OPINION OF MR ADVOCATE GENERAL VERLOREN VAN THEMAAT
delivered on 19 June 1985 *

Mr President,
Members of the Court,

1. Introduction

1.1. *The questions referred by the Bundesgerichtshof*

In a dispute with its French franchisor over the payment of arrears of royalties, a German franchisee successfully pleaded in the appeal court that the franchise agreement in question was void under EEC competition law. According to the appeal court Article 85 of the EEC Treaty prohibits franchise agreements of the kind at issue in the proceedings, inasmuch as they contain restrictions of competition which are not exempted, under Article 85 (3) of the EEC Treaty and Regulation No 67/67/EEC of 22 March 1967 (Official Journal, English Special Edition 1967, p. 10), from the prohibition laid down in Article 85 (1) of the Treaty.

The plaintiff in the main proceedings appealed against that judgment to the Bundesgerichtshof. The Bundesgerichtshof considered that the judgment of the appeal court raised questions of Community law, and therefore, by an order of 15 May 1984, referred a number of questions to the Court of Justice.

According to writers on the subject, distribution systems involving franchise agreements did not gain currency in the Member States until the early 1970s. Systems of that kind developed very quickly, however, and now constitute a significant proportion of distribution systems. Even if, in answering the questions referred, the Court restricts itself to franchise agreements having the characteristics of the agreements at issue, its answers will therefore have repercussions for the validity of tens of thousands of contracts. Furthermore, the importance of the Court's answers to the questions referred is reinforced by the fact that according to the written and oral observations which it presented in these proceedings the Commission has not yet adopted a clear policy in the matter.

The questions referred by the Bundesgerichtshof are as follows:

(1) Is Article 85 (1) of the EEC Treaty applicable to franchise agreements such as the contracts between the parties, which have as their object the establishment of a special distribution system whereby the franchisor provides to the franchisee, in addition to goods, certain trade names, trade marks, merchandising material and services?

(2) If the first question is answered in the affirmative: Is Commission Regulation No 67/67/EEC of 22 March 1967 on the application of Article 85 (3) of the Treaty to certain categories of exclusive dealing agreements (block exemption) applicable to such contracts?

* Translated from the Dutch.

(3) If the second question is answered in the affirmative:

(a) Is Regulation No 67/67 still applicable if several undertakings which, though legally independent, are bound together by commercial ties and form a single economic entity for the purposes of the contract participate on one side of the agreement?

(b) Does Regulation No 67/67, and in particular Article 2 (2) (c) thereof, apply to an obligation on the part of the franchisee to advertise solely with the prior agreement of the franchisor and in a manner that is in keeping with the latter's advertising, using the publicity material supplied by him, and in general to use the same business methods? Is it relevant in this connection that the franchisor's publicity material contains price recommendations which are not binding?

(c) Does Regulation No 67/67, and in particular Articles 1 (1) (b), 2 (1) (a) and 2 (2) (b) thereof, apply to an obligation on the part of the franchisee to confine the sale of the contract goods exclusively or at least for the most part to particular business premises specially adapted for the purpose?

(d) Does Regulation No 67/67, and in particular Article 1 (1) (b) thereof, apply to an obligation on the part of the franchisee — who is bound to purchase most of his supplies from the franchisor — to make the rest of his purchases of goods covered by the contract solely from suppliers approved by the franchisor?

(e) Does Regulation No 67/67 sanction an obligation on the franchisor to give the franchisee commercial, advertising and professional support?

1.2. *The main provisions of the contracts entered into by the franchisee concerned*

As appears from the three contracts between the parties in the main proceedings, which were submitted to the Court at its request after the hearing, the franchisor binds itself:

(i) Not to grant to any third party the right to use the trade-mark 'Pronuptia de Paris' in the contract territory concerned (Hamburg, Oldenburg and Hanover respectively) (Article 1 (1));

(ii) Not to open any other Pronuptia shops in the contract territory (Article 1 (2));

(iii) Not to provide goods or services to third parties in the contract territory (Article 1 (2));

(iv) To provide commercial assistance to the defendant in advertising, in establishing and stocking her shop, in training staff and with regard to sales techniques, fashions and products, purchasing and marketing and, very generally, to help the defendant to increase her turnover and profits (Article 3 (1)).

The franchisee (who according to Article 3 (5) remains the sole proprietor of her business, bears the risks of the business herself and her sole enjoyment of the profits) is obliged *inter alia*:

To sell the products covered by the agreement, using the trade name and trademark Pronuptia de Paris, only in the shop

referred to in Article 1, which must be equipped mainly for the sale of bridal fashions, in accordance with the brand image of Pronuptia de Paris (Articles 3 (3) and 4 (1));

To purchase from the franchisor 80% of wedding dresses and accessories, together with a proportion of cocktail and evening dress to be set by the defendant (Article 3 (6));

To purchase the remaining wedding dresses and accessories and cocktail and evening dress exclusively from suppliers approved by the franchisor (Article 3 (6));

To pay to the franchisor a royalty of 10% on all sales (including sales of articles not supplied by Pronuptia) during the validity of the contract (Article 5 (1));

To refrain, during the period of validity of the contract and for one year after its termination, from competing in any way with a Pronuptia shop and in particular from engaging in the specialized sale of wedding dresses and accessories in the Federal Republic of Germany, in West Berlin or in an area where Pronuptia is already represented (Articles 6 (6) and 9);

To make the sale of the goods covered by the contract her main objective (Article 6 (6));

To carry on business in a specified location and to equip the premises primarily for the sale of bridal wear, in accordance with the image of Pronuptia de Paris and following its instructions (Articles 1 (3), 3 (3) and 4 (1));

To carry on business, and in particular to sell products covered by the contract, under the trade-mark and trade name Pronuptia de Paris, only in those premises (Articles 3 (3) and 4 (1));

To use the trade-mark Pronuptia de Paris in her advertising only with the prior approval of the franchisor; to harmonize her advertising with that of Pronuptia, using the advertising material made available by Pronuptia with the recommended prices included therein (Articles 1 (1) and 6 (1));

To advertise, to distribute advertising material to the best of her abilities and in general to apply the business methods of the franchisor (Article 6 (5));

Strictly to respect all industrial and commercial property rights of Pronuptia and to inform Pronuptia immediately of any infringements of those rights by third parties of which she might become aware (Article 14).

Pursuant to Article 6 (1), Pronuptia is to recommend to the franchisee appropriate standard prices; both parties are to regard these standard prices as guidelines for retail sale (without prejudice to the franchisee's liberty to set prices herself).

1.3. *Plan of discussion*

As I have already pointed out, the answer to be given by the Court to the questions referred may have repercussions on the validity of other franchise agreements, and on the approach to be adopted by the Commission in this field. In the second part of this opinion I shall therefore make a number of general remarks regarding this system of distribution, which is relatively new to the Community. In particular, I shall examine to what extent a sufficient degree of certainty with regard to the content and legal nature of franchise agreements for the sale of products already exists in legislation,

judicial decisions and academic literature, and especially within the trade organizations concerned, so as to enable the Court to deliver a more general ruling. I do not think that the wording of the questions referred by the Bundesgerichtshof prevents that. It precludes the Court only from ruling with regard to franchise agreements which have been current in the Community for a longer period (for example, in the hotel, café and restaurant sector) in relation to the provision of services or to manufacturing.

In the third part of my opinion I shall investigate the similarities and differences between franchise agreements, in particular franchise agreements such as that now at issue, and other distribution systems already current in Community legal practice, especially those which have been discussed in judgments of the Court, such as agency agreements, exclusive distribution or purchasing contracts, selective distribution systems, brewery contracts, and licensing agreements. I shall also discuss what conclusions may be drawn in this case from previous decisions of the Court.

In the fourth part of my opinion I shall state how, in my view, the questions referred in this case should be answered.

2. General remarks regarding franchise agreements for the distribution of products

2.1. *The development of the franchise system as a new distribution system*

It appears from the already quite extensive literature on the subject, that the franchise system, based on earlier American experience, was introduced into the EEC in the early 1970s. Its subsequent development has however been rapid. In 1969 there were only a few franchise systems in the distribution sector in the Federal Republic of Germay. By 1978 the total number of franchise systems (including arrangements for the provision of services) had risen to 85 (with 11 000 franchisees); in May 1982 there were 200 such systems, with 120 000 franchisees and a total turnover of DM 100 thousand million, of which DM 65 to 75 thousand million was in the retail sector. In France (where franchising also began to develop in the early 1970s) there were more than 300 franchise systems in 1981 and 500 in 1985 (with 25 000 participating shops and 8% of total retail sales). In the Netherlands there were 280 franchise systems in 1983. Similar development took place after 1970 in other Member States.

2.2. *Legal characteristics of the franchise system according to academic opinion*

It appears from the literature, and was confirmed by the Commission at the hearing, that none of the Member States has specific legislative provisions regarding franchise agreements. Furthermore, no precise definition of franchise agreements in general, or of franchise agreements for the distribution of products in particular, can be drawn from the case-law that exists or from the relevant academic writing. The main elements of franchise systems for the distribution of products in all the Member States examined seem however to be the following: (1) although they remain independent and bear their own risks, franchisees are integrated to a considerable extent in the franchisor's distribution network; (2) marketing strategy is based on a chain effect, brought about by the use, in return for payment, of a common business name, trade-mark, sign or symbol, and —

in many cases — uniform arrangement of shop premises; (3) exclusive rights are granted to the franchisee within a defined area and for defined products, and exclusive rights that vary in scope are granted to the franchisor with regard to the supply or selection of the products to be sold by the franchisee. The writers on the subject also seem to be agreed that the term 'franchise agreement', as it is used in Europe, must be understood in a much more restricted sense than the original American term, which applied to many more distribution systems. As will appear from my remarks below, however, recent American literature also uses the term in a more restricted sense.

On the basis of a comparative legal study Mr E. M. Kneppers-Heynert, in a recent article in the *Bijblad Industriële Eigendom* (1984, No 10, p. 251), arrived at the following general description, which seems to me to be reasonably representative:

'Franchising is a contractually governed form of commercial cooperation between independent undertakings, whereby one party, the franchisor, gives one or more other parties, the franchisees, the right to use his trade name or mark and other distinguishing features, in the sale of products or of services. The sale takes place on the basis of an exclusive marketing concept (system or formula) developed by the franchisor; in return, the franchisor receives royalties. The use of those rights by the franchisee is supervised by the franchisor in order to ensure uniform presentation to the public and uniform quality of the goods or services.'

The 'European Code of Ethics for Franchising', drawn up by the European Franchising Federation and the eight national associations of which it is composed (six of them from EEC Member States), was submitted to the Court at the hearing. It refers *inter alia* to the following six characteristics of a franchise agreement: [1]

(1) 'Ownership [by the franchising firm (the Franchisor)] of a Company Name, a Trade Name, Initials or Symbols (possibly a Trade Mark) of a business or a service, *and* Know-how, which is made available to the franchised firm(s) — the Franchisee(s) . . . [and its] control of a range of Products and/or Services presented in a distinctive and original format, and which must be adopted and used by the franchisee(s), the format being based on a set of specific business techniques which have been previously tested, and which are continually developed and checked as regards their value and efficiency.'

(2) 'Implicit in any Franchising Agreement is that there shall be a payment made in one form or another by the Franchisee to the Franchisor in recognition of the service supplied by the Franchisor in providing his name, format, technology and know-how.'

(3) 'Franchising is therefore something more than a Sales Agreement or a Concession Agreement of a Licence Contract in that both parties accept important obligations to one another, over and above those established in a conventional trading relationship.'

(4) 'The Franchisor will guarantee the validity of its rights over the brand, sign, initials, slogan, etc. and will grant the franchised firms unimpaired

1 — *Translator's note:* What follows is taken from the published English version.

enjoyment of any of these which it makes available to them.'

(5) 'The Franchisor will select and accept only those franchise candidates who possess the qualifications required by the franchise. All discrimination on the grounds of politics, race, language, religion or sex, will be excluded from the qualifications.'

(6) 'The Franchise Contract will specify in particular the points set out below, it being understood that the provisions adopted will be consistent with national or community law:

The method and conditions of payment of fees and royalties.

The duration of the Contract and the basis for renewal; the time and duration of notice.

The rights of the Franchisor prior to assignment by the Franchisee.

The definition of "open territorial rights" granted to the Franchisee, including options (if granted) on adjoining territories.

Basis for distribution of the assets affected by the Contract, if the Contract is terminated.

Distribution arrangements relative to supply of goods, including responsibility for transport and transport charges.

Terms of payment.

Services provided by the Franchisor: Marketing assistance, Promotion, Advertising: Technology & Know-how: Managerial Administrative & Business Advice: Financial & Taxation Advice: Conditions under which these services to be provided and relevant charges: Training.

Obligations of the Franchisee: To provide Accounts & Operating Data: To receive Training and to accept Inspection Procedures.'

With regard to training and assistance the Code of Ethics also contains a large number of specific guidelines, of which only the following seem relevant to the assessment of franchise agreements of the kind referred to in the Code of Ethics in the light of Article 85 of the EEC Treaty:

'The Franchisor will assist the Franchisee by providing guidance as to the operating costs and margins that he should be achieving at any given time in his business.

...

Any non-concurrence [sic] clause applicable after breach or termination of the contract, must be precisely stated and defined in the contract as regards its duration and territorial extent.'

2.3. *Case-law*

Only in France have the definitions formulated by the trade organizations been more or less adopted by the courts: see Tribunal de grande instance de Bressuire, 19 June 1973 (*SVPNAS* v *Billy*); Tribunal correctionnel de Paris, 4 March 1974 (*Maje Distribution*); Cour d'appel de Paris (Fifth Chamber), 28 April 1978 (*Morvan* v *Intercontinents*); Cour d'appel de Paris, 10 May 1978 (*Télefleurs* v *Interflora*, Cahiers de droit de l'enterprise No 6-78); Cour d'appel de Douai, 22 April 1982 (Gazette du Palais

1982, Doctrine, p. 565); Cour d'appel de Colmar (First Civil Chamber), 9 June 1982 (*Felicitas* v *Georges* Dalloz 1982, ECR at p. 553). In those judgments it is striking that exclusive rights are not always regarded as essential (Cour d'appel de Colmar and Cour d'appel de Douai), but permission to use a trade name, signs and symbols and the application of uniform sales methods are so considered. In the absence of legislative definitions, moreover, franchise agreements are assessed exclusively on the basis of the provisions of the agreement at issue.

Within the Community it is only in the judgment of the Bundesgerichtshof of 23 March 1982 (*Meierei-Zentrale* Wirtschaft und Wettbewerb 1982, p. 781) that I have been able to find a judicial ruling on the competition law aspects of franchise agreements. In that judgment the prohibition of resale price maintenance laid down in Article 15 of the *Gesetz gegen Wettbewerbsbeschränkungen* [German Law on restrictive trade practices] was considered applicable to a franchise agreement in which resale prices were fixed. In its 1981 report 'Full-line Forcing and Tie-In-Sales', however, the British Monopolies and Mergers Commission did take the view that exclusive supply obligations could in certain circumstances be significant from the point of view of competition law.

As I have already pointed out, in the United States the term franchise agreement was initially used in a very wide sense. According to the more recent restricted use of the term (which served as a model for the European development) a franchise is defined as a licence from the owner of a trade-mark or trade name permitting another to sell a product or service under that mark or name (Black's Law Dictionary, 5th Edition, 1979; von Kalinowski, Antitrust Laws and Trade Regulation, Vol. 2, paragraph 6H.01/1981 supplement).

In the United States, as in the United Kingdom, exclusive purchase obligations contained in franchise agreements are not automatically regarded as 'tying arrangements' prohibited by competition law. In appropriate market conditions they may however fall under that prohibition. Since the 1977 *Sylvania* judgment the 'rule of reason' has been applied to vertical territorial restriction clauses in order to ascertain whether there is restriction of competition (in particular horizontal restriction). Contract provisions regarding resale prices are regarded as prohibited *per se* where it appears that the franchisor, not content with mere price recommendations, is attempting one way or another to force the franchisee to apply his suggestions or recommendations. In the *Sylvania* judgment the 'rule of reason' was applied to territorial restrictions, in particular restrictions on premises, such as those at issue in the Pronuptia case, notwithstanding the resulting restrictions on competition between retailers of Sylvania products. Despite the concomitant restrictions on 'intra-brand' competition, vertical restrictions on competition such as those at issue in the Sylvania case were regarded as beneficial for 'inter-brand' competition. Only in certain cases and on the basis of their actual economic consequences may such vertical restrictions of competition be held to be caught by the *per se* prohibition contained in American anti-trust legislation. Having regard to the later American legal practice the decisive question seems to be whether or not there is effective competition with other products on the relevant market. In speaking of the American practice I should point out that in the United States the problem peculiar to the EEC of separate

national markets with prices which are often widely divergent does not exist. A single internal market was achieved long ago in the United States, so that the problem of obstacles to parallel imports does not arise.

2.4. *Conclusions*

On the basis of academic opinion and case-law in the Community, on the basis of the views of the European Franchising Federation and on the basis of the most recent American definitions of franchise agreements of the type at issue, I think that the significant distinguishing features of a franchise agreement for the sale of products are the independence of the undertakings involved, the existence of a licence for the use of a company name, trade name, emblem or other symbols, and for know-how in a broad sense, together with a uniform manner of presentation, the usual consideration being the payment of a royalty by the franchisee for the licences granted. In the American case-law it seems that the market position of the undertakings concerned and the distinction between the vertical relationship between franchisor and franchisee and the horizontal relationship between each of the franchisees and their competitors are of particular importance in assessing such agreements from the point of view of competition law. Except in extra-ordinary market conditions, it seems that inter-brand competition is considered more important for the maintenance of effective competition than intra-brand competition. In the United States the imposition of fixed prices by franchisors seems to be regarded as automatically contrary to the prohibition of price agreements, just as it is in the Federal Republic of Germany. For the rest, the judicial practice in the United States and in three of the large Member States of the EEC seems to be to judge each agreement on its own merits, taking into account its specific provisions and, in so far as competition aspects are to be dealt with, the specific circumstances of the relevant market. The last-mentioned factor is particularly relevant with regard to the various exclusivity clauses to be found in franchise agreements.

3. Similarities and differences between franchise agreements and other distribution systems considered in previous judgments of the Court

3.1. *Exclusive agents*

Since in the literature and the case-law on franchise agreements the fact that the franchisee is an independent undertaking or that he deals in his own name and at his own risk is considered to be an essential characteristic of such agreements, I think, contrary to Pronuptia's contention, that comparison of this new type of agreement with agency agreements as referred to in the Commission communication of 24 December 1962 (Journal Officiel 2921/62) is not relevant to the questions referred by the Bundesgerichtshof. As appears from Article 3 (5) of the agreements at issue, they do not differ in that respect from the general picture.

3.2. *Exclusive distribution agreements*

The contracts in question are similar in more respects to exclusive distribution agreements. In particular the franchisee's exclusive purchase rights laid down in Article 1 (1) and (2), and the franchisor's (restricted) exclusive supply rights laid down in Article 3 (6) are clearly similar, at first sight, to the characteristics which determine the applicability of Regulation No

67/67/EEC of 22 March 1967 on the application of Article 85 (3) of the Treaty to certain categories of exclusive dealing agreements. It is not surprising, therefore, that in this case the national court raised separate questions on the issue of the applicability of that regulation.

With regard to the first question referred by the national court, regarding the applicability in principle of Article 85 to franchise agreements, I think a particularly relevant analogy may be made with the Court's statement of the problem in its judgment of 13 July 1966 in Case 32/65 (*Italy* v *Commission* [1966] ECR 389). In particular the third paragraph on page 407 of the Reports may, subject to the differences which I shall discuss later between franchise agreements and 'classical' exclusive distribution agreements, be applied by analogy in answering the first question put by the national court.

In that paragraph it is stated:

'It is not possible either to argue that Article 85 can never apply to an exclusive dealing agreement on the ground that the grantor and the grantee thereof do not compete with each other. For the competition mentioned in Article 85 (1) means not only any possible competition between the parties to the agreement, but also any possible competition between one of them and third parties. This must all the more be the case since the parties to such an agreement could attempt, by preventing or limiting the competition of third parties in the product, to set up or preserve to their gain an unjustified advantage detrimental to the consumer or the user, contrary to the general objectives of Article 85. Therefore even if it does not involve an abuse of a dominant position, an agreement between businesses operating at different levels may affect trade between Member States and at the same time have as its object or effect the prevention, restriction or distortion of competition and thus fall under the prohibition in Article 85 (1). Thus each of Articles 85 and 86 has its own objective and so soon as the particular features of either of them are present they apply indifferently to various types of agreements.'

In the following paragraph the Court refuses to compare exclusive distribution systems with agency agreements and other forms of integration in which a single undertaking incorporates its distribution network into its own organization (and there is thus no question of agreements between several independent undertakings).

I think the particular importance of the passage quoted lies in the fact that it seems valid *mutatis mutandis* for all bilateral vertical agreements. Furthermore, like the American case-law, it appears to treat possible restrictions on horizontal competition as decisive for the application of Article 85 (1), rather than the mutual restrictions on their commercial freedom agreed to by the parties to a vertical relationship.

That conclusion is not affected by the Court's statement in the *Grundig-Consten* judgment (Joined Cases 56 and 58/64 *Consten and Grundig* v *Commission* [1966] ECR 299, at p. 342) (with regard to the argument that the agreement in question

had increased competition between similar products of different brands) that 'although competition between producers is generally more noticeable than that between distributors of products of the same make, it does not thereby follow that an agreement tending to restrict the latter kind of competition should escape the prohibition of Article 85 (1) merely because it might increase the former'. The Court went on to state that 'for the purpose of applying Article 85 (1), there is no need to take account of the concrete effects of an agreement once it appears that it has as its object the prevention, restriction or distortion of competition'.

Closer examination of the *Grundig-Consten* judgment as a whole shows, I think, that there too the Court was particularly concerned with restrictions of competition between the exclusive distributor and third parties (in that case, parallel importers of products of the same brand), that is, intentional restrictions on horizontal competition. In that respect I refer in particular to the Court's remarks at the bottom of page 342 and the top of page 343 of the Reports. Greater importance is however ascribed also to horizontal 'intra-brand competition', especially where national markets are protected against parallel imports, than is the case in recent American judgments.

The necessary details were set out by the Court in a preliminary ruling of 30 June 1966 in Case 56/65 (*Société Technique Minière* v *Maschinenbau Ulm* [1966] ECR 235) where it held (p. 250) that 'in order to decide whether an agreement containing a clause "granting an exclusive right of sale" is to be considered as prohibited by reason of its object or of its effect, it is appropriate to take into account in particular the nature and quantity, limited or otherwise, of the products covered by the agreement, the position and importance of the grantor and the concessionnaire on the market for the products concerned, the isolated nature of the disputed agreement or, alternatively, its position in a series of agreements, the severity of the clauses intended to protect the exclusive dealership or, alternatively, the opportunities allowed for other commercial competitors in the same products by way of parallel re-exportation and importation'.

3.3. *Brewery contracts*

The exclusive distribution agreements which the Court has been called upon to consider mainly concerned exclusive importers, and according to statements made by the Commission at the hearing that was also generally true of exclusive distribution agreements notified to it. In particular they did not directly concern large numbers of retailers, as is the case here. In that respect the Court's judgments regarding brewery contracts may however be relevant. Building on a passage from the *Maschinenbau Ulm* judgment cited above, in the first *Haecht* judgment (Case 23/67 [1967] ECR 407, at p. 415) the Court held with regard to brewery contracts of the kind in question (involving the obligation to purchase from one brewery only) that:

'... in order to examine whether it is caught by Article 85 (1) an agreement cannot be examined in isolation from the ... context, that is, from the factual or legal circumstances causing it to prevent, restrict or

distort competition. The existence of similar contracts may be taken into consideration for this objective to the extent to which the general body of contracts of this type is capable of restricting the freedom of trade.'

If that paragraph, together with the paragraph which follows it, is applied by analogy to franchise agreements, I think it can be inferred that Article 85 (1) is applicable where a franchisor from one Member State has such a market position in a second Member State that through his subsidiaries, if any, and by means of a number of franchise agreements with independent traders he significantly impedes the access to the market of other producers or wholesalers in that second Member State.

It appears from paragraph 5 of the judgment of the Court in Case 43/69 *(Bilger* v *Jehle* [1970] ECR 127) that in taking into account other comparable contracts not only contracts concluded by a large number of retailers with the same producer (or wholesaler) should be considered but also similar exclusive supply contracts concluded with other producers from the same State. In the case of brewery contracts the combined effects of such contracts between retailers and producers in the same Member State may indeed result in partitioning of the market. As far as I have been able to ascertain the Court has until now only had to deal with brewery contracts between a brewery and its commercial clients in a single Member State. I think, however, that in principle the partitioning of markets (or other forms of restriction on horizontal competition) may come about as a result of the combined effect of franchise agreements for similar products independently of the place where the producer or wholesaler is established.

On the subject of brewery contracts, I think that the judgment of the Court of 1 February 1977 in Case 47/76 (*De Norre* v *Brouwerij Concordia* [1977] ECR 65) is also of some relevance to the second question referred by the Bundesgerichtshof in the present case. In that judgment the Court held that in spite of certain differences, recognized by the Court, between such agreements and traditional exclusive distribution agreements, for which Regulation No 67/67 was originally enacted, the regulation also applies to brewery contracts, that is, 'agreements to which only two undertakings from one Member State only are party, under which one party agrees with the other to purchase only from that other certain goods for resale and which do not display the features set out in Article 3 of Regulation No 67/67 of the Commission . . . if, failing exemption, they would fall under the prohibition contained in Article 85 (1) of the EEC Treaty'. That ruling was based in particular on a finding that 'agreements such as that in question fulfil the conditions laid down in Article 1 (1) (b) of Regulation No 67/67', as appears from paragraph 13, and on the previous judgment in the *Roubaix-Wattrelos* case (Case 63/75 [1976] ECR 111), as appears from paragraphs 16 to 33.

Again with reference to that judgment, I think that in deciding whether or not it is possible to apply it by analogy in the present case the fact that the judgment is restricted to agreements to which only two undertakings from the same Member State are party is not of vital significance. There is

nothing in the judgment to indicate that the Court would not have considered Regulation No 67/67 to be applicable to a brewery contract between a retailer in one Member State and a brewery in another Member State.

However, the judgment naturally leaves entirely open the question whether other characteristics of franchise agreements of the kind at issue in these proceedings do indeed militate against the applicability of Regulation No 67/67. As I shall argue in more detail in the following part of my opinion, I think that is indeed the case.

3.4. *Selective distribution systems*

In these proceedings Pronuptia has also relied on the judgment of the Court in Case 26/76 (*Metro* v *Commission* [1977] ECR 1875). In paragraph 20 of that judgment the Court held that:

'In the sector covering the production of high quality and technically advanced consumer durables, where a relatively small number of large- and medium-scale producers offer a varied range of items which, or so consumers may consider, are readily interchangeable, the structure of the market does not preclude the existence of a variety of channels of distribution adapted to the peculiar characteristics of the various producers and to the requirements of the various categories of consumers.

On this view the Commission was justified in recognizing that selective distribution systems constituted, together with others, an aspect of competition which accords with Article 85 (1), provided that resellers are chosen on the basis of objective criteria of a qualitative nature relating to the technical qualifications of the reseller and his staff and the suitability of his trading premises and that such conditions are laid down uniformly for all potential resellers and are not applied in a discriminatory fashion.'

The mere fact that the franchise agreements in question contain not only qualitative but strict quantitative criteria means, in my view, that this last sentence is not applicable by analogy in this case.

The preceding sentence of paragraph 20 is indeed of some indirect relevance to this case, as is the second last sentence of paragraph 21, which reads as follows:

'For specialist wholesalers and retailers the desire to maintain a certain price level, which corresponds to the desire to preserve, in the interests of consumers, the possibility of the continued existence of this channel of distribution in conjunction with new methods of distribution based on a different type of competition policy, forms one of the objectives which may be pursued without necessarily falling under the prohibition contained in Article 85 (1), and, if it does fall thereunder, either wholly or in part, coming within the framework of Article 85 (3).'

The second sentence of paragraph 22 also seems to me to be of some relevance to the present case. It states that:

'the Commission must ensure that this structural rigidity [of prices, referred to in the preceding sentence] is not reinforced, as might happen if there were an increase in the number of selective distribution networks for marketing the same product.'

Finally, paragraph 24 states which provisions were not considered by the Commission to be restrictive of competition.

In its judgment in Case 31/80 (*L'Oréal* v *De Nieuwe AMCK* [1980] ECR 3775) the Court held in paragraph 17 that:

'When admission to a selective distribution network is made subject to conditions which go beyond simple objective selection of a qualitative nature and, in particular, when it is based on quantitative criteria, the distribution system falls in principle within the prohibition in Article 85 (1), provided that, as the Court observed in its judgment of 30 June 1966 (*Société Technique Minière* v *Maschinenbau Ulm GmbH* Case 56/65 [1966] ECR 235), the agreement fulfils certain conditions depending less on its legal nature than on its effects first on "trade between Member States" and secondly on "competition".'

The following two paragraphs define those conditions in further detail (according to paragraph 18, regard must be had in particular to the consequences of the agreement in question for the possibility of parallel imports, while paragraph 19 refers *inter alia* to the paragraphs of the first *Haecht* judgment quoted above). In the *Lancôme* case (Case 99/79 [1980] ECR 2511) the Court had already taken the same position as that expressed in paragraph 17. The paragraphs referred to are also of some relevance to the present case.

With regard to the prohibited nature of a 'premises clause' such as that contained in Article 4 of the agreements at issue, the Commission has also relied on paragraph 51 of the judgment of the Court of 21 February 1984 in Case 86/82 (*Hasselblad* v *Commission* [1984] ECR 883). After confirming that quantitative selection criteria are prohibited, that paragraph states that 'Clause 28 of the dealer agreement allowed the applicant in fact to restrict the freedom of dealers, even authorized dealers, to establish their business in a location in which the applicant considers their presence capable of influencing competition between dealers'. Paragraph 52 goes on to confirm that that clause, among others, is prohibited.

3.5. *Licence agreements*

Since licences also play a key role in franchise agreements, the judgments of the Court in *Nungesser* (Case 258/78 [1982] ECR 2015) and *Coditel II* (Case 262/81 [1982] ECR 3381) are also relevant to this case. In paragraph 58 of the *Nungesser* judgment the Court concluded that 'having regard to the specific nature of the products in question . . . in a case such as the present, the grant of an open exclusive licence, that is to say a licence which does not affect the position of third parties such as parallel importers and licensees for other territories, is not in itself incompatible with Article 85 (1) of the Treaty'. In paragraph 61 of the same judgment the Court pointed out that it had consistently held 'that absolute territorial protection granted to a licensee in order to enable parallel imports to be controlled and prevented results in the artificial maintenance of separate national markets, contrary to the Treaty'. The key importance of that statement is confirmed in paragraph 78.

In the *Coditel II* case the Court held that: 'A contract whereby the owner of the copyright for a film grants an exclusive right

to exhibit that film for a specific period in the territory of a Member State is not, as such, subject to the prohibitions contained in Article 85 of the Treaty. It is, however, where appropriate, for the national court to ascertain whether, in a given case, the manner in which the exclusive right conferred by that contract is exercised is subject to a situation in the economic or legal sphere the object or effect of which is to prevent or restrict the distribution of films or to distort competition on the cinematographic market, regard being had to the specific characteristics of that market.' However, it is stated in paragraph 19 of that judgment, that the exercise of the exclusive right to exhibit a cinematographic film must not give rise *inter alia* to 'the possibility of charging fees which exceed a fair return on investment, or an exclusivity the duration of which is disproportionate . . . '. That paragraph in particular is relevant to the present case, since the basic issue concerns the royalties.

4. Proposed replies to the questions referred

4.1. *General remarks*

All the judgments referred to contain, I think, elements which should be borne in mind in answering the questions referred.

The type of franchise agreement referred to in the questions corresponds, in my view, to the description of franchise agreements contained in the literature and case-law reviewed above, inasmuch as the right to the use of the company name and the mark or sign 'Pronuptia de Paris', the provision of know-how in a broad sense and the obligation to arrange the premises in accordance with the image of the franchisor and according to its instructions are central to those agreements (Articles 1 (3), 3 (1) and (3), 4 (1) and 14). The fundamental importance of those factors is confirmed by the licence royalties agreed upon, in the amount of 10% of the franchisee's total turnover (Article 5 (1)). Under Article 3 (5) of the agreement, however, the franchisee alone bears the risks of his business. From an economic point of view I think it is above all these characteristics which make franchise agreements extraordinarily attractive to franchisors as a new distribution method. To outside observers a shop set up and run in accordance with the contract resembles a subsidiary. Contrary to the case of a subsidiary, however, the franchisor does not have to carry any investment costs. Nor need he conduct any market studies in the place where the shop is to be established, since in the event of inadequate sales (in particular where costs are high and profits low) he bears no risk whatsoever, but is still entitled to the substantial royalty of 10% of total turnover.

It would appear from the rapid development of the new system that it also has advantages for the franchisee; the main advantage is probably the fact that it gives him (usually exclusive) access to products of high quality the market for which is already established. The market for such products may in particular be established where, as in this case and in other franchise systems mentioned by the franchisee, the franchisor already has subsidiaries in other parts of the Member State concerned, and the franchise

system thus constitutes an extension of a system of subsidiaries which has already stood the test of the market.

For consumers, finally, the presence of a franchise system alongside other distribution systems may have some appeal for the same reasons, but also under the same conditions, as those set out in paragraph 20 of the *Metro* judgment with regard to selective distribution systems. In so far as the admission of franchisees to the system is made subject to quantitative restrictions (for example, by accepting only one franchisee in a defined area, as in this case), I consider, on the basis of the *L'Oréal*, *Lancôme* and *Hasselblad* judgments, that Article 85 (1) must be held to be applicable in principle to the agreement in question, if the general conditions developed in the Court's judgments in Cases 32/65, 56 and 68/64, 56/65, 23/67, 43/69, 47/76, 26/76 and 258/78 (cited above) are fulfilled.

I think the following criteria relevant to the assessment of franchise agreements such as those at issue can be drawn from the judgments referred to:

(a) Since the important point for the application of Article 85 (1) is, according to all the judgments referred to, the horizontal effects of vertical agreements (for instance the exclusion of certain competitors, such as parallel importers), it seems to me that the question whether or not a franchise agreement results in a fair division of costs and benefits as between franchisor and franchisee is not in itself relevant to the question whether Article 85 (1) is applicable. The same is true in principle of specific obligations of the franchisee, such as the obligation of specialization (Articles 3 (3), 4 (1) and 6 (6)), the obligation to advertise (Articles 1 (1) and 6 (4) and (5)) and the obligation to set up and run the shop in a particular manner (Articles 3 (3) and 4 (1)). With regard to such vertical obligations I think Article 85 (1) can only apply when it can be shown in a particular case that they cause injury to third parties (competitors, suppliers or purchasers), which will seldom be the case where there are adequate alternative chains of distribution for similar products.

(b) If the main issue is thus the 'horizontal' effects, or more correctly the results of the agreement for third parties, then, according to the judgments of the Court, particular attention must be paid to the questions whether (i) parallel imports remain possible (see for example the *Grundig-Consten*, *Bilger* and *Nungesser* judgments); (ii) whether, having regard to the market position of the suppliers concerned, access to the market for other suppliers or dealers is restricted (see the quotations from Cases 56/65, 23/67, 43/69, 26/76 and 31/80); and (iii) whether the agreement results in price increases (*Metro* and *Coditel II*) or involves price-fixing by means of contractual obligations or concerted practices on the part of the franchisor, its subsidiaries and its various franchisees.

With regard to this last criterion I am of the view, contrary to the American and German case-law referred to, that the Court's judgments regarding resale price maintenance and other forms of price agreement

need only be applied in a case where a party is in a position of economic strength on the local markets concerned, or where price maintenance is also applied by competitors. In the light of paragraphs 21 and 22 of the *Metro* judgment I think, too, that the strong upward influence on prices which will almost certainly be exerted by the royalty provision in the agreement at issue should only be regarded as a ground for applying Article 85 (1) where a franchisor from one Member State plays a role of price leader or otherwise occupies a position of economic strength in a significant number of local markets in a second Member State.

On the basis of those criteria I think it possible to give a sufficiently clear answer to the first question referred by the national court to enable that court to reach a decision on the facts of this case. I think a more concrete answer than that proposed by the Commission is desirable.

Since, for reasons which I shall discuss, I am of the view that Regulation No 67/67/EEC is not applicable to franchise agreements such as those here at issue, Question 3 in the order for reference does not as such require an answer. In its judgment the Court might, however, wish to make it clear that obligations such as those referred to in subparagraphs (b), (d) and (e) of Question 3 cannot, except in unusual circumstances, be regarded as restrictions of competition within the meaning of Article 85 (1).

4.2. *Answer to the first question*

In the light of the criteria which I have deduced from the judgments of the Court and summarized above, I think Articles 1 (1) and (2), 3 (3), 4 (1), 5 (1) and 6 (1) and (6) of the agreements are of particular importance for the answer to the first question. Since, according to the existing literature and case-law, the nature of franchise agreements remains undefined, I would go so far as to suggest that the Court should restrict its answer to the first question asked by the Bundesgerichtshof to franchise agreements with the same content as those concluded between the parties in this case. It would of course be very useful for practitioners if the Court included a summary of those agreements in its judgment.

The answer to the first question could in my view be as follows:

Article 85 (1) of the EEC Treaty is applicable to franchise agreements such as those concluded between the parties in this case in so far as, *inter alia*:

(a) they are concluded between a franchisor from one Member State, or its subsidiary as referred to in Question 3 (a), and one or more franchisees in one or more other Member States;

and

(b) by way of its subsidiaries and franchisees in one or more of those other Member States or in a significant part of their territory the franchisor has a substantial share of the market for the relevant product;

and either

(c) the agreements prevent or restrict, or are intended to prevent or restrict, parallel imports of the products covered by the contract into the contract territory or exports of those products by the franchisee to other Member States;

or

(d) the agreements result — in particular through the establishment of local or regional monopolies for the products covered by the contract, through royalty provisions and contractual provisions or concerted practices with regard to the setting of prices and on account of the absence of effective competition from similar products — in the setting of unreasonably high retail prices, that is to say, prices which could not be charged if effective competition existed, even allowing for the superior quality of the products covered by the contract.

In the wording of this answer I have made it clear that criteria (c) and (d) are to be regarded as alternative criteria. In accordance with the judgments of the Court, criterion (c) places the emphasis on the absolute territorial protection of national markets, which cannot fail to result in significant restriction of horizontal competition unless the market shares involved are negligible. In criterion (d), on the other hand, the accent is placed on the prevention of monopolistic price increases, which as a rule will only be possible where the party concerned has a substantial share of the relevant local or regional markets and where there is no downward influence on prices as a result of other means of distribution for similar products.

4.3. *Answer to the second and third questions*

I agree with the Commission and the French Government that block exemption for franchise agreements is desirable. I consider it particularly desirable having regard to the frequency with which they now occur and their generally beneficial nature; as a rule, it is only in particular market circumstances (in particular, the absence of competing distribution systems) or where they are applied in a particular manner that the intentional or unintentional restriction of competition associated with them may stand in the way of exemption under Article 85 (3) of the EEC Treaty.

As a rule franchise agreements will presumably benefit consumers by improving the distribution of products, since they make possible the rapid penetration of new products or products with particular qualities onto discrete local retail markets. It is the task of the Commission first to acquire the necessary experience by adopting a number of individual decisions in representative cases, and then, in a block-exemption regulation in accordance with the four conditions of Article 85 (3), to lay down the conditions in which the positive effects of franchise agreements can be attributed a greater weight than the

restrictions on competition which may be considered essential to their positive effect.

Like the Commission and the French Government I am also of the view, however, that Regulation No 67/67 cannot be considered applicable to franchise agreements such as those now at issue. For me the following considerations were decisive in arriving at that conclusion:

In the *first* place, it is clear that when Regulation No 67/67 was adopted franchise agreements for the distribution of products within the Community were still extremely rare; during the preparation of the regulation, therefore, no consideration could be given to the specific problems which they raise. The problems to which consideration was given in preparing that regulation, and in regard to which sufficient experience had been gained, as required by the fourth recital in the preamble to Regulation No 19/65/EEC, related in fact only to exclusive importers. Similarly, according to the Commission's answer to a question which I posed at the hearing, during the preparation of the recent block exemptions for exclusive distribution and exclusive purchasing agreements their application to franchise agreements was not advocated by interested parties or by government experts.

Secondly, on the basis of the literature and case-law referred to and the views of the franchising organizations mentioned above, I think that franchise agreements are predominantly characterized by the effort, by means of licences for trade names, trademarks, signs or symbols and know-how in a broad sense and by other provisions, to assimilate the commercial practices of the franchisee as closely as possible to those of the franchisor or its subsidiaries. The franchisee, for his part, is entirely responsible for the risks of his business and must pay a royalty, in this case a substantial one, to the franchisor. Exclusive supply and purchase obligations play only a subordinate role, and from the point of view of competition policy they can only be assessed in the context of the objective pursued, namely the thorough integration of franchisees in the franchisor's network of uniformly managed retail outlets. In Regulation No 67/67, on the other hand, it is licensing agreements which are subordinate in nature.

Thirdly, franchise agreements with the characteristics of those in question also differ substantially from brewery contracts (to which the Court has held Regulation No 67/67 to be applicable) inasmuch as they result in the formation of rigid local or regional monopolies for the products concerned. In that regard I refer in particular to Article 1 of the agreements which were submitted. Furthermore, the difference referred to in the previous paragraph between those agreements and exclusive distribution agreements also exists in relation to brewery contracts.

Fourthly, I think that the application of Regulation No 67/67 is excluded by Article 3 (b) of that regulation. Franchise agreements such as those here at issue give the franchisee absolute territorial protection and make it difficult for dealers to obtain supplies of the products covered by the contract from other dealers within the common market. In addition to Article 1, which I have already mentioned, I refer in that regard to Articles 3 (3) and (6) and 4 (1) of the agreements.

For those four reasons I propose that the Court should answer the second question asked by the national court in the following manner:

Regulation No 67/67/EEC on the application of Article 85 (3) of the Treaty to certain categories of exclusive dealing agreements is not applicable to franchise agreements with a content similar to those concluded between the parties in this case.

It would not then be necessary to reply to the third question referred by the national court. However, the answer which I propose to the first question may, perhaps in combination with remarks which the Court may wish to make in its judgment regarding clauses of the agreement which do not restrict competition, enable the national court to decide which of the provisions of the agreement referred to in the third question must be considered relevant for the application of Article 85 (1).