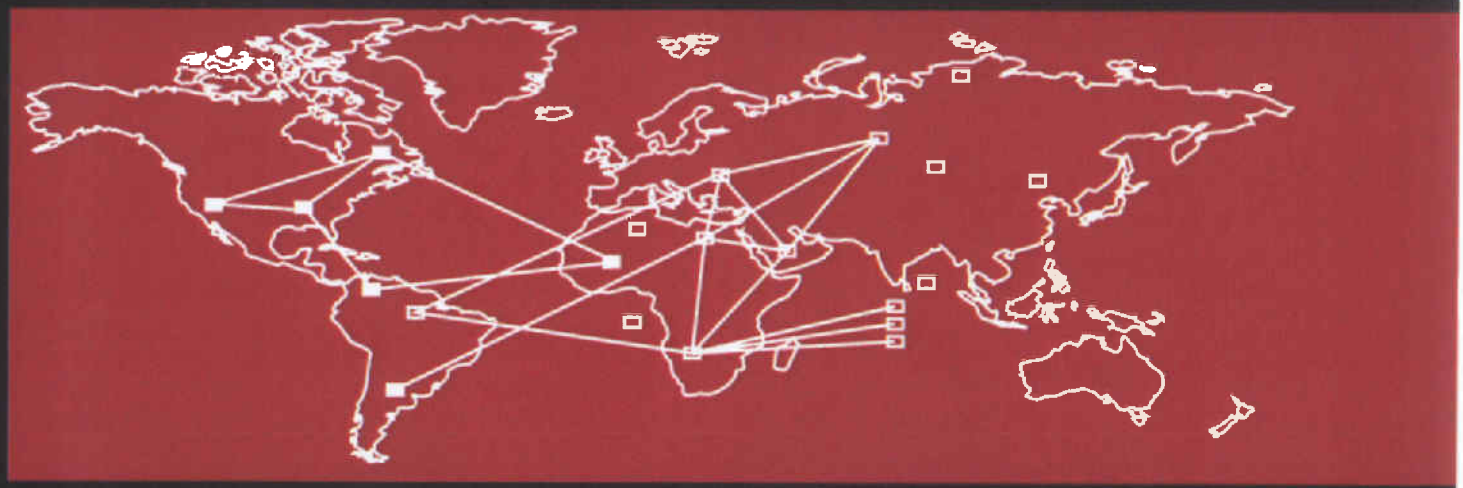
CLAERHOUT PUBLISHING

Volume 8 2010 Issue 1



INTERNATIONAL JOURNAL OF FRANCHISING LAW

Edited by Martin Mendelsohn

AUSTRIA – RECENT DECISIONS OF THE SUPREME COURT RELATED TO DISTRIBUTION RELATIONSHIPS

By Dr. Benedikt Spiegelfeld, *Partner and* **Mag. Mark Krenn,** *Senior Attorney, CHSH Cerha Hempel Spiegelfeld Hlawati, Vienna*

The Austrian Supreme Court has clarified the boundaries between employment relationships and independent contractor relationships such as commercial agency and franchising agreements, an important distinction when an agency or franchising agreement is terminated. The Austrian courts do however consider employment related case law in respect of premature termination of such agreements, including cases involving contributory negligence by the franchisee

A tightly organised franchise system does not cause a franchisee to be considered as an employee

The Austrian Supreme Court (9ObA54/07t, 09.07.2008) held that franchise systems are typically tightly organised and that such a tight organisation on its own is no reason to consider a franchisee an employee of the franchisor and therefore benefiting from employment laws.

A commercial agent independently operated a retail store in a shopping mall based on a commercial agency agreement (the "agreement"). The agreement imposed several obligations and restrictions, which usually are contained in franchise agreements, e.g. to keep the shop open during specified hours, only sell and market goods of the principal, maintain furniture, fixtures and equipment of the store, grant access to representatives of the principal, and so on. The commercial agent was free to employ personnel to fulfil his duties under the agreement. After termination of the agreement, the commercial agent claimed that – due to the restrictions and obligations imposed – he should be considered an employee and hence sued the principal for supplementary grants, severance payment, overtime salary and holiday compensation, as well as the difference between the commissions received and the salary he would have received as an employee.

While the court of first instance (Labour and Social Court) decided in favour of the plaintiff – as this type of court usually does in cases where an employee acts as the plaintiff – the Court of Appeals as well as the Austrian Supreme Court wholly rejected the claim.

The Austrian Supreme Court, supporting the decision of the Court of Appeals, stated that the agreement contained elements of a franchise system and that franchise systems are usually tightly organized but that such circumstances themselves do not lead to the qualification of a commercial agent

"... similarities of the position of an agent/franchisee and an employee in terms of an assumed economical inferiority in relation to their principal/franchisor or employer ..."

as an employee. The Austrian Supreme Court held (confirming previous case law) that in particular:

(i) the independence of personal instructions; and

(ii) the lack of duty to personally perform work in the retail store under the Agreement

draws the line between an employee relationship and an independent contractor relationship.

Needless to say, this decision is of vital importance for all freelance driven distribution relationships – including franchising – and confirms industry practice. As regards the criterion "*independence of personal instructions*" it is worth mentioning that a principal, franchisor, and so on, may of course "instruct" his subordinated contractor to fulfil his contractual obligations based on the underlying agreement. He should avoid personally instructing the contractor on how to fulfil the respective obligations in detail, *e.g.* when to go on holidays, which cleaning company to use, which accountant to use, etc.

Franchisee's contributory negligence in case of unjustified termination of his contract by the franchisor

The Austrian Supreme Court (8ObA61/08s, 23.02.2009) held that premature termination provisions of the Commercial Agent Act are to be interpreted in the light of employment case law also with respect to contributory negligence.

Due to the similarities of the position of an agent/franchisee and an employee in terms of an assumed economical inferiority in relation to their principal/franchisor or employer, Austrian courts usually fall back on employment case law in commercial agency/franchising matters in terms of reasons for and the procedure related to the premature termination of a commercial agency or franchising agreement.

It is not surprising therefore that the Austrian Supreme Court in a recent decision followed this principle in relation to claims arising out of the premature termination of a franchising agreement, including contributory negligence of a franchisee as cause for the termination by franchisor. This practice is supported by the relevant sections of the Employment Act (sec. 32) and the Commercial Agent Act (sec. 23 para 2) (applied by analogy to franchising relationships), which more or less are identical.

Nevertheless, it is worth taking a closer look at the respective sections. The respective sections state that in case of a (i) justified or (ii) unjustified premature termination of the agreement, which was *mutually caused* by both parties, the amount of compensation arising out of such a premature termination may be assessed by the court in its sole discretion.

The bottom line is that the cause asserted for the premature termination (whether justified or not) may not correspond to the cause for giving notice of the termination (effectively terminating the agreement):

In its decision 8ObA61/08s the Austrian Supreme Court had to assess the following case: a franchisee had been operating a gasoline station (including a retail shop) based on several related agreements (lease, commercial agency and franchise agreement) for 17 years for its principal until all agreements were terminated for cause by the franchisor. During the last contract year, the franchisor complained several times about infringements of the agreements, which were in most cases remedied by the franchisee. The final review of the premises by the principal revealed that all but one infringement were remedied – the best-before-date of four packs of camembert cheese had just expired the day before and the franchisor as a consequence terminated the agreements with immediate effect. Subsequently, the

franchisee claimed that this termination was unjustified due to the marginal nature of the infringement and claimed damages as well as compensation payment in accordance with the Commercial Agent Act. Before the court the defendant claimed that the termination was justified and *in eventu* (in case the court would hold the termination unjustified) claimed contributory negligence attributable to the franchisee due to his infringement of the agreements which gave rise to the premature termination, in order to reduce the franchisee's claim for damages and compensation payments.

Firstly, the Austrian Supreme Court held that even where the principal has complained of infringements of the agreements on several occasions, the specific infringement triggering the premature termination has to be sufficient important to meet the requirement of a justified termination. The court rejected the argument that the expiry of the best-before-date of four packs of camembert cheese constituted an infringement that would justify a premature termination even in the light of previous infringements of the same nature identified by the franchisor.

Furthermore, the Court rejected the defendant's *in eventu* claim that the franchisee's infringement of the agreements, which had been held not to justify premature termination, had induced the franchisor to give notice of termination. The Court considered it would not be legitimate to assert a premature termination, which is unjustified, while at the same time arguing that such unjustified cause reduces the other party's claim for damages and compensation resulting out of the unjustified termination.

Benedikt Spiegelfeld and Mark Krenn

Benedikt Spiegelfeld is Senior Partner and Head of Department Corporate & Commercial at the Austrian law firm Cerha Hempel Spiegelfeld Hlawati. He practises in the areas of mergers & acquisitions, corporate, franchising and distribution law, and arbitration.

Mark Krenn is a senior attorney at the Austrian law firm Cerha Hempel Spiegelfeld Hlawati, specialising in corporate, mergers & acquisitions and distribution law.