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Obligations Arising from the Conclusion of the Franchise Contract

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Abstract

This study discusses the obligations arising from the conclusion of the franchise contract. It is important because it deals with a topic that has attracted the attention of international legislators, especially because it imposes obligations on its parties. The objective of this study is to identify the obligations that result from concluding a franchise contract, whether those on the franchisor or the licensee, or those mutual obligations on both of them. The franchise contract is one of the new contracts that has been widely used in many countries of the world. The researcher concludes that the conclusion of the franchise contract imposes a set of obligations on its parties. The study concludes with a set of recommendations, the most important of which is that the parties of the franchise contract shall clarify the nature and conditions of the franchise system under the contract, so that consequent problems can be avoided during the implementation stages.

Keywords: Franchise, Obligations on the Parties, Commercial Law, Contract.

Introduction

There is no doubt that the conclusion of contracts imposes a set of obligations on its parties. Likewise, the conclusion of franchise contracts imposes various obligations, some specialized jurists divided them into financial and non-financial obligations, while other jurists went to divide them into obligations on the licensee, obligations on the licensor, and other mutual obligations on both of the two parties (Al-Mulhim, 1996, p. 264).

The obligations resulting from the conclusion of the franchise contract are clear to each of its parties according to the role and objective. If the objective of concluding the contract is to transfer new and modern technical knowledge, the licensor (the franchisee owner) is

obligated in such a case to provide assistance to the other party, which is the licensee, by explaining how to use this knowledge. The obligations arising from franchising contracts are not only binding after the conclusion of the contract, but rather, the conclusion of the franchise contract is preceded by a commitment by its owner to inform the licensee, who is the other party to the contract, about the nature and system of its privileges (Allah, 1979, p. 23).

On the other hand, the conclusion of the franchise contract requires that the licensee maintain confidentiality, which is a basis for the success and continuation of activity in this type of contract. The licensee's use of the franchise entails an obligation to pay a financial amount to its owner (Al-Saghir, 1993, p. 34).

In addition to these obligations, there are a number of reciprocal obligations between the two parties of the contract. This study attempts to identify the obligations arising from the conclusion of the franchise contract. To achieve the objective of this study, the researcher uses the qualitative method as a scientific method that is compatible with this type of studies.

One of the most important studies related to the subject of this study is Sasia's study (2015), which aims to demonstrate the legal nature of the franchise contract and the obligations resulting from its conclusion. The study uses the descriptive analytical method as an approved scientific method in addition to the comparative method to lay the basis of comparison between the Algerian and Tunisian legislations. The study presents the mechanism of concluding the franchise contract and its characteristics, the position of this contract, its legal nature, the obligations of its parties and its expiry and the implications of this expiration. The study recommends the need to amend the Algerian and Tunisian legislations regulating this contract.

Al-Bishtawi's study (2008), entitled: "The Franchise Contract and Its Effects", is considered one of the important studies that dealt with this topic. The study aims to identify the nature of the franchise contract, its effects, obstacles to its application, and the obligations arising on its parties. In order to achieve the general objective of the study, the researcher uses the mixed research method through describing and analysing the nature of this contract and making a comparison between the Egyptian, Jordanian and Palestinian legislations that organize its provisions and demonstrate the obligations resulting from its conclusion. One of the most important results of the study is that this contract has an independent and distinct system from other contracts and behaviours similar to it because it combines several characteristics of many contracts and commercial actions.

Through this study, the researcher explains, in some details, the obligations arising from the conclusion of the franchise contract, through demonstrating the obligations of the franchise owner, and then stating the obligations of the licensee, taking into consideration that there has to be a guarantee to protect each party in the franchise contract (Lapiedra et al, 2012). The study concludes with a demonstration of the mutual obligations between the franchise owner and the licensee, as follows:

Obligations of the Franchise Owner

Here is a set of obligations arising from the franchise contract, where the licensor is committed to a set of obligations that are specific to this contract and differ from other contractual obligations. They are presented as follows:

- **The Licensee about of the Franchise before Contracting**

One of the obligations of the franchise contract is that its owner must inform the licensee before concluding the franchise contract of the nature and location of the franchise system that he owns, so that the licensee can identify all the elements and components of the franchise. Among these obligations, the franchise owner must disclose some information such as data related to the franchisor's company and his experiences. Another obligation of the franchise owner is to inform the licensee of the intellectual property rights he owns related to the franchise before concluding the contract (Al-Ahwany, 1996, p. 68).

- **To Provide Technical Assistance**

In fact, providing technical assistance is the basic and most important element in franchising contracts. This means that the franchisor must, in addition to transferring knowledge, commit to providing assistance in this context, so that the licensee can benefit from the subject of the contract, which is the technical knowledge transferred to him. This also means that the transfer of technical knowledge without the abiding to provide technical assistance may prevent the licensee from using it, and this is what necessitates the licensor to provide the necessary technical assistance to the licensee in order to achieve the objective of the contract (Al-Najjar, 2007, p. 211).

It is worth noting that the obligation to provide technical assistance is achieved once the agreement is completed, i.e. before starting the activity. Among the forms of providing assistance in transferring knowledge before the actual start of the activity are the following:

- Providing training programs on how to manage the franchise business, repair it, and form of sales.
- Establishment of accounting systems.
- Advise users, and establish a marketing department.
- Assistance in choosing a location.
- Creating internal networks and websites and linking them to the Internet.
- Provide a detailed manual for operation.

This obligation requires the licensor to continue to provide technical assistance to the licensee from the beginning of the agreement until the end of the contractual relationship (Al-Najjar, 2007, p. 223).

Licensor's Commitment to Warranty

One of the most important requirements for the success of franchise contracts and to achieve the objective of their conclusion is that the franchisor shall abide by the warranty, as part of his obligation to transfer knowledge upon which the provisions of delivery apply. This means that the provisions of the warranty shall also apply to them, whether it is an exposure, maturity or even a defect warranty. This is explained as follows:

- **Warranty of Exposure Issued by the Franchisor**

The meaning of this warranty is that the owner of the franchise is obligated to refrain from any action that may prevent the licensee's ability to benefit from the subject matter of the contract, even partially, even if the exposure is direct or indirect, and whether the exposure is legal or financial (Baroud, 2008, p. 25).

- **Maturity warranty "Third Party Exposure"**

One of the requirements of enabling the licensee to benefit from the subject matter of the contract is that the franchisor, who is the licensor, is obligated to guarantee payment of the exposure of a third party when the exposure is legal, immediate and not probable. In the case in which the licensor fails to prevent that exposure by giving a right to a third party on the subject matter of the franchise contract that prevents the licensee from benefiting from it, the licensor shall compensate the licensee for the damage he sustained (Al Hadidi, 2006, p. 217).

- **The Warranty against Hidden Defects**

Among the warranties that have been acknowledged as a commitment on the franchise owner is to guarantee the delivery of the entire contract subject without any defect that may make it invalid for what it is allocated to. This means that the licensor is obligated to present the subject matter of the contract "the franchise system" according to what is agreed upon under the contract, i.e. free from any defect. Proofing the defect requires the availability of a set of conditions in order to oblige the franchise owner to compensate the other party, which is that the defect shall be effective, old, hidden, and unknown to the licensee at the time of the conclusion of the contract (Al Hadidi, 2006, p. 220).

Obligations of the Licensee

The franchise contracts have to be governed by a law to settle any dispute between the parties and to prevent any violation of their rights (Bauch, 1994). In exchange for the obligations incurred by the licensor or the owner of the franchise, there is a set of obligations that the licensee shall perform under the franchise contract. This is what the study deals with as follows:

- **Commitment to Maintain Confidentiality**

There is no doubt that the owner of the franchise owns something private for himself to be a true owner of the subject matter of the contract. For example, the owner of the franchise keeps the product's data, shape, specifications and method of production. The franchise contract obliges its owner to provide this technical information to the licensee, and this is a disclosure of the secret that he kept. Therefore, in order to guarantee the rights of the licensor, it is necessary for the licensee to abide by confidentiality a basis and a main condition by which the franchise system is distinguished from other contracts. The licensee is not entitled in any way to discuss or transfer the technical information related to the subject matter of the contract to any other party (Abdullah, 2008, p. 26).

The information that the owner gives to the licensee are protected under law even before concluding the contract (Sitaru, 2013). Therefore, the obligation to maintain confidentiality by the licensee begins from the first moment of the start of negotiations about the subject matter of the franchise, not from the time of signing the contract, as in most contracts (Abdul Salam, 2000, p. 24).

- **Commitment to Pay in Return for the Subject Matter of the Franchise**

There is a payment in return for every contract, work or benefit provided by the owner to others. In the franchise contract, the licensee is obligated to pay for the use of the technical knowledge and the trademark that is used under the franchise contract. The payment obtained by the licensor, the "franchise owner," may be moral through achieving greater

fame for his trademark, expanding the franchise network, and entering new markets with investments. This may result in an indirect financial benefit after that, and there is a direct financial return that the licensor gets from licensees (Ahmed, 1999, p. 34).

In fact, the licensee pays a sum of money after the conclusion of the contract in return for the franchise owner's approval to let the licensee join the franchise system. This amount is paid once when concluding the contract. The licensee is also obliged to pay a sum of money periodically during the validity period of the contract, which means that the licensee remains obliged with the financial return until the expiry date of the contract. In this case, the international obligation may be a monetary amount and it may be in kind, such as a quantity of the commodity of the franchise. In all cases, the return will be in accordance with the agreement between the franchisor and the licensee (Radwan,1990, p. 35).

Mutual Obligations between the Parties of the Contract

In addition to the obligations arising on the licensor and the licensee separately, which were previously mentioned, there are a set of mutual obligations that result from concluding the franchise contract. They are presented as follows:

- **Exclusivity Condition**

The condition of exclusivity is considered a basic condition that characterizes the franchise contract. This condition is intended to grant the licensee the right to monopolize the subject matter of the contract at specific time and region. This means that the franchisor shall refrain from granting any authorization to himself or others to practice the licensed activity during that period and within the that territory (Ammar, 1992, p. 72).

In fact, the previous concept of exclusivity means that there are two scopes for exclusive activity in franchise contracts; the first scope is exclusivity of territory, that is, the licensee exercises the exclusive right in a specific country, continent or place exclusively in accordance with what is agreed upon in the franchise contract, so that he is the only one who has the exclusive right of the Franchise in that territory (Abdul Salam, 2000: 31).

The other scope in franchising contracts is the exclusivity of supply, whereby the parties of the contract supply each other through purchasing production requirements as a reciprocal obligation. The licensee undertakes not to supply the production requirements of goods and services except from the owner of the franchise, who is obligated to supply the necessary goods and services necessary for his activity or from another supplier approved and specified by the franchise owner (Al-Hadidi, 2006, p. 223).

- **Exchanging Improvements**

The improvements within the scope of the franchise contract mean: "Every subsequent development in the elements of the subject matter of the contract" (Al-Najjar, 2007, p. 223).

It is known that the franchise is a contract that has its effect through time, not immediately, because it depends on the development of its original owner. Since the element of time is important, the franchise evolves and changes from time to time and thus can be developed by the owner of the franchise. The development and improvement is not limited to the owner of the franchise who developed it, but extends to the licensee as well (Al-Mulhim, 1996, p. 264).

In this context, some have narrowed the scope of the improvements that the licensee can benefit from, linking them to those subsequent improvements related to the technical

knowledge in the contract. Others consider that limiting improvements to knowledge only without the rest of the contract elements empties the latter of its content (Al-Hadidi, 2006, p. 227).

The researcher adopts the opinion that the improvements that come in the franchise system include all the developments and improvements related to the elements of the contract and not just technical knowledge. It is not acceptable for the “licensor” to change the shape of the trademark without being obligated to allow the licensee to use this new mark.

The obligations of the parties are related to the exchange of improvements throughout the validity period of the contract, from the moment of its signing until its expiry. Understanding emotional and cognitive processes can help researcher to better understand peoples’ behavior, decision-making, the obligations of the parties (see Alsharif et al., 2021a; 2021b; 2021c; 2021e; 2021f).

With regard to the licensee, the most valid opinion is that any development carried out by the licensee that contributes to the process of modernizing the franchise and its success is subject to two rules: the first when the issue is regulated in the contract, then it is subject to the terms of the contract. If it is not regulated in the contract, the researcher adopts the perspective that there has to be a payment in return of the exchange of improvements (Al-Mulhim, 1996, p. 264).

Discussion and Conclusion

The study concludes that the franchise contract is one of the newly developed contracts that has been widely used in many countries of the world, and that the conclusion of the franchise contract imposes a set of obligations on its parties. The study also concludes that there is a set of obligations on the franchise owner, and other obligations on licensee, in addition to a third set of mutual obligations that falls on the two parties.

The study also concludes that one of the obligations on the franchise owner under the contract is to inform the licensee of the subject matter of franchise before contracting, and he is also responsible for providing technical assistance, and his obligation to provide warranty, whether non-exposure and merit warranties, in addition to the warranty against hidden defects. The study concludes that there are obligations on licensee presented in maintaining confidentiality and paying in return, whether financial or in kind.

The study also concludes that the exchange of improvements is an obligation on the licensor, and if the licensee makes a development in the system that shall be transferred by the contract, he is obliged to transfer it according to the contract. If the contract does not include this obligation to transfer, the franchisor shall pay for that improvement. The researcher reaches a set of recommendations as follows:

- i. The parties of the franchise shall clarify the nature and conditions of the franchise system under the contract, so that later problems can be avoided during the implementation stages.
- ii. The competent authorities in the countries shall set up a special system to identify the obligations resulting from the franchise contracts to ensure the seriousness of its parties when setting the conditions included in these contracts in order to avoid deception and fraud.
- iii. The researcher recommends holding conferences and training courses that encourage citizens and businesspersons to enter into this kind of contracts, which in turn will be reflected positively on the country's economy.

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