Legal update on the Franchise Act in the Netherlands

THIS LEGAL UPDATE IS ESSENTIAL READING FOR FRANCHISORS AND/OR FRANCHISEES WITH ANY PART OF THEIR BUSINESS LOCATED IN THE NETHERLANDS

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Does the Franchise Act impact your business?

Are you a franchisor or franchisee? Is your business, or part of it, located in the Netherlands? If you answered yes to either of these questions, you will now have to deal with the Franchise Act, which came into effect in the Netherlands on 1 January 2021 ("Franchise Act").

As from 1 January 2021, all franchise agreements will need to be drafted in line with the Franchise Act. However, a transitional period of two years applies for existing agreements that have been concluded before 1 January 2021 with an expiry date later than **31 December 2022**.

This update will give you a short overview of some important changes under the Franchise Act and information on when you need to make amendments to existing agreements.

Important changes to franchising under Dutch Law

Precontractual phase

An important element of the Franchise Act is strengthening franchisees' information position before the agreement is in place, also known as the "precontractual phase". As of 1 January 2021, franchisors and franchisees are required to share certain information with each other prior to entering into a franchise agreement, and this information in extensive. The requirement is designed to give both parties sufficient opportunities to assess the risks of entering into an agreement.

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The franchisor must provide the franchisee with a draft franchise agreement. More detailed financial information has to be provided, especially by the franchisor. It is recommendable to opt for a Precontractual Information Document, signed by franchisor and franchisee, stating clearly what documents had been made available to the other party.

Standstill period

After receiving all the relevant financial information, such as the draft agreement, a four- week "standstill" period applies. During the standstill period the franchisor may not add extra conditions to the agreement (at the expense of the franchisee), impose financial burdens or obligations or enforce payments.

This period gives the franchisee time to reflect on the draft agreement, carry out necessary research and due diligence, and appoint an expert to review it. Be aware – if the franchisee decides to accept the draft agreement, the franchisor is bound by it.

Duty to inform and right of consent

The Franchise Act also strengthens the franchisee's position after the agreement is in place. The franchisor now has an ongoing information obligation towards the franchisee. If the franchisor intends to amend the franchise agreement or operate a derivative formula and these plans have certain financial consequences for the franchisee, they must inform the franchisee of its intentions. They might even have to get consent from the franchisee before going ahead.

It is possible to include a threshold in the franchise agreement, so that you only need the franchisee's consent for amendments that have financial impact beyond that threshold. This stipulation can prevent you having to get consent for very small amendments.

Legal break-up

The Franchise Act also includes provisions that protect the franchisee if both parties go their separate ways. These include the following conditions.

Non-competition clause

There is a chance that the departing franchisee wants to remain active in the same branch, but will a non-competition clause prevent this from happening? A non-competition clause will now only be valid if it is agreed in accordance within the limits of the Franchise Act. The post-contractual non-competition clause must be strictly necessary to protect the knowhow of the franchise and must be limited to one year only.

Goodwill

As a franchisee, you build up goodwill: the value you add over the years to your company and wider business. The franchise agreement must include provisions that describe how goodwill is determined, what part of it is attributable to the franchisee, and to what extent goodwill is compensated if/when the agreement terminates.

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Transitional rules

Transitional period

There are a number of obligations for the franchisor in the Franchise Act that will require an amendment to franchise agreements. When these amendments need to be made depends on the effective date of the agreement.

The Franchise Act includes a transitional period of two years, at the end of which all existing franchise agreements must be compliant. The two-year transitional rule applies only to franchise agreements that already existed at 1 January 2021 with an expiry date later than 31 December 2022. These franchise agreements must be amended by that date. If an existing franchise agreement has an expiry date earlier than 31 December 2022, the Franchise Act applies immediately in full, meaning that the franchise agreement will need to be amended straightaway if the franchise relationship is continued by parties. Even if, for example, it has been contractually agreed that the existing franchise agreement will be automatically extended beyond 31 December 2022.

In any case, the transitional period applies to the provisions regarding goodwill, the non- competition clause[1], and the right of consent[2], where the franchisees' is financial impact beyond the threshold. Except for these specific provisions, the Franchise Act applies in full for all franchise agreements that exist on 1 January 2021.

Holla legal & tax, in collaboration with TLT LLP, is happy to guide you with implementing the Franchise Act under Dutch law and carrying out the required amendments for existing franchise agreements.

1 Article 7:920 Dutch Civil Code

2 Article 7:921 Dutch Civil Code.

Would you benefit from more information?

In 2020 TLT and Holla legal & tax became strategic alliance partners, joining forces to deliver international cross-border services for business. From an established network of offices in the UK, the Netherlands and beyond, TLT and Holla legal & tax actively share knowledge, expertise and innovation to provide our clients with seamless cross-border advisory, disputes and transactional services.

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