insignificant market share (less than 20% on each side) or if the written agreement constitutes a commercial
  \end{itemize}
\end{itemize}

\textsuperscript{84} Id. at para 25.
\textsuperscript{85} Vertical Guidelines \textit{supra} note 34 at para 129-131.
\textsuperscript{86} See above explanations on non-compete clauses, at p. ____.
\textsuperscript{87} Russia Federal Law No. 135-FZ of 2006 on the Protection of Competition (hereinafter “RLPC”).
\textsuperscript{88} The Law of Ukraine On Economic Competition Protection (The Official Journal of the Verkhovna Rada (OJVR), 2001, No. 12, p. 64) (hereinafter “ULPC”).
\textsuperscript{89} Franchise in 33 jurisdictions worldwide, at 208 (Philip F Zeidman ed., \textit{Getting the Deal Through} 2013) (hereinafter “\textit{Getting the Deal Through}”).
concession (franchise). Franchisors are thus free to set the price of the contract products sold or the contract services provided by the franchisee.

Ukrainian Competition Law also deviates from the EEA regulations as its Article 8(1) allows resale price maintenance in vertical agreements unless it leads to either a substantial restriction of competition, a restricted market access or an economically unjustified raise of prices.

2. **Product Sourcing**

Russian Competition law generally prohibits exclusive purchasing obligations. They are, however, exempt within commercial concessions such as franchise agreements.

Article 8(1) ULPC exempts those provisions from the prohibition on concerted actions which relate to the procurement of goods, which by their nature or in terms of trade customs and other fair customs in entrepreneurial activities do not relate to the subject of the agreement. Specified purchasing obligations may be necessary to secure the image of the franchise system and may as such be exempt.

3. **Exclusivity, Territories and Non-Competition**

Non-competition clauses in vertical agreements constitute a hardcore restriction pursuant to Article 11 (2) RLPC. However, franchise agreements are generally exempted from antimonopoly law prohibitions by Article 12 (1) RLPC. Therefore, the franchisee may be obliged not to operate competitive businesses, the franchisor can also prohibit the franchisee from selling similar goods and services under third party names, and the franchisor itself may be prohibited from competing with the franchisee in a certain territory.

The Ukrainian Competition Law exempts restrictions relating to either the use of goods, supplied by the participant, or goods of other suppliers, the procurement of other goods from other undertakings or sale of other goods to other undertakings or consumers from the prohibition on concerted practices, unless it leads to either substantial restriction of competition, restricted market access or economically unjustified price increases. A non-compete covenant is generally hard to enforce under Ukrainian law. In any case, non-compete covenants may only be applicable for the period of validity of the franchise agreement.

### III. NORTH AMERICA AND LATIN AMERICA

#### A. **Brazil Competition Law**

Brazil has had a franchise disclosure law (the Franchise Law) for close to 20 years that has changed little over time, but Brazil just recently overhauled its competition law. The new Brazilian Competition Law became effective on May 29, 2012. The Competition Law

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90 RLPC supra note 87 at art. 12(1).
91 Getting the Deal Through supra note 89 at 170.
92 See ULPC supra note 88 at art. 8(2).
93 RLPC supra note 87 at art. 11(4).
94 Id. at art. 12(1).
95 Getting the Deal Through supra note 89 at 170.
96 See ULPC supra note 88 at art. 8(1).
97 See Id. at art. 8(2).
98 Brazilian Franchise Law No. 8,955/94 (hereinafter “Brazilian Franchise Law”).
99 Brazilian Competition Act (Law No. 12,529/11) (hereinafter “Brazilian Competition Law”).
focuses on actions or agreements that could constitute an abuse of a dominant position, and, therefore, a breach of the economic order. Franchise agreements are covered by the Competition Law. While the Competition Law is still very new, Article 36 sets forth an extremely broad list of acts that could be characterized under the Competition Law as “violations of the economic order.” Such list is set forth in full below.

After reviewing the laundry list of potential violations, a franchisor might wonder if it can or should enter into Brazil. However, as with many international jurisdictions, the law on the books and practical enforcement are, to date, very different. The Brazilian body that was formed to administer the Competition Law, the Administrative Council for Economic Defense (CADE), is tasked with interpretation and enforcement and is supposed to consider the nature

100 Id. at art. 36 (stating that acts designed to “limit, restrain or in any way injure free competition or free initiative; control the relevant market of goods or services; arbitrarily increase profits; and to exercise a dominant position abusively” are considered violations of the public order).


102 Brazilian Competition Law supra note 99 at art. 36, containing the following list of violations of the Competition Law:

I – to agree, join, manipulate or adjust with competitors, in any way: the prices of goods or services individually offered; the production or sale of a restricted or limited amount of goods or the provision of a limited or restricted number, volume or frequency of services; the division of parts or segments of a potential or current market of goods or services by means of, among others, the distribution of customers, suppliers, regions or time periods; prices, conditions, privileges or refusal to participate in public bidding;

II - to promote, obtain or influence the adoption of uniform or agreed business practices among competitors;

III - to limit or prevent the access of new companies to the market;

IV – to create difficulties for the establishment, operation or development of a competitor company or supplier, acquirer or financier of goods or services;

V – to prevent the access of competitors to sources of input, raw material, equipment or technology, and distribution channels;

VI - to require or grant exclusivity for the dissemination of advertisement in mass media;

VII – to use deceitful means to cause oscillation of prices for third parties;

VIII - to regulate markets of goods or services by establishing agreements to limit or control the research and technological development, the production of goods or services, or to impair investments for the production of goods or services or their distribution;

IX - to impose on the trade of goods or services to distributors, retailers and representatives, any resale prices, discounts, payment terms, minimum or maximum quantities, profit margin or any other market conditions related to their business with third parties;

X - to discriminate against purchasers or suppliers of goods or services by establishing price differentials or other operating conditions for the sale or provision of services;

XI – to refuse the sale of goods or provision of services for payment terms within normal business practice and custom;

XII – to hinder or disrupt the continuity or development of business relationships of undetermined term, because the other party refuses to abide by unjustifiable or anticompetitive terms and conditions;

XIII - to destroy, render useless or monopolize the raw materials, intermediate or finished products, as well as to destroy, disable or impair the operation of equipment to produce, distribute or transport them;

XIV - to monopolize or prevent the exploitation of industrial or intellectual property rights or technology;

XV - to sell goods or services unreasonably below the cost price;

XVI – to retain goods for production or consumption, except to ensure recovery of production costs;

XVII - to partially or totally cease the activities of the company without proven just cause;

XVIII - to condition the sale of goods on the acquisition or use of another good or service, or to condition the provision of a service on the acquisition or use of another good or service; and

XIX - to abusively exercise or exploit intellectual or industrial property rights, technology or trademark.
of the business, the product or service involved, the size of the market, the commercial sector, and the type of the transaction.\textsuperscript{103} Importantly, as with most international competition analysis, potential enforcement is likely to be most applicable in connection with a company or group of companies that has dominance in the market, which is assumed under the Competition Law where a “company or group of companies is able to unilaterally or jointly change market conditions or when it controls 20% or more of the relevant market.”\textsuperscript{104}

Pursuant to the Competition Law, parties must submit economic concentration agreements to CADE for analysis of whether the transaction that runs afoul of the prohibitions in Article 36.\textsuperscript{105} Economic concentration agreements include agreements relating to:

(a) the merger of independent businesses;
(b) the direct or indirect acquisition of control of a part of a business, by means of the purchase or exchange of securities or tangible or intangible assets;
(c) one or more businesses merging into another; or
(d) two or more businesses entering into any kind of affiliation or partnership, consortium, or joint venture agreements.

While submission is voluntary, in many instances certain economic concentration agreements must be submitted if the total transaction values reach certain annual turnover limits.\textsuperscript{106}

To date, franchisors in Brazil have not routinely sought CADE approval of their franchise agreements. In fact, some Brazilian franchise counsel take the position that registration of international franchise agreements with the Brazilian patent and trademark office (INPI), which has been a long-standing requirement for franchise agreements in Brazil, can be considered as prima facie evidence that the franchise agreement complies with the antitrust regulations since INPI has the ability to seek CADE’s analysis of agreements as part of its review.\textsuperscript{107}

1. Resale Price Maintenance

As noted above, the Competition Law directly regulates pricing and the imposition of retail prices in a number of ways, including by making it an express violation of the economic order to, among other things:

(a) agree, join, manipulate or adjust with competitors the prices of goods or services individually offered;

(b) use deceitful means to cause oscillation of prices for third parties;

\textsuperscript{103} Brazilian Competition Law supra note 99 at art. 4.
\textsuperscript{104} Id. at sec. 2, art. 36.
\textsuperscript{105} Brazilian Competition Law supra note 99 at art. 53.
\textsuperscript{106} See Fundamentals supra note 101, at 279.
\textsuperscript{107} Id. at 279-80.
(c) impose on the trade of goods or services to distributors, retailers and representatives, any resale prices, discounts, payment terms, minimum or maximum quantities, profit margin or any other market conditions related to their business with third parties;

(d) discriminate against purchasers or suppliers of goods or services by establishing price differentials or other operating conditions for the sale or provision of services;

(e) refuse the sale of goods or provision of services for payment terms within normal business practice and custom; or

(f) sell goods or services unreasonably below the cost price.\textsuperscript{108}

It is too early to tell how these seemingly all-encompassing restrictions will be applied generally or to franchisors, but such restrictions certainly seem to provide a wide array of potential causes of action against a franchisor who attempts to use pricing with its franchisees or other competitors to better its position in the market.

2. \textbf{Product Sourcing}

Similar to its broad pricing coverage, the Competition Law directly regulates product sourcing in several key ways, including by making it an express violation of the economic order to, among other things:

(a) manipulate the production or sale of a restricted or limited amount of goods or the provision of a limited or restricted number, volume or frequency of services;

(b) divide parts or segments of a potential or current market of goods or services by means of, among others, distributing customers, suppliers, regions or time periods;

(c) create difficulties for the establishment, operation or development of a competitor company or supplier, acquirer or financier of goods or services;

(d) prevent the access of competitors to sources of input, raw material, equipment or technology, and distribution channels;

(e) regulate markets of goods or services by establishing agreements to limit or control the research and technological development, the production of goods or services, or to impair investments for the production of goods or services or their distribution;

(f) refuse the sale of goods or provision of services for payment terms within normal business practice and custom;

(g) destroy, render useless or monopolize the raw materials, intermediate or finished products, as well as to destroy, disable or impair the operation of equipment to produce, distribute or transport them; and

\textsuperscript{108} Brazilian Competition Law \textit{supra} note 99 at subsections I, VII, VIII, IX, XI, XV, sec. 3, art. 36.
(h) condition the sale of goods on the acquisition or use of another good or service, or to condition the provision of a service on the acquisition or use of another good or service.  

3. **Exclusivity, Territories and Non-Competition**

The Competition Law is equally broad in its oversight of exclusive territorial grants and restrictions. Specifically, Article 36 restricts, among other things, parties from agreeing to:

(a) the division of parts or segments of a potential or current market of goods or services by means of, among others, the distribution of customers, suppliers, regions or time periods;

(b) limit or prevent the access of new companies to the market;

(c) create difficulties for the establishment, operation or development of a competitor company or supplier, acquirer or financier of goods or services;

(d) prevent the access of competitors to sources of input, raw material, equipment or technology, and distribution channels; and

(e) monopolize or prevent the exploitation of industrial or intellectual property rights or technology.

In addition to the express Competition Law restraints, the Franchise Law requires certain basic disclosures regarding the franchisee’s territory and territorial rights, namely if:

(i) the franchisee is guaranteed exclusivity or a right of first refusal in any particular territory or activity and, if so, under what conditions; and
(ii) the franchisee has the right to sell or render services outside its territory or provide such services outside Brazil. However, the Franchise Law does not regulate or provide restrictions on granting territories, whether exclusive or nonexclusive.

Apart from the Franchise Law, non-competition provisions in Brazil should be carefully drafted in order to reduce the likelihood that the provision will be stricken as being overly broad. For example, a post-term non-competition provision needs to be limited in scope, geographic area and time and, if applicable to an employee, may be subject to the Brazilian labor law, which will generally accept such restrictions, provided again, that the time frame and geographic scope are reasonable. Additionally, in limited circumstances (especially where the franchisee worked in the field prior to entering into a franchise agreement), a judge may require the franchisor to compensate the franchisee for its commitment to non-competition. Compensation for adherence to a post-term covenant can take two forms. The franchise agreement or an ancillary document can require the franchisor to make a specific payment or periodic payments to the franchisee for the express purpose of restricting his right to work (e.g., $50.00 a month or $1,000 a year for refraining from competition). Please note that such values are just examples and the specific amount cannot be accurately estimated, as it will depend on particular aspects of the case.

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109 Id.
In-term covenants not to compete may be perpetual and are not scrutinized like post-term covenants. Notwithstanding these general principles, any restriction which limits a company’s ability to freely compete may be questioned before CADE and may be considered partly unenforceable under antitrust legislation if the provision is deemed abusive to the affected party.

Brazilian law provides for specific performance of post-term noncompetition provisions in circumstances where the franchisor can demonstrate that the breach of such covenant is a result of a franchisee’s egregious behavior. Injunctions are easier to obtain with respect to breaches of in-term covenants not to compete. In the alternative, a franchisor’s remedy for breach of these provisions is to assert a claim in court (or through arbitration) for the losses suffered.

B. Canada Competition Law

The principal source of competition law in Canada is the federal Competition Act (the “Act”)\textsuperscript{110} which sets out criminal offenses and civilly reviewable conducts. In 2009, the Act was significantly amended.\textsuperscript{111}

The Act distinguishes between conduct which is a criminal offense, subject to fines and/or imprisonment, and conduct which is a civil reviewable practice, subject to only a remedial order (except for abuse of dominance which may also be subject to administrative monetary penalties (“AMPs”)).\textsuperscript{112} Criminal offenses are dealt with by the courts while reviewable practices are dealt with by the Competition Tribunal (the “Tribunal”). An application to the Tribunal may only be instituted by the Commissioner of Competition (the “Commissioner”) except for the reviewable practices of refusal to deal, price maintenance, tied selling, market restriction and exclusive dealing in respect of which an application may also be initiated by an affected party.

It is noteworthy that the Act provides for a right to civil action for recovery of actual damages only in respect of activity which is prohibited by its criminal provisions.\textsuperscript{113}

With respect to franchising directly, the Provinces of Ontario\textsuperscript{114}, Alberta\textsuperscript{115}, Prince Edward Island\textsuperscript{116}, New Brunswick\textsuperscript{117} and most recently Manitoba\textsuperscript{118} have franchise specific pre-sale disclosure laws that contain certain quasi-competition law requirements and restrictions. For instance, the laws generally state that every franchise agreement imposes on each party a duty of fair dealing in its performance and enforcement. A party to a franchise agreement has a right of action for damages against another party to the franchise agreement who breaches the duty of fair dealing, and there have already been cases where parties have incurred liability specifically for breaching this obligation.

\textsuperscript{110} Competition Act (R.S.C. 1985, c. C-34) (hereinafter “Competition Act”).
\textsuperscript{111} The amendments included, among others, the creation of a “two-track” approach for agreements between competitors, repeal of the criminal predatory pricing, price discrimination, promotional allowance, and price maintenance provisions (with the latter replaced with a new provision allowing for civil review of resale price maintenance), significant increases to criminal and civil penalties for deceptive telemarketing practices, and the introduction of administrative monetary penalties (“AMPs”).
\textsuperscript{112} Competition Act supra note 110 at sec. 45.
\textsuperscript{113} Id.
\textsuperscript{114} Arthur Wishart Act (Franchise Disclosure), 2000, SO 2000.
\textsuperscript{115} Franchises Act (RSA 2000, c F-23).
\textsuperscript{116} Franchises Act (RSPEI 1988, c F-14.1).
\textsuperscript{117} Franchises Act (SNB 2007, c F-23.5).
\textsuperscript{118} The Franchises Act (CCSM c F156).
The laws define fair dealing as including the duty to act in good faith and in accordance with reasonable commercial standards. Also, the laws state that a franchisee may associate with other franchisees and may form or join an organization of franchisees, and that a franchisor may not interfere with a franchisee’s right to associate with other franchisees. Any provision in the franchise agreement which restricts a franchisee from exercising any right to associate is void, and a franchisee has a right of action for damages for a contravention of such right.

1. **Resale Price Maintenance**

The 2009 amendments to the Act included the replacement of the criminal price maintenance provision\(^{119}\) with a new civil price maintenance provision\(^{120}\). The new civil provision uses language largely identical to the former criminal prohibition. Under the new section, on application by the Commissioner or a person granted leave under section 103.1 of the Act, the Tribunal may make a remedial order where a producer or supplier of a product directly or indirectly, by agreement, threat, promise or any like means, has influenced upward or discouraged the reduction of the price at which the person’s customer suppliers, offers to supply, or advertises the product within Canada, and this conduct has had, is having or is likely to have an adverse effect on competition in a market.\(^{121}\)

With the important exceptions of: (i) being a criminal rather than a civilly reviewable provision; and (ii) not requiring the demonstration of any “adverse effects on competition”,\(^{122}\) the former section 61 the Act was almost identical in form and substance to the current section 76 of the Act.

Under the former section 61, “resale price maintenance” gave rise to criminal convictions and enforcement actions.\(^{123}\) Class action suits for damages were launched in recent years\(^{124}\) as was other private litigation. While it would seem unlikely that enforcement of the civil provision could be as active as its *per se* criminal predecessor, given the “adverse impact on competition” requirement in section 76, the Commissioner was the first to test the new provision before the Tribunal, having commenced an action against Visa and MasterCard in 2010.\(^{125}\)

The Act specifically contemplates suppliers suggesting resale prices to their customers. The suggestion of a resale price to a customer by a supplier is proof that the price is influenced in accordance with the suggestion, in the absence of proof that the supplier made it clear to the

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\(^{119}\) Competition Act *supra* note 110 at sec. 61.

\(^{120}\) Competition Act *supra* note 110 at sec. 76.

\(^{121}\) Competition Act *supra* note 110 at sec. 61.

\(^{122}\) The meaning of the term “adverse effect on competition” is not entirely clear; however, it is likely a standard which is less than a “substantial” lessening of competition.

\(^{123}\) See, for example, *R. v. Labatt Brewing Company/La Brasserie Labatt Limitée* (November 23, 2005), Quebec 500-73-02495-055 (C.Q.), where Labatt pleaded guilty to price maintenance with respect to the retail price of discount beer sold by convenience stores and grocery retailers in Sherbrooke and other parts of Quebec. The Court ultimately fined Labatt $250,000.

\(^{124}\) See, e.g., *Quizno’s Canada Restaurant Corporation v. 2038724 Ontario Ltd.*, 2010 ONCA 466 (hereinafter “Quizno’s”). This case is further discussed below.

\(^{125}\) See *The Commissioner of Competition v. Visa Canada Corp. and MasterCard Int’l Inc.*, CT-2010-010 (where the Commissioner alleged that rules imposed on merchants by Visa and MasterCard had effectively eliminated competition between Visa and MasterCard for merchants’ acceptance of their credit cards, resulting in increased costs to businesses and, ultimately, consumers. Merchants in Canada pay an estimated $5 billion annually in hidden credit card fees); see also Competition Bureau, *Competition Bureau Alleges Anti-Competitive Conduct by Visa and MasterCard: Hearing Starts Today*, available at: http://www.competitionbureau.gc.ca/eic/site/cbbc.nsf/eng/03465.html.
customer that it was under no obligation to accept the suggestion and that it would not suffer in its business relations with the supplier if it rejected the suggestion.126

2. Product Sourcing

Subsection 75(1) of the Act provides that where:

(a) a customer is substantially affected in its business or is precluded from carrying business because it is unable to obtain adequate supplies of a product anywhere in a market on usual trade terms;

(b) this occurs as a result of insufficient competition among suppliers;

(c) the product is in ample supply;

(d) the customer is willing and able to meet usual trade terms; and

(e) the refusal to deal is having or is likely to have an adverse effect on competition in a market,

the Tribunal may order one of more suppliers in the market to supply the customer with the product within a specified time and on usual trade terms. An application for such an order may be sought by either the Commissioner or a person granted leave under section 103.1 of the Act.

The Act provides a right of private action in respect of refusal to deal.127

In 2012, the Ontario Superior Court of Justice dismissed a $2 billion franchise and competition class action against Tim Hortons.128 The plaintiffs’ claim was essentially based on two significant changes to the franchise agreement between the franchisor and franchisees: (i) Tim Hortons’ conversion to the “par baking” method for baking donuts and other baked goods, known as “Always Fresh”; and (ii) the introduction of soups, sandwiches and other lunch menu items. The plaintiffs argued that the “Always Fresh” requirement increased their cost to produce baked goods, cutting into their profit margins. The plaintiffs also argued that Tim Hortons required franchisees to sell lunch menu items at a loss or at break-even prices while profiting through rent, royalties, and advertising payments based on franchises sales.

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126 There is no Canadian law prohibiting the establishment of a maximum resale price policy. Although such policies were at one time held to be per se illegal in the United States, they have never been prohibited in Canada.

127 See, e.g., Nadeau Poultry Farm Ltd. v. Groupe Westco Inc., [2011] F.C.J. No. 844, 2011 FCA 188. This was a dispute between the appellant, Nadeau Poultry Farm, the operator of the only chicken slaughtering plant in New Brunswick, and the main respondent, Group Westco Inc., a chicken producer that, along with its subsidiaries, owns or controls just over half of the chicken production in New Brunswick. In 2007, Westco offered to buy or invest in the Nadeau plant, but negotiations between the parties broke down. Westco made it clear that if Nadeau was not willing to sell its plant, Westco would construct its own slaughtering plant in partnership with Nadeau’s main competitor and thereby deprive Nadeau of 50% of its supply. Eventually, Westco gave written notice that it would stop supplying chickens to Nadeau and the other respondents followed soon after, leading to the commencement of a private action before the Tribunal for an order for resumed supply. Nadeau was ultimately unsuccessful with the Federal Court upholding the Tribunal’s decision to dismiss the application.

128 See Fairview Donut Inc. v. The TDL Group Corp, 2012 ONSC 1252 (leave to the Supreme Court was dismissed in February 2013).
The court rejected the plaintiffs’ claim that the franchisor was required by the statutory duty of fair dealing and/or implied terms of the franchisee agreement to supply products to franchisees at the price obtained by the franchisor from its suppliers. The Court found that the law recognizes that the franchisor is not required to sell products to its franchisees at the lowest price available and that there is no requirement for the franchisor to ensure that the franchisee makes a profit on every product it sells.

We note that the court’s decision highlights that many franchisee/franchisor disputes are commercial disputes that do not involve any consideration of anti-competitive conduct contrary to the Act. In this case, the core dispute related to the commercial reasonableness of the pricing and supply arrangements. The court’s decision also underscores that in many instances, allegations of criminal conduct relating to conspiracy and price maintenance are not necessarily the appropriate means by which such commercial disputes should be resolved.

In Quizno’s Canada Restaurant Corporation v. 2038724 Ontario Ltd., the representative plaintiff alleged that franchisees were charged exorbitant prices for food and other supplies purchased for use in restaurants. The plaintiff alleged this implicated Competition Act conspiracy and price maintenance claims between Quizno’s, the franchisor, and Gordon Food Services, from whom franchisees were required to purchase supplies used at Quizno’s restaurants.

In its 2010 decision, the Ontario Court of Appeal affirmed the Divisional Court’s certification of a competition and franchise class action against a significant national franchisor for a range of contractual and antitrust claims arising from the franchisor’s vertical supply and pricing arrangements. The Court of Appeal’s decision appears to have lowered the threshold for the certification of competition class actions in Canada. Historically, the courts had been reluctant to certify competition class actions in contested cases, due to the challenges of clearly formulating a methodology for establishing loss and liability on a class-wide basis, particularly in cases involving diverse products distributed through a complex distribution chain. It may be argued that the facts of the Quizno’s case are unique and can be potentially distinguished on the basis that it is a strictly vertical resale price maintenance case involving a direct class of purchasers.

3. Exclusivity, Territories and Non-Competition

a. Exclusive Dealing

Exclusive dealing arrangements are common in Canada and often arise in the context of agreements relating to financing, franchising, agency, distributorships, dealerships and other similar arrangements.

Paragraph 77(1) of the Act defines “exclusive dealing” to include:

(a) any practice whereby a supplier of a product, as a condition of supplying the product to a customer, requires that customer to

(i) deal only or primarily in products supplied by or designated by the supplier or the supplier’s nominee, or

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129 Quizno’s supra note 124.
130 Id.
(ii) refrain from dealing in a specified class or kind of product except as supplied by the supplier or the nominee, and

(b) any practice whereby a supplier of a product induces a customer to meet a condition set out in subparagraph (a)(i) or (ii) by offering to supply the product to the customer on more favourable terms or conditions if the customer agrees to meet the condition set out in either of those subparagraphs.

Where a practice of exclusive dealing (i) impedes entry or expansion of a firm into a market; (ii) impedes introduction of a product into or expansion of sales of a product in a market; or (iii) has any other exclusionary effect in a market, with the result of substantially lessening competition, the Tribunal may make an order prohibiting the conduct.

Market restriction is any practice whereby a supplier of a product, as a condition of supplying the product, requires a customer to supply any product only to a defined market, or exacts a penalty from a customer if the customer supplies any product outside a defined market. As in the case of exclusive dealing, the Tribunal may make an order prohibiting the practice where it results in a substantial lessening of competition.

b. **Exclusive Territories**

As a general proposition, exclusive territories are permissible in Canada, subject to market restriction provisions discussed above.

c. **Non-Competition**

Covenants against competition are generally enforceable in Canada, but unlike in many U.S. jurisdictions, Canadian courts will not generally blue pencil or re-write a covenant so a covenant not to compete will be void unless it is reasonable. According to Fundamentals, supra note 101, at 298. Accordingly, Canadian counsel advises against “stacking” alternative covenants with varying degrees of geographical scope. Further, franchisors should clearly specify the competitors or the types of businesses that are to be covered by the covenant. Canadian courts are unlikely to attempt to interpret the meaning of a covenant that restricts operation of a “same or similar business.”

C. **Mexico Competition Law**

The Mexican Federal Law of Economic Competition (the Competition Law) is the overarching competition law in Mexico and is enforced by the Mexican Federal Competition Commission (FCC). The Competition Law was enacted on December 18, 1992 and became effective as of July 1993. It was subject to a prior comprehensive amendment in July 2006, and was most recently amended effective May 11, 2011, with the amendments focused on providing the FCC greater powers to investigate and impose sanctions for anticompetitive conduct.

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131 Fundamentals supra note 101, at 298.
Mexico’s competition policy stems from the current Constitution, enacted in 1917, which among other things prohibits monopolies and monopolistic practices. However, the Constitutional provisions regarding competition were largely ignored for years because there were no regulations or other legislative guidance as to what constituted prohibited behavior, and there was no specific enforcement agency tasked with investigating possible violations. The original Competition Law passed in 1992 was largely focused on monopolies, and this rang true through the 2006 amendments as focus and enforcement was limited mainly to areas such as telecommunications, broadcasting and other industries controlled by one or only a few very large companies.

The purpose of the Competition Law is “to protect the competition process, and the free market access, by preventing monopolies, monopolistic practices and other restrictions that deter the efficient operation of the goods and services market”. Importantly, the Competition Law separates potential monopolistic practices into “absolute monopolistic practices” and relative monopolistic practices. Absolute monopolistic practices are “contracts, agreements, arrangements, or combinations among competitive economic agents, whose aim or effect are any of the following: (a) to fix, raise, to agree upon or manipulate the purchase or sale price of the goods or services supplied or demanded in the markets, or to exchange information with the same aim or effect; (b) to establish the obligation to produce, process, distribute or market only a restricted or limited amount of goods, or to render a specific volume, number, or frequency of restricted or limited services; (c) to divide, distribute, assign or impose portions or segments of the current or potential market of goods and services, by means of a determinable group of customers, suppliers, time or spaces; or (d) to establish, agree upon or coordinate bids or to abstain from bids, tenders, public auctions or bidding.” Absolute monopolistic practices are deemed void and the parties to the absolute monopolistic practices are automatically subject to penalties.

Relative monopolistic practices are acts, contracts, agreements, or combinations whose aim or effect is to improperly displace other persons from the market, substantially hinder their access to the market, or to establish exclusive advantages in favor of one or several entities or individuals. The Competition Law lists seven examples of relative monopolistic practices,

135 Art. 28, Political Constitution of the Mexican United States (1917).
136 Mexican Competition Law supra note 132 at art. 2.
137 Id. at art. 9.
138 Id.
139 Id. at art. 10.
140 Id., containing the following laundry list of non-exclusive relative monopolistic practices:
(a) some of the economic agents that do not compete among themselves are: to set, impose or establish the exclusive distribution of goods and services, by means of the subject, geographical location, or specific periods of time, including the division, distribution or assignment of customers and suppliers; and also the obligation to not manufacture or distribute goods or services for a specific period of time or that may be specified;
(b) setting the prices or other conditions that a distributor or supplier has to abide by when marketing or distributing goods or providing services;
(c) the conditioned sale or transaction when buying, acquiring, marketing or providing other goods or additional services, normally different or that can be differentiated, or on the basis of reciprocity;
(d) the sale or transaction subject to the condition of not using or acquiring, marketing or providing goods or services produced, processed or distributed or sold by a third party; The unilateral action based on refusing to sell or provide to specific individuals, goods or services available and normally offered to third parties;
(e) the agreement reached among several economic agents or the invitation extended them to exert pressure against customers or suppliers, in order to discourage them from specific behaviors, to apply retaliations or force them to act in a specific manner; or
but confirms that these and any other potential relative monopolistic practices require proof, namely that: (i) the responsible party has substantial power in the relevant market; and (ii) such practices are carried out in connection with the goods or services corresponding to that specific relevant market.\textsuperscript{141}

Defining the relevant market requires a review of the following criteria: (i) the possibility of substituting the goods or services by other national or domestic goods or services, taking into consideration the technological potential, to what extent consumers have the possibility to substitute the good or service and the time required for said substitution; (ii) the costs involved in the distribution of the relevant goods (such as freight, insurance, and custom duties) and the likelihood of substitutable goods from other regions and from abroad, taking into account freight, insurance, custom duties and non-custom restrictions, the restrictions imposed by the involved economic agents, and the time required to supply those regions; (iii) the costs and potential access to other markets by users or consumers; and (iv) the federal, local, or international standard restrictions that limit the access of users or consumers to alternative supply sources, or the access of the suppliers to alternative customers.\textsuperscript{142} Once the relevant market is defined, the Competition Law calls for evaluation of six factors to determine if a party has substantial power in the relevant market, including:

(a) market share and whether it can unilaterally set the prices or restrict the supply in the relevant market without the competitive agents being able to act or to potentially counteract that power;

(b) the entry barriers and the elements that may alter those barriers and also other competitors’ offer;

(c) the competitors existence and power;

(d) possible access to input resources that the economic agent and its competitors have;

(e) its recent performance; and

(f) all other criteria established in the regulations of the Competition Law.\textsuperscript{143}

Apart from the Competition Law, the Mexico franchise disclosure law, originally codified in 1991 as part of the 1991 Industrial Property Law (“IPL”),\textsuperscript{144} and implemented through its Regulations issued in 1994 (“1994 Regulations”),\textsuperscript{145} was amended in 2006 and among the key amendments were new competition law based requirements for inclusion in franchise agreement, such as, among others, the geographical zone within which the franchisee may operate and the franchisor’s policies relating to inventory, marketing, advertising which are related to products which may be purchased and suppliers which may be used by the franchisee. In addition, the

\textsuperscript{141} Id. at art. 11.
\textsuperscript{142} Id. at art. 12.
\textsuperscript{143} Mexican Competition Law supra note 132 at art. 13.
\textsuperscript{144} Industrial Property Law (1991) at art. 142 (hereinafter “IPL”).
\textsuperscript{145} Regulations to Industrial Property Law (1991) at art. 65 (hereinafter “1994 Regulations”).
2006 amendment included several new restrictions “prohibited practices” on franchisees’ and franchisors’ conduct, including:

(a) a prohibition on forcing a franchisee to sell its assets to the franchisor or its designee upon the termination of the franchise agreement, or to make the franchisor a partner of the franchisee unless the franchise agreement gives the franchisor those rights;

(b) a prohibition on franchisors being involved in the organization and operation of their franchisees, except to the extent that such involvement is strictly necessary to guarantee compliance with image standards of the franchise;

(c) franchisees are prohibited from disclosing the franchisor’s confidential information during and after the term of the franchise agreement; and

(d) neither a franchisor nor a franchisee may unilaterally terminate or rescind a franchise agreement in the absence of an indefinite term for the agreement, or in the absence of a just cause; and failure to follow the franchise agreement’s standards for termination is a violation of the law.

Interestingly, some of the more onerous aspects of the original draft of the amendments to the IPL were removed in the final version, but the legislation contains a statement that is grounded in competition law tenets dispute the IPL being an inherently intellectual property based franchise law: “To establish legal certainty and conditions among the parties in the operation of franchises, as well as to guarantee non-discriminatory treatment for all franchisees of the same franchisor.”

1. **Resale Price Maintenance**

As noted above, the Competition Law directly regulates pricing such that a franchisor that mandates pricing could be susceptible to review and potential sanctions for retail price maintenance in Mexico. Specifically, Section II, Article 10 of the Competition Law deems the setting of prices or other conditions that a distributor or supplier (including a franchisee) has to abide by when marketing or distributing goods or providing services a “relative” monopolistic practice. Thus, while setting prices is not an absolute monopolistic practice, a franchisor who desires to set prices in Mexico would need to determine the relevant market pursuant to the factors in Article 12 of the Competition Law and then determine if they have substantial power in the relevant market pursuant to the factors in Article 13 of the Competition Law. The authors and their Mexican counsel are not aware of any actions brought by the FCC to date against franchisors in the pricing area since as noted above the focus has been on different industries and perceived monopolies of extremely large companies\(^{146}\), and to date there have not been many franchise systems of the size and in the type of industry that has garnered the FCC’s attention.

2. **Product Sourcing**

Similar to resale price maintenance, the Competition Law regulates product sourcing. Specifically, Section III, Article 10 of the Competition Law deems the conditioned sale or transaction of different products or services when buying, acquiring, marketing or providing other goods or additional services as a “relative” monopolistic practice, but again similar to

\(^{146}\) Fundamentals *supra* note 101, at 303.
resale price maintenance, there is no known history of enforcement with respect to franchising in part due to the lack of perceived market power of most franchisors operating in Mexico.\textsuperscript{147} However, the Mexican Franchise Law amendments of 2006 did require that certain information be set forth in the franchise agreement as a minimum requirement, including among other things, information regarding profit margin policies, inventory, marketing, and advertising policies, and the criteria for supervision, evaluation and grading of performance.\textsuperscript{148} Interestingly, these topics have less been addressed in the franchise agreement as in the franchise disclosure document.

3. **Exclusivity, Territories and Non-Competition**

Section I, Article 10 of the Competition Law deems exclusive distribution arrangements that carve up geographic areas or periods of time for access customers and suppliers as a "relative" monopolistic practice. However, as noted above, to date the Commission has not focused on the franchise market in these areas.

With respect to covenants against competition in franchise agreements, in-term covenants not to compete are largely enforceable in Mexico. However, post-termination covenants not to compete are generally contrary to the freedom to work in Mexico (both a civil and constitutional right); however, such covenants can be acceptable when competition involves the misuse or unauthorized use of industrial or trade secrets, copyrights, patents, trademarks or other industrial, property rights which have not become a part of the public domain, during the term of the franchise agreement. Language tying the competition to misuse of trade secrets should be added to development agreements, franchise agreements, principal's covenants and confidentiality agreements in order to aid in enforcement of the noncompetition provisions.

A limited form of injunctive relief is available and generally issued by the Mexican Industrial Property Institute only when such rights have been infringed (\textit{i.e.}, if an employee or franchisee operates a similar franchise using the franchisor's proprietary rights). In the event of a breach of the franchise relationship not involving proprietary rights, franchisors are relegated to terminating the franchise relationship and seeking liquidated damages.

Further, a Mexican court may find in-term and post-term covenants not to compete to be void if such covenants or conditions impose obligations that contradict any civil rights or constitutional rights (\textit{e.g.}, freedom to work is a civil right that is fundamental to the Mexican Constitution). Any provisions that contravene this right or any public policy right may be declared void by a Mexican court, except that unauthorized use or disclosure of proprietary rights will be punishable under the IPL.

IV. **ASIA-PACIFIC AND MIDDLE EAST**

Unlike in the EU or North America, the state of development of competition laws in Asia-Pacific and the Middle East is quite uneven. On the one hand, these are jurisdictions such as Australia, Japan, Korea and Taiwan, which are established and as mature as the EU and the US. On the other hand, these are major emerging economies like China and India, that have only recently established their competition law regimes but have been rapidly developing their competition laws and (perhaps more importantly) implementation regulations in recent years.\textsuperscript{149}

\textsuperscript{147} Id. at 304.
\textsuperscript{148} IPL supra note 144 at art. 142.
\textsuperscript{149} As an example of the rapid development of competition laws in these jurisdictions, the Guangdong High Court of China’s Guangdong province released its decision on the \textit{Qihoo 360 v. Tencent} case on March 28, 2013. It is a
In July 2010, the Hong Kong Government published the long-awaited Competition Bill which is intended to introduce general competition law in Hong Kong. In August 2010, the member States of the Association of Southeast Asian Nations (ASEAN) all committed to introduce nation-wide competition policies and laws by 2015.

In general, most countries in these regions have established, or are in the process of establishing, competition laws. These competition laws cover most of the same topics that are covered in other more “advanced” jurisdictions, including, for example, merger control, trust/cartel arrangements, vertical restrictions, abuse of dominant market position, etc. Many of these provisions will affect the franchise agreements to be implemented in these jurisdictions.

As such, franchisors and their advisors will be well-advised to consider these issues before the franchisors embark on an exemption strategy in these markets. In particular, franchisors and their advisors should seek to construct a franchise program that can be consistently operated throughout these jurisdictions, and at the same time remain flexible enough to adapt any local variations.

A. Australia Competition Law

Unlike some other jurisdictions that have franchise laws (e.g., Mexico and Brazil), Australia is an international jurisdiction that has its franchise law rooted in Australian competition law. In fact, the Australian Franchising Code of Conduct (Code), which became effective on July 1, 1998, and has been amended multiple times, is actually a regulation issued under the Australian Competition and Consumer Act 2010 (Competition and Consumer Act). The Competition and Consumer Act only came into effect in January 2011. It essentially replicated and updated the Trade Practices Act 1974, which was previously the relevant legislation.

The Australian antitrust/unfair competition laws that have the most potential to affect franchisors who grant franchises in Australia are:

(a) Section 47 of the Competition and Consumer Act, which prohibits exclusive dealing where the conduct has the purpose or is likely to have the effect of substantially lessening competition in a market;

(b) Sections 47(6) and (7) of the Competition and Consumer Act, which prohibit “third line forcing” conduct outright, such as an offer to supply goods or services on the condition

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landmark decision in many respects – it is by far the most detailed antitrust analysis provided by a Chinese court concerning topics such as “relevant market” and “dominant market position”; it is also probably the first significant antitrust decision regarding competition in the Internet-based industries.


152 Fundamentals supra note 101, at 283.


155 Id.


157 Id. at sec. 47(6) and (7).
that the person being supplied must acquire goods or services from a designated third party or
designated third parties, even if that third party is related to the first party and no matter the
effect on competition. There is a procedure available to exempt certain third line forcing from
automatic prohibition if it is publicly notified to the anti-trust regulator. In addition, if the list of
suppliers a franchisee may use is not closed, but is only subject to genuine quality
requirements, this provision will not be infringed;

(c) Division 2 of Part IV of the Competition and Consumer Act\textsuperscript{158} which prohibits a
corporation from making or giving effect to a contract, arrangement or understanding that
contains a cartel provision. A cartel provision is a provision relating to, among other things,
price-fixing or allocating customers, suppliers or territories, by parties that are or would be
competitors;

(d) Section 4D of the Competition and Consumer Act\textsuperscript{159} which prohibits exclusionary
provisions, being an arrangement between two or more competitors (or their affiliates) which
gives rise to a boycott of some other person or class of persons. These provisions are
prohibited even if they have no effect on competition. Similar other sections of the Competition
and Consumer Act also address this issue;

(e) Section 48 of the Competition and Consumer Act,\textsuperscript{160} which prohibits resale price
maintenance (i.e., the practice of inducing or attempting to induce a person not to sell at a price
less than a price specified by the supplier), even if it has no effect on competition. Genuine price
recommendations are generally permitted;

(f) Section 18 of Schedule 2 of the Competition and Consumer Act,\textsuperscript{161} which prohibits a person from engaging in conduct “that is misleading or deceptive or is likely to
mislead or deceive”;

(g) Sections 20-22 of Schedule 2 of the Competition and Consumer Act\textsuperscript{162} which
prohibit a person from engaging in unconscionable conduct; and

(h) Section 29 of Schedule 2 of the Competition and Consumer Act\textsuperscript{163} which
prohibits a person from making false or misleading representations about goods or services.

A breach of the Code will constitute a breach of the Competition and Consumer Act. There
are no civil or criminal penalties for non-compliance with the Code. However, the
Competition and Consumer Act includes a number of remedies that the antitrust regulator may
invoke for a breach of the Code, such as injunctions, enforceable mandates to comply with the
Code, and corrective advertising. Further, any person who suffers loss or damage by conduct
in breach of the Code may recover that loss or damage by taking civil action under the
Competition and Consumer Act. In some circumstances, a court may impose penalties
pursuant to specific provisions of the Competition and Consumer Act (e.g., provisions that make
it is an offense to make false or misleading representations and provisions relating to the
characteristics of goods of services).

\textsuperscript{158} Id. at div. 2, pt. IV.
\textsuperscript{159} Id. at sec. 4D.
\textsuperscript{160} Id. at sec. 48.
\textsuperscript{161} Trade Practices Amendment (Australian Consumer Law) Act (No. 2) 2010, at sch. 2, section 18.
\textsuperscript{162} Id. at sch. 2, sec. 20-18.
\textsuperscript{163} Id. at sch. 2, sec. 29.
There is no obligation on franchisors or franchisees to file franchise agreements with any competition authorities. However, third-line forcing requirements do need to be notified to the Australian Competition and Consumer Commission (ACCC) to gain immunity from prosecution. Further, any provisions in a franchise arrangement that may breach other competition laws can be “authorized” by the ACCC and therefore be immune from prosecution where there is a net public benefit. It is important to review franchise agreements with franchise and/or competition counsel in Australia to determine if the provisions run afoul of the restrictions and should be notified to the ACCC.

1. **Resale Price Maintenance**

Current law in Australia dictates that a franchisor that does not operate company-owned stores in competition with franchisees, and so has a purely vertical relationship with franchisees, is generally able to control the pricing of its franchisees. However, a franchisor that supplies products to the franchisees may only set maximum prices for the resupply of those products. Any attempt to set a minimum price will be illegal resale price maintenance.

If the franchisor operates company-owned stores that compete with franchisees, price fixing is not permissible. Any attempt to set or control discounts or minimum prices in the franchised outlets will constitute price fixing and, therefore, will be illegal. Price fixing is classified as cartel conduct under the CCA and is punishable by severe fines (the maximum fine is the greater of three times the benefit, 10% of annual group turnover, or a $10 million per offense and up to 10 years imprisonment). However, a franchisor that supplies products to franchisees can set maximum prices even if the franchisor also competes with those franchisees.

There is a limited exemption that allows franchisees and franchisors to discuss and agree on both the acquisition and selling prices for stock that has been “collectively acquired”. Unfortunately, the term collectively “acquired” is not defined in the act and has never been interpreted by the courts. As the scope of this exemption is unclear, it is not commonly relied upon.

2. **Product Sourcing**

As noted above, Sections 47(6) and (7) of the Competition and Consumer Act, which prohibit “third line forcing” conduct outright, such as an offer to supply goods or services on the condition that the person being supplied must acquire goods or services from a designated third party or designated third parties, even if that third party is related to the first party and no matter the effect on competition. There is a procedure available to exempt certain third line forcing from automatic prohibition if it is publicly notified to the anti-trust regulator. In addition, if the list of suppliers a franchisee may use is not closed but is only subject to genuine quality requirements, this provision will not be infringed.

In *Australian Competition & Consumer Commission v. Simply No-Knead (Franchising) Pty Ltd* 168, Simply No-Knead (Franchising) Pty Ltd (“SNK”) was sued by the Commission and its franchisees after SNK refused to deliver flour to its bakery franchisees who failed to pay for the

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164 See Fundamentals *supra* note 101, at 284.
165 *Id.*
166 *Id.*
167 *Id.*
franchisor's advertising brochures. The franchisees objected to the content and price of the brochures that were required to be purchased, and stopped paying for them. SNK responded by stopping the sale of required flour necessary to run the bakery. SNK was sued and ultimately the Commission deemed the tying of the sale of flour to the purchase of the brochures was unconscionable within the Australian Trade Practices Act.169

3. Exclusivity, Territories and Non-Competition

Generally, franchisors are permitted to grant franchisees an exclusive territory or exclusive customer classes.170 The franchisor may agree not to grant another franchise within a franchisee's territory and the franchisee may agree not to actively market or solicit customers outside its territory. However, horizontal agreements between competing franchisees are strictly prohibited. For example, any agreement between two franchisees to refuse to deal with a customer who has come from the other's territory would be an illegal market-sharing agreement. This is often expressed as the principle of "own the territory, not the customer."

As a matter of public policy, restrictive covenants are unenforceable in Australia unless the party seeking to enforce them can establish that they were no more than was reasonable in the circumstances to protect a legitimate interest. This will be the case despite the choice of governing law. An Australian court may enforce a damages award made by a foreign court or arbitrator. However, it would not enforce an order of a foreign court or arbitrator seeking to enforce a restrictive covenant: such enforcement action would need to be brought in an Australian court.

The law relating to enforcement of non-compete covenants in Australia is similar to the position in the United States. However, Australian courts will generally not apply a "blue pencil" rule to rewrite a provision that is unreasonable to a level it considers reasonable (the only exception is the power given to New South Wales courts by the Restraints of Trade Act to pare down unreasonable restraints of trade to a level they consider reasonable). For this reason, it is important that any restrictive covenant a party wishes to enforce in Australia should be drafted so that the separate restraints are clearly severable.

If a franchisor imposes confidentiality obligations on a franchisee, it must disclose such obligation in the disclosure document and, if the franchisee is required to sign a separate confidentiality agreement, provide a copy of this agreement to the franchisee at least 14 days before the franchisee signs the franchise agreement or as soon as it is available.

Restraint of trade clauses in franchise agreements were at the forefront of a 2009 case involving the Blockbuster chain in Australia, BB Australia Pty Ltd v. Karioi Pty Ltd.171 The Blockbuster case involved a franchisee Karioi Pty Ltd ("Karioi") that had operated video stores under two other brands since 1990 and then entered into a series of franchise agreements beginning in 1998 with an Australian subsidiary of Blockbuster.172 The franchise agreements contained typical in-term and post-term covenants against competition.173

The 10 year term agreements expired in 2008, but Karioi continued to operate video stores at the former Blockbuster locations, and then later entered into franchise agreements

\[^{169}\text{id.}\]
\[^{170}\text{Fundamentals supra note 101, at 284.}\]
\[^{171}\text{[2010] NSWCA 347 (hereinafter "Karioi").}\]
\[^{172}\text{id. at 10-14.}\]
\[^{173}\text{id. at 44.}\]
with a different video store brand for a number of the former Blockbuster locations. Blockbuster filed for injunctive relief to Karioi and its owners to cease operating competitive stores at two of the former Blockbuster locations for a period of two years after the expiration of the Blockbuster franchise agreements.

Blockbuster’s injunctive relief claim focused on the goodwill it believed it held in the former Blockbuster locations, specifically the customer database and customers themselves that visited the former Blockbuster locations, and the intellectual property and confidential information that Blockbuster provided to Karioi relating to the operation of video stores, including proprietary operating systems, marketing strategies and pricing structures. Karioi countered that it had significant experience in the video store market before contacting with Blockbuster and converting the two former Blockbuster locations to Blockbuster video stores, and, therefore, much of the goodwill, customer database and other expertise pre-dated Blockbuster. Karioi also claimed that Blockbuster’s real benefit to them was its superior buying power with the movie studios, which was not at issue in connection with the covenant not to compete.

Ultimately, the court took a pragmatic approach that both recognized that Blockbuster had added value to Karioi’s business and had certain interests that should be protected, but also recognized that Karioi was not a typical franchisee that learned the business solely from its franchisor. The court rejected the full injunctive relief requested by Blockbuster deeming it overbroad with respect to protecting Blockbuster’s legitimate interests in the goodwill, and noting that if the full restraint of trade was enforced, the two former Blockbuster stores would have to close and their staff terminated. However, the court recognized that (a) the customer base grew at the former Blockbuster locations while they were operated under the Blockbuster brand due in part to Blockbuster’s branding and marketing efforts in support of the Blockbuster brand; and (b) Blockbuster was entitled to generally protect is intellectual property and confidential information. Therefore, the court ordered that Karioi and its directors could not use any part of any database, including the customer database of the two former Blockbuster locations. While some relief was granted and Karioi’s new business hindered to some extent, the failure to obtain injunctive relief and enforce its post-termination noncompetition provisions was a blow to Blockbuster and foretells that franchisors in Australia must be wary of enforcing post-termination covenants against competition where the franchisee had prior experience or operations in a similar business.

B. China Competition Law

China was one of the last major world economies to establish a general competition law regime. After over a decade of protracted debate, the Standing Committee of the National People’s Congress finally adopted the Anti-Monopoly Law (the “Anti-Monopoly Law”) on August 30, 2007, which went into effect on August 1, 2008. It was the country’s first comprehensive

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174 Id.
175 Id.
176 Id. at 44-47.
177 Karioi supra note 171 at 48-50.
178 Id. at 50.
179 Id. at 58-60.
180 Id.
181 Id. at 60-62.
182 Id. at 68-69.
competition law. Before the Anti-Monopoly Law, China had enacted several laws that dealt with certain aspects of competition law issues, including the 1993 Anti-Unfair Competition Law (which prohibits certain anti-competitive behaviors aimed at competitors), the 1997 Price Law (which focuses on certain price-related anti-competitive behaviors) and the 1999 Bidding Law (which regulates bidding practices to promote competition).

The first draft of the Anti-Monopoly Law was prepared by the Ministry of Commerce’s predecessor in 1994. The version ultimately adopted, after much public debate, was modeled after the EU competition laws. As such, readers will find the discussion of many elements of China’s Anti-Monopoly Law familiar given its European origin; however, as with most things Chinese, China’s Anti-Monopoly Law has many elements that are of “Chinese characteristics.” Most importantly, the regulators, when enforcing the Anti-Monopoly Law, are asked to take China’s industrial policies into account. In addition, the Anti-Monopoly Law has been, and will be, interpreted and enforced within the context of the Chinese political, economic, legal, and cultural environment. As such, any speculation of how particular rules will be interpreted or enforced based on the interpretation or enforcement of similar rules in other more developed jurisdictions (including the European Union) must remain as speculation only.

At this time, it is simply too early to predict the outcome of a number of competition law issues, given that the Anti-Monopoly Law remains in its infancy (despite its rapid development in the last five years), and much of the jurisprudence remains to be developed. With the development of its competition law enforcement agencies and, perhaps more importantly, with the much-anticipated private right of action (and its increasing use), coupled with its position as the world’s second largest economy, China is poised to become an “important” competition law jurisdiction, along with the United States and the European Union.

China enacted the Anti-Monopoly Law amid the country’s continued economic reforms and the transformation from a planned economy into one that is market-based. In the Anti-Monopoly Law’s first four years, enforcement actions focused on merger notifications. This merger notification regime is similar to that of other developed jurisdictions such as the

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187 For a comparative study of the competition laws in China and the EU, see Frank Schoneveld et al., A Comparison of the Competition and Distribution Rules of China and the European Union, at 3-13 (Distribution and Franchising Committee, ABA Section of Antitrust Law, Feb. 2013).
188 The Anti-Monopoly Law’s enforcement is separated into three agencies – the Ministry of Commerce (merger notification), the State Administration of Industry and Commerce (non-price related activities), and the National Development and Reform Commission (price-related activities).
189 For example, one of the exemptions from price maintenance prohibition is if such arrangement is for the purpose of “safeguarding the appropriate interest in foreign trade and foreign economic cooperation.” Such exemption can be easily understood if placed in the broader context of China’s efforts to promote its export industry, a key to its economic development. See, China Anti-Monopoly Law supra note 183 at art. 15.6.
190 As an example, given the high inflation rate, it has been reported that Chinese government has put pressure on big retailers and other companies that supply “key consumer products” (e.g., oil companies) to keep their price from rising too fast. Many of China’s biggest super markets and convenient stores have franchised operations, and these franchisors have been “strongly encouraged” by the government to control their franchisees’ prices. Although this is seemingly contradictory to the principles of China’s competition laws, the authorities view such intervention as being a vital part to their claim to power.
191 See China Anti-Monopoly Law supra note 183 at art. 50.
European Union and the United States. The much publicized rejection of Coca Cola’s proposed acquisition of Chinese fruit juice maker Huiyuan is a high profile example of such enforcement.\(^{192}\)

In recent years, however, with the maturing of the merger notification regime, Chinese regulators and courts have started turning their attention to anti-competitive behaviors in the marketplace, evidenced by an increasing number of implementation rules and high profile cases in this area. In the last week of 2010, the National Development and Reform Commission (“NDRC”) issued the “Anti-Price Monopoly Rules,”\(^{193}\) and the State Administration of Industry and Commerce (“SAIC”) issued three rules implementing its mandate to enforce non-price non-merger related provisions under the Anti-Monopoly Law.\(^{194}\)

As such, franchisors and their advisors should examine their franchise agreements for use in China, including those that are already concluded, to determine whether any change, either in the agreements themselves or, perhaps more likely, in the way that franchisor interacts with its Chinese franchisees, is necessary to avoid running afoul of the Anti-Monopoly Law.

1. Resale Price Maintenance

The Anti-Monopoly Law prohibits resale price maintenance (“RPM”) that arises either as horizontal agreement\(^ {195}\) or a vertical agreement.\(^ {196}\) In addition, the Anti-Monopoly Law prohibits minimum price restrictions.\(^ {197}\) However, it is not clear whether the Anti-Monopoly Law views RPM as hardcore or \emph{per se} violations, as the Anti-Monopoly Law provides a set of exemptions for RPM.\(^ {198}\) These exemptions apply to all types of horizontal and vertical agreements, not just price restrictions. Examples include technological improvement, research and development, efficiency enhancement and public interest. In addition, the Anti-Monopoly Law contains a general exemption for acts that are undertaken “in accordance with intellectual property laws, regulations and administrative rules, except for any abuse of such intellectual property rights to exclude or restrict competition.”\(^ {199}\)

\(^{192}\) According to its spokesman, as of May 24, 2013, the Ministry of Commerce received 698 merger notifications. Of the 627 applications that it accepted, it granted unconditional approval to 562 applications; granted conditional approval to 16 applications; and rejected only 1 application. Therefore, as of May 2013, the rejection of Coca Cola’s acquisition of Huiyuan remains the first and only rejection under China’s merger notification regime.


\(^{195}\) China Anti-Monopoly Law supra note 183 at art. 13.1.

\(^{196}\) Id. at art. 14.1.

\(^{197}\) Id. at art. 14.2.

\(^{198}\) Id. at art. 15.

\(^{199}\) Id. at art. 55.
Given these exemptions, it is likely that China will view RPM in a manner similar to that of the United States by applying a US-style benefits and harm test – that is, the "Rule of Reason" analysis, particularly if such restrictions are in a franchise relationship, which at its heart is a license of intellectual property rights.

This view has been confirmed, to some degree, by recent cases and enforcement actions. In *Rainbow v. Johnson & Johnson Medical*, Johnson & Johnson Medical (China) Ltd ("J&J") was sued by its former distributor, Beijing Ruibang Yonghe Technology Trading Co., Ltd. ("Rainbow"), alleging resale price restrictions on J&J sutures distributed by Rainbow. The Shanghai First Intermediate Court handed down its ruling in May 2012, dismissing the damages claims of the distributor. The Court requested market and product-related information to assess whether the RPM allegations had the effect of restricting or eliminating competition. The distributor was unable to prove harm to the competition. J&J, on the other hand, demonstrated that there were many suppliers of the same products in the upstream market, and thus there was no harm to competition. It is apparent from the Court's approach that it did not view the RPM as illegal *per se*. The case is now on appeal to the Shanghai High Court.

In January 2013, two Chinese premium liquor distillers (Maotai and Wuliangye) were investigated by China's antitrust regulators, shortly after these two companies penalized some of their distributors for selling under their minimum retail price. Upon investigation, both companies announced that they had withdrawn the penalties and would reorganize their sales practices to comply with the Anti-Monopoly Law. In February 2013, two provincial competition regulators (in the province where the manufacturers were located) issued fines of RMB247 million (approximately USD40 million) and RMB202 million (approximately USD33 million), which figures represented 1% of their respective annual sales of the products in question. In one of the announcements, the regulator stated that the RPM restricted or eliminated competition. Because the regulator issued such fines with a finding that the RPM restricted or eliminated competition, this suggests a reluctance to consider RPM to be an automatic violation, or one that need not include a determination that competition was distorted, restricted or eliminated.

However, franchisors should not take comfort in assuming that, because the courts and regulators will review any RPM under a rule of reason analysis, they would likely be able to justify their RPM arrangements in China. Aside from the exemptions provided for under Article 15 of the Anti-Monopoly Law, which tend not to be relevant in the franchising context, there has not been any clear guidance as to what would justify a RPM in a vertical arrangement. NDRC's Anti-Price Monopoly Rules purposefully shied away from providing any additional clarity on vertical price restrictions. It has been reported that China is in the process of drafting guidelines on vertical agreements and available exemptions and defenses. These guidelines may provide more clarity on how China will evaluate the legality of RPM. Before such guidelines become available, Chinese regulators and courts will continue to assess allegations of RPM on a case-by-case basis, and it is even possible that they might view RPM on a *per se* violation basis, not under a rule of reason analysis.

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201 For related news coverage, see, e.g., 茅台和五粮液因价格垄断被罚4.49亿元 [*Maotai and Wuliangye are Fined RMB 449 Million*], available at: http://news.xinhuanet.com/2013-02/19/c_124364847.htm.
In that context, it is worth noting that in a pre-Anti-Monopoly Law era franchise case, an appellate court in Anhui province held that a franchisor violated the Anti-Unfair Competition Law and Price Law by penalizing its franchisee for selling products below its prescribed minimum prices. In *Hefei Nanxiang Automotive Distribution Company v. South East Automotive Group*, the franchisor, South East Automotive Group, entered into a franchise agreement with the car dealership, Hefei Nanxiang. To prevent its franchisees from selling cars below its prescribed prices, the franchisor required all franchisees to deposit the equivalent of approximately USD35,000 with it as a “guaranty,” which would be forfeited to the franchisor if the franchisee violated the price restrictions. When this actually happened, the franchisee sued the franchisor for the forfeited deposit. Both the trial court and appellate court found for the franchisee, on the ground that the franchisor violated the price restriction prohibitions in the Anti-Unfair Competition Law and Price Law (which provisions are similar to those in the Anti-Monopoly Law). However, neither court offered much reasoning for its decision, and seemed to have taken a *per se* violation stance towards the RPM practice alleged in the case. In addition, the franchisor was imposing price restrictions as part of its pricing cartel agreements with several of its competitors, which surely made its case considerably weaker.

In a more recent case, according to a series of media reports in 2012, Daimler’s China joint venture Beijing Benz was investigated by China’s competition regulator for imposing minimum resale price requirements on its dealers. Though no official announcement was made on this investigation, reports indicated that the automaker revised its dealership contracts and structurally reformed its Chinese distribution practices by eliminating the retail pricing restrictions.

### 2. Product Sourcing

The Anti-Monopoly Law provides that a company with dominant market power is prohibited from engaging in tying (or “bundling,” as such practice is commonly referred to in China), unless some justifications exist. In addition, the Anti-Monopoly Law prohibits a company with dominant market power to require its counterparty to purchase from its designated suppliers, unless some justifications exist. The implementation rules further clarify that regulators would see a tying arrangement as unjustified if it is not in accordance with industry practice, consumer habit or the functions of respective products. And illegal tying could exist if there is no explicit requirement/agreement, if it is achieved by means such as pricing discount.

NRDC’s Anti-Price Monopoly Rules state that justifications for such restrictions could include: (a) ensuring product safety and quality; (b) maintaining brand image or to improve service; or (c) achieving significant cost saving, improve efficiency, and share with the consumers the benefit derived from such savings/improvement. SAIC’s Rules against Abusing Dominant Market Position instruct regulators, in determining the existence of justifications, to consider whether the relevant conduct is carried out in the party’s ordinary course of business,

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202 Although this case was reported in the news media, the full decision was not published by the court. Baohe District Court of the Hefei, An Hui. For an example of the news coverage, see He Fei Evening News, Apr. 28, 2005.


204 China Anti-Monopoly Law supra note 183 at art. 17.5. See also SAIC Rules against Abusing Dominant Market Position, at art. 6.

205 Id. at art. 17.4. See also SAIC Rules against Abusing Dominant Market Position, at art. 5.2; NDRC Anti-Price Monopoly Rules supra note 193 at art. 14.

206 SAIC Rules Against Abusing Dominant Market Position supra note 194 at art. 6.1.

207 NRDC Anti-Price Monopoly Rules supra note 193 at art. 14.
and how such conduct might affect economic efficiency, public interest and economic development.\textsuperscript{208}

To determine whether a party has “dominant market power,” the Anti-Monopoly Law and its implementation rules list factors that include, among other things: (a) market share and the competition in the relevant market; (b) the ability to control distribution market and the supply market; (c) the party’s financial and technological capacities; (d) the reliance of others on the relevant party; and (e) the threshold for market entrance.\textsuperscript{209} It is not clear whether a Chinese regulator or court would narrowly define a relevant market as being specific to a franchisor’s brand; most writings on this subject recommend following the approach taken by the United States and the European Union on this subject, which would suggest that the relevant market would be broadly defined to include other franchise opportunities.

However, it is important to note that although the Anti-Monopoly Law only regulates this issue if the franchisor has dominant market power, the Anti-Unfair Competition Law, which prohibits tying (but not exclusive sourcing from designated parties), does not have such a precondition.\textsuperscript{210} In practice, tying cases alleging Anti-Unfair Competition Law typically involve parties that have monopolistic or dominant market power, but the statutory language itself does not restrict the prohibition to such instances. In addition, this prohibition in the Anti-Unfair Competition Law does not have a “justification” based carve-out.

As reported above, the Chinese government is drafting a set of vertical arrangement rules, which hopefully will offer greater clarity on this issue. But such implementation rules cannot be expected to reconcile the differences between Anti-Monopoly Law and the Anti-Unfair Competition Law. As such, franchisors will be well advised to ensure that, when they require their franchisees to purchase exclusively from them, or their designated supplies, such requirement is supported by one or more justifications described in the Anti-Monopoly Law implementation rules. Even though such justifications are not mentioned in the Anti-Unfair Competition Law, one has to assume that their existence will give courts and regulators pause before finding such a sourcing requirement to be in violation, especially if the franchisor does not have dominant market power.

3. Exclusivity, Territories and Non-Competition

As discussed above, exclusive dealing requirements are not permitted under the Anti-Monopoly Law, if the party benefiting from such an arrangement has dominant market power, and if there are no “justifications.”\textsuperscript{211} In addition, SAIC’s Rules against Abusing Dominant Market Position prohibit a party with dominant market power from imposing non-competition obligations on its counterparties, without justification.\textsuperscript{212} Finally, SAIC’s Rules against Abusing Dominant Market Position also prohibit a dominant supplier from imposing “unreasonable restrictions on the territory of sales or customers” without justification.\textsuperscript{213}

\begin{flushright} \textsuperscript{208} SAIC Rules Against Abusing Dominant Market Position supra note 194 at art. 8. \textsuperscript{209} See China Anti-Monopoly Law supra note 183 at art. 18; SAIC’s Rules against Abusing Dominant Market Position, at art. 10; NRDC’s Anti-Price Monopoly Rules supra note 193 at art. 17. \textsuperscript{210} China Anti-Unfair Competition Law supra note 184 at art. 12. \textsuperscript{211} See China Anti-Monopoly Law supra note 183 at art. 17.4; SAIC Rules against Abusing Dominant Market Position, at art. 5.1. \textsuperscript{212} SAIC Rules Against Abusing Dominant Market Position supra note 194 at art. 5.3. \textsuperscript{213} Id. at art. 6.3. \end{flushright}
As discussed in Section IV.B.2 above, it is not clear whether the Chinese regulators or courts will define the relevant market as narrow as a brand-specific market. Even if they do (which seems unlikely given the development of competition law jurisprudence up to this point), franchisors would still be able to justify the exclusive dealing/non-compete obligations by invoking one or more justifications listed in the implementation rules.

The Anti-Monopoly Law does not explicitly regulate post-term non-competition provisions. The Anti-Monopoly Law does, however, prohibit a party with dominant market power from “imposing unreasonable trading conditions.”\(^{214}\) SAIC’s Rules against Abusing Dominant Market Position further elaborate that such “unreasonable trading conditions” could include “contract period, payment methods, product transportation and delivery methods, or methods of providing services.”\(^{215}\) It is not clear whether regulators and courts will use these rather vague concepts in determining the legality of post-term non-competition provisions.

Many commentators have suggested that, in China, non-competition obligations in franchise agreements should be viewed similar to such obligations in an employment agreement, although a few commentators have expressed disagreement to this approach.\(^{216}\) In general, most commentators have suggested post-term restrictions that are no more than two to three years in length, and are geographically tailored (considering the location of the original franchised business), should be enforceable. Many have further suggested that, similar to employment situations, for post-term non-competition obligations to be enforceable, the franchisor will need to provide compensation to the restricted former franchisee.\(^{217}\)

It should be noted that the competition laws, in addition to possibly limiting non-compete covenants, can also aid franchisors in pursuing former franchisees who misuse the franchisors’ intellectual property rights after the termination of the franchise agreements. In *Fornet v. Xinyuan You*, the franchisor (of a dry cleaning system) successfully persuaded the Jiangsu High Court that the use by its former franchisee of the “Fornet” name (and its Chinese translation) was a form of “unfair competition” prohibited under the Anti-Unfair Competition Law.

C. GCC Competition Laws

The Gulf Cooperation Council (“GCC”) consists of six member countries: Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and United Arab Emirates. All six GCC countries are members of the WTO.\(^{219}\) Four of the six member countries have passed some form of competition law (some more comprehensive than others) aimed at promoting competition and with the objective of complying with the WTO requirements.

As the analysis below illustrates, when it comes to competition law concerns, GCC members by and large only focus on companies with dominant market positions, and whether their conduct would restrict trade. It is far from certain how the regulators and courts will

\(^{214}\) China Anti-Monopoly Law *supra* note 183 at art. 17.5.

\(^{215}\) SAIC Rules Against Abusing Dominant Market Position *supra* note 194 at art. 6.2.

\(^{216}\) See, *e.g.*, 肖朝阳 Xiao chao yang, 特许经营法律实务 [Practice of Franchise Law], 中信出版社 CITIC Press (2002), at p.138-140.


interpret what the relevant markets are in the franchising context, as all the competition laws in the region are quite new (the first was adopted in Saudi Arabia in 2004), and guidance from the regulators and courts has been limited. Assuming such relevant markets will not be determined as brand-specific (which seems like a reasonable assumption), it appears that foreign franchisors should be able to implement their franchise programs in this region with limited adaptations necessary to comply with local competition laws.

The Kingdom of Saudi Arabia was the first GCC country to introduce a competition law by passing Royal Resolution No. (M/25), dated June 22, 2004, which came into force on December 31, 2004 (“Saudi Arabia Competition Law”). The law and principles apply generally to all businesses operating in Saudi Arabia, including foreign companies, except for public corporations and companies wholly owned by the Kingdom of Saudi Arabia.\(^{220}\)

Qatar issued Law No. 19/2006 Concerning Protection of Competition and Prevention of the Monopolistic Practices on June 29, 2006 (“Qatar Competition Law”). The provisions do not apply to sovereign ventures of the State, or to the ventures of institutions, groups, companies or entities subject to State direction and supervision.\(^{221}\)

On April 29, 2007, Kuwait adopted Law No. 10/2007 Concerning Protection of the Competition, which became effective on February 22, 2009 (“Kuwait Competition Law”). Executive Regulations accompanying this law have also been brought into force under Cabinet Resolution nbr. 106 of 2009. Government-owned projects, projects required by a particular law, cooperation between companies aimed at facilitating market activity, and research and development activities are not considered to violate the Kuwait Competition Law.

On October 10, 2012, the UAE passed Federal Law No. 4 of 2012 on the Regulation of Competition, which came into effect on February 23, 2013 (“UAE Competition Law”). The law aims to protect and enhance competition within the UAE and companies have a six month transitional period (until August 23, 2013) to ensure that their agreements and practices are in compliance with the new law. The actions of federal and local governments, and any state-owned establishments are expressly excluded from the application of the UAE Competition Law.\(^{222}\) Small and medium establishments (SMEs) are also excluded from the law.\(^{223}\) Further, certain sectors have been carved out from the scope of the application of the UAE Competition Law, including some of the most prominent in the UAE: telecommunications, financial services, cultural activities (readable, audio and visual), pharmaceutical, utilities, waste disposal, transportation, oil and gas, as well as postal services.\(^{224}\)

Bahrain has no competition law in force; however, certain laws refer to the concept of competition (for example, Law 7 of 1987 (Commercial Code)). Similarly, Oman has no specific competition law, although Law 55 of 1990 (Commercial Law) contains certain provisions relating to unlawful competition. Nevertheless, both countries do have general statutory provisions restriction deception and fraud in disposing of goods, which could be interpreted to cover the issues discussed in this paper.

1. **Resale Price Maintenance**

\(^{220}\) Saudi Arabia Competition Law, at art. 3.
\(^{221}\) Qatar Competition Law, at art. 6.
\(^{222}\) UAE Competition Law, at art. 4(3).
\(^{223}\) Id. at art. 4(1).
\(^{224}\) Id. at art. 12.
There are a number of restraints relating to price maintenance in Saudi Arabia (under the Saudi Arabia Competition Law and its Implementing Regulations). Notably, the Saudi Arabia Competition Law bans any firm that enjoys a “dominant market position” from carrying out any practice that restricts competition among firms, including: (i) controlling prices of commodities and services meant for sale by increasing, decreasing, fixing their prices or in any other manner detrimental to lawful competition; (ii) influencing the normal price of sale, purchase, or supply quotations of commodities and services whether in government or non-government bids or auctions; and (iii) limiting flow of goods and services to or from markets totally or partially through hiding or storing them without right, or refraining from dealing with them. Further, Article 5 of the Saudi Arabia Competition Law bans firms with a dominant market position from restricting competition by engaging in a number of activities, including selling a commodity or service at a price below cost, with the intention of forcing competitors out of the market, and imposing restrictions on the supply of a commodity or service, with the intention of creating an artificial shortage in its availability in order to raise prices.

Similarly, in Qatar, it is forbidden to enter into agreements or undertake practices that violate the rules of competition, including (among other things), manipulating the prices of the products being handled, either by raising, lowering or fixing those prices, or by any other means. Additionally, persons who exercise control must not misuse it through unlawful practices, which include: refraining from, limiting or hindering the handling of products, either for sale or purchase, in such a way as leads to the imposition of artificial prices; and selling products below their marginal cost or average variable cost.

In Kuwait, all agreements, contracts and practices which are detrimental to free trade or competition are prohibited. Some prohibited practices include: (i) limiting the free flow of goods or services by increasing, decreasing, or fixing prices, or by other means harmful to competition; (ii) creating a sudden abundance of the product resulting in an artificial market price which affects other competitors; and (iii) selling products at a price lower than their actual cost with the intention of causing harm to competing producers.

The UAE Competition Law prohibits “restrictive agreements.” Prohibited restrictive agreements include (but are not limited to) agreements that fix prices, rig bids, divide markets, allocate customers, preclude or impede entry into a business or business activity, refuse purchases from, or supplies to, another firm, limit the free flow of goods or services in a relevant market, limit terms of sale or purchase, or prohibit or limit production, development, distribution, marketing or other investments. Certain agreements that may otherwise be seen as

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226 In this context, “domination” refers to a situation where an entity or a group of entities has a market share of at least 40% of total sales for a period of 12 months and/or the entity or group of entities is in position to influence the prevailing price in the market.
227 Saudi Arabia Competition Law, at art. 4.
228 Id. at art. 5. Additionally, The Competition Protection Council may exempt certain practices and agreements violating competition (as set forth in Articles 4 and 5 of the Implementing Resolutions) which lead to improvement in performance of entities and benefit customers to an extent greater than the effects of restriction of free competition, if the relevant entity or entities submit the request for exemption in writing along with supporting justifications.
229 Qatar Competition Law, at art. 3(1).
230 In this context, “control” means “the power of a person, or group of persons acting together, to dominate the market and effectively to influence prices and the volume of products on offer, while their competitors have no power to prevent this.”
231 Kuwait Competition Law, at art. 4.
232 Id.
233 UAE Competition Law, at art. 5.
“restrictive agreements” are exempted from the application of the law. Such exempt agreements are referred to as “weak-impact agreements” and include agreements entered into between entities whose overall market share does not exceed a certain percentage of the total overall transactions in the relevant market.234

Bahrain and Oman have no similar restrictions related to pricing. However, in Bahrain, the Ministry of Industry and Commerce may investigate customer complaints regarding prices.

2. Product Sourcing

Unlike resale price maintenance, by and large, there is no indication that sourcing restrictions is high on the list for GCC member countries in terms of competition law issues.

The Implementing Regulations of the Saudi Arabia Competition Law provide that "[a]ny...agreements...between competing or potentially competing entities which violate, restrict or prevent competition shall be prohibited, particularly those...[whose purpose is] setting a limit for production of goods or the rendering of services."235

The Qatar Competition Law provides that it is forbidden to undertake practices that would limit the freedom of products to enter or exit markets, either completely or partially, by concealing them, refusing to handle them despite the fact that they are available, or stockpiling them without justification.236 Further, no agreements may restrict production, manufacture, distribution or marketing of products; or limiting the distribution, volume or kind of services, or placing conditions or restrictions on their supply.237 Persons who have control may not impose the obligation not to manufacture, produce or distribute a product for a set period or set periods of time,238 and persons who have control or domination must not fail to make a scarce product available when its availability is economically viable.239

In Kuwait, as discussed above, the Kuwait Competition Law prohibits any practice that would limit the free flow of goods or services by increasing, decreasing, or fixing prices, or by other means harmful to competition.

As discussed above, the UAE Competition Law prohibits restrictive agreements, which may include agreements that preclude or impede entry into a business or business activity, refuse purchases from, or supplies to, another firm, and limit the free flow of goods or services in a relevant market.

3. Exclusivity, Territories and Non-Competition

In Saudi Arabia, a firm with dominant market power may not restrict competition with other firms by, among other things, dividing or allocating markets for selling or purchasing commodities and services pursuant to any of the following criteria: geographical regions, distribution centers, type of clients, and seasons and time periods.240 Also, firms may not refuse

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234 Id.
235 Implementing Regulations to Saudi Arabia Competition Law, at art. 4(2).
236 Qatar Competition Law, at art. 3(2).
237 Id. at art. 3(6). For example, persons who exercise control cannot fail to make a scarce product available when its availability is economically viable.
238 Id. at art. 4(4).
239 Qatar Competition Law, at art. 4(8).
240 Saudi Arabia Competition Law, at art. 4.
to deal with another firm without justification in order to restrict its entry into the market. An entity with a market share below 40% can still be “dominant” if it is in a position to influence prevailing prices. Further, a merger or acquisition which may result in an entity becoming dominant must be cleared by the Competition Protection Council.

In Kuwait, any natural or artificial person who is capable of influencing the market price of a product or service, through control of more than 35% of the market share of business, is also prohibited from engaging in practices that limit competition. Also, an individual or entity must obtain approval from the Authority for the Protection of Competition prior to any acquisition that may lead to its control over a specific market. Article 4 of the Kuwait Competition Law also provides that "preventing or impeding a person from practicing any commercial activity in the market or ceasing to do so" or "dividing the market by categorizing them according to geographical location, distribution center, type of customer or commodity, season or time period with the intent of harming competitors" is a prohibitive practice.

The Qatar Competition Law provides that it is forbidden to prevent or hinder any person from practicing economic or commercial activity in the market, or to divide or allocate product markets on the basis of geographical area, distribution centers, type of customers, seasons or time periods, or goods.

Similarly, the UAE Competition Law prohibits the use of a dominant position in a market to restrict competition. Actions that can constitute an abuse of dominance include but are not limited to: imposing resale price terms, predatory pricing, discriminatory pricing, refusing to deal, compelling others not to deal, restricting supply, conditioning the sale of a good or service on the purchase of another good or service, disseminating false information about products or prices as well as artificially increasing or decreasing quantities in a market. A dominant position is defined by reference to an entity's share in a relevant market and includes a position where an entity can, by itself or in collaboration with other entities, control or affect the relevant market – however, the threshold has not yet been set by the Cabinet.

D. Other Notable Jurisdictions

From our discussion above regarding Australia, China and GCC, one can see that, while the competition laws in these jurisdictions have taken quite divergent forms, on the issues that are being examined in this paper, they take more or less the same approach, which approach also, at some level, resembles the approach taken elsewhere in the world.

For example, it is perhaps not surprising that Israel seems to have taken a page from the European Union’s competition law regime. Its Restrictive Trade Practices Law prohibits a number of practices that are perceived to be anti-competitive, including resale price maintenance, sourcing restrictions and exclusivity/non-compete requirements. The regulators have issued a set of “block exemption” rules specific to franchise agreements, which allow such restrictions in franchise agreements, if the agreements meet certain conditions. However, one of the conditions for claiming the exemptions is that the duration of the franchise agreement

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241 Id.
242 Id., Kuwait Competition Law, at art. 4.
243 Id.
244 Id., Qatar Competition Law, at art. 3(4).
cannot be longer than 10 years,\textsuperscript{247} which could pose issues for franchise systems with large upfront investment requirements and hence typically longer terms.

Indonesia took a somewhat similar approach. Its general competition law is Law No.5 of 1999 on the Prohibition of Monopolistic and Unfair Business Practices (the “Indonesia Competition Law”). The regulatory agency, the Commission for the Supervision of Business Practices (KPPU), issued Decree No. 57/KPPU/Kep/III/2009, which essentially exempts franchise agreements from the coverage of the Indonesia Competition Law. However, just like Israel, such exemption is not absolute. For example, resale price maintenance clauses are not exempted, because the regulators do not view those arrangements as within the scope of a franchise/license relationship; rather, they view those as being in the “distribution” arena and therefore should still be subject to the general Indonesia Competition Law. Under the Indonesian Competition Law, RPM is not \textit{per se} illegal; rather, scrutiny is triggered only if the party has dominant market position, and still then it will be reviewed under a rule of reason standard.\textsuperscript{248} Similarly, sourcing restrictions and exclusivity/non-compete requirements will be allowed, as long as there are reasonable justifications for such clauses tied to the uniformity and performance of the franchise system.

Pakistan adopted its first competition law in 2010 (the “Pakistan Competition Law”).\textsuperscript{249} However, while the Pakistan Competition Law contemplates the possibility of “block exemptions” for certain categories of agreements (including, presumably, IP license or franchise agreements),\textsuperscript{250} the agency (Competition Commission of Pakistan) has yet to issue such block exemptions. As such, technically all exclusivity/non-compete provisions in franchise agreements are not allowed under the Pakistan Competition Law.\textsuperscript{251} The Pakistan Competition Law does provide for an individual case-by-case exemption process,\textsuperscript{252} which must be completed before such restrictions could be put in place by the franchisors and franchisees.

Instead of the “general prohibition + exemption” approach adopted by the countries mentioned above, Korea opted to issue its Fair Franchise Transactions Act\textsuperscript{253} under the auspices of its competition law – the Monopoly Regulation and Fair Trade Act (“MRFTA”).\textsuperscript{254} As such, the Fair Franchise Transactions Act itself, rather than the general MRFTA, should be consulted first for guidance on a number of restrictions that are relevant to the issues discussed in this paper. However, the Fair Franchise Transactions Act does not cover every facet of these issues – for example, while the Fair Franchise Transactions Act prohibits price fixing,\textsuperscript{255} it is silent on maximum or minimum price restrictions. These issues instead are regulated in the MRFTA – minimum pricing is \textit{per se} illegal, while maximum pricing will be reviewed under a rule of reason analysis.\textsuperscript{256}

\textsuperscript{247} Id. at art. 3(9).
\textsuperscript{248} See, Indonesia Competition Law, at art. 8.
\textsuperscript{249} The Competition Act, 2010 (promulgated by Majlis-e-Shoora (Parliament) and signed by the President on Oct. 6, 2010, effective Oct. 13, 2010), \textit{available at} http://www.cc.gov.pk/index.php?option=com_content&view=article&id=60&Itemid=104
\textsuperscript{250} Id. at art. 9.
\textsuperscript{251} See id. at art. 4.
\textsuperscript{252} See id. at art. 5.
\textsuperscript{253} Fair Franchise Transactions Act (enacted on May 13, 2002 as Law No. 6704, and revised on Jan. 20, 2004 as Law No. 7109), \textit{available at} http://www.jftc.go.jp/eacpf/01/Korea-franchise.pdf
\textsuperscript{254} Monopoly Regulation and Fair Trade Act (enacted on Dec. 31, 1980 as Law No. 3320, last revised on Dec. 31, 2004 as Law No. 7315), \textit{available at} http://www.jftc.go.jp/eacpf/01/Korea-monopoly.pdf (hereinafter “MRFTA”).
\textsuperscript{255} Fair Franchise Transactions Act, at art. 12.(1).2.
\textsuperscript{256} MRFTA \textit{supra} note 254 at 7.
V. CONCLUSION

If you have read the entirety of this paper, you surely understand that attempting to comprehend and apply foreign competition law to franchise agreements and relationships in a vacuum is nearly impossible. There are jurisdictions such as Brazil and Mexico that have new, extremely broad competition laws that would seem to be traps for the unwary, but to date have had little practical impact on franchising in these countries. Of course, only time will tell if that continues, and the very fact that these countries recently overhauled their competition laws is evidence that perhaps international interest in competition issues is growing as the global economy expands and the haves and have nots battle within and across borders.

In other jurisdictions, such as Australia and the EU, competition law is the underlying source of franchise law and seemingly looms over all that franchisors do, with practitioners over the years actively keeping up with and seeking guidance on third line forcing, block exemptions and related case law. Still other countries such as China and Indonesia have new or amended laws that are likely ripe for greater enforcement due to political, economic and other reasons stemming from their blossoming economies and (relative) opening up to world trade.

In all cases, the authors would be remiss in not reiterating that there is no substitute for obtaining current, local advice from franchise and/or competition law counsel when entering into these markets, especially if your system is of a size that might satisfy market power definitions or your contractual or product related controls are of the type that may run afoul of pricing, product sourcing or territorial aspects of an international competition law.
Mr. Lauer is a partner in the Haynes and Boone, LLP Franchise and Distribution Group focusing on domestic and international franchise transactions. Mr. Lauer previously served as in-house franchise and litigation counsel for a large Texas-based restaurant franchisor and has represented clients in: the structuring and negotiation of various franchise transactions, including international franchise and master franchise agreements in Europe, the Middle East, Asia and Central and South America; the preparation, interpretation and enforcement of franchise, license and distribution agreements and related documentation both domestically and abroad; advising clients regarding matters of compliance with domestic and international franchise registration and disclosure laws; resolution of disputes arising between franchisors and franchisees; the establishment and structuring of new franchise systems; and a Chapter 11 bankruptcy filing by a franchisor and subsequent sale of franchise assets through a bankruptcy court approved auction and sale. Mr. Lauer was named to Chambers, Global Franchising, Band 3, 2011; Band 4, 2012; Band 3, 2013; Chambers USA, Franchising (Nationwide), Up and Coming, 2012; the International Who's Who of Franchise Lawyers, Law Business Research, 2010 through 2013; The Best Lawyers in America® for Franchise Law in 2008 through 2013; and a “Texas Rising Star” by Law & Politics Magazine and Texas Monthly from 2005 through 2012. Mr. Lauer is also the speaker for the Texas Bar Association's Ten Minute Mentor video tutorial on "What Every Texas Attorney Should Know About Franchise Law". He is a member of the ABA Forum on Franchising (and former member of the International Division’s Steering Committee from 2008 to 2011), and a former vice-chair of the franchise and distribution section of the Dallas Bar Association. Mr. Lauer is a 1997 cum laude graduate of the St. Mary's University School of Law where he served as an Associate Editor of the St. Mary's Law Journal, and a 1994 graduate of Trinity University in San Antonio, Texas.
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As a lawyer, he has, over the years, advised on the structure of a number of well-known national and international franchising systems and the expansion of those systems nationally and internationally. Karsten Metzlaff is a member of the International Bar Association (IBA), the German Franchise Association (DFV) and the European Franchise Federation (EFF) and its Legal Committees. He has lectured and written on many various domestic and international issues of franchising and distribution law. He is the exclusive contributor to the International Law Office Newsletter for franchising in Germany (see www.InternationalLawOffice.com).

Karsten Metzlaff has been named in the latest JUVE edition (2012/2013) on German law firms as one of the leading attorneys in the country in this field. He has been selected again for inclusion in The International Who’s is Who of Business Lawyers, Franchise (2013). He has also been selected for inclusion in the Best Lawyers list for Germany in the practice area of Franchise.
Tao Xu
Partner
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Tao Xu is a partner with DLA Piper’s world-leading Franchise and Distribution practice group, based in the firm’s Northern Virginia and Washington, DC offices.

Mr. Xu devotes his practice to franchising and distribution matters, especially international franchising, licensing and distribution transactions. He counsels a broad range of clients in their international expansions, including master franchising, multi-unit licensing, area development, single-unit licensing and direct investment (both joint venture and wholly owned).

He has an active retail, restaurant, hospitality and leisure practice, advising various clients in connection with multi-unit development transactions in the United States and around the world.

Mr. Xu has been deeply involved in franchising activities in China. He is a member of DLA Piper's US and China joint team, which represents the International Franchise Association in lobbying the Chinese government to adopt a new franchise regulatory regime. He has also represented many US and European clients in entering into the Chinese market, covering such industries as quick-service restaurants, premium dining, lodging, service, retail, real estate service and education.