



LESSONS FOR LICENSORS: KEEP YOUR BRAND FRESH

VANESSA UDY*
ROBIC, LLP
LAWYERS, PATENT AND TRADE-MARK AGENTS

On June 21, 2012, the Superior Court of Quebec rendered a judgment in favour of Dunkin' Donuts franchisees operating in Quebec, ordering their franchisor, Dunkin' Brands Canada Ltd. (formerly Allied Domecq Retailing International (Canada) Ltd. "ADRIC") to pay more than \$16,4 million in damages to the franchisees for its failure to protect and enhance the Dunkin' Donuts brand in Quebec [*Bertico inc. v. Dunkin' Brands Canada Ltd.* [2012] Q.J. No. 4996].

In 1996, the franchisees alerted ADRIC to the gradual crumbling status of the Dunkin' Donuts brand in Quebec and their concerns with respect to Tim Hortons' increasing foothold in the market. Despite the warning, little was done by ADRIC to improve the brand's reputation or to counter Tim Hortons' competition, other than the introduction of a remodel incentive programme in late 2000 designed to render the franchise more attractive to Quebec consumers. Overall, the remodelling plan was a failure. Few franchisees participated, as the program required the franchisees to incur significant expenses in the short term. ADRIC also failed to inject the funds it had promised to improve the brand's reputation on the market.

Between 1998 and 2008, the number of Dunkin' Donuts stores open in the province of Quebec plummeted from 210 to 41. At the time of judgment, that number had further dropped to 13 stores. Similarly, Dunkin' Donuts' market share dwindled from 12.5% in 1995 to 4.6% in 2003. As a result of the dramatic decline in the value of the Dunkin' Donuts brand, the franchisees lost profits and the opportunity to sell their stores at their traditional value.

The main issue debated by the parties to the litigation was whether ADRIC had committed a contractual fault. The Dunkin' Donuts franchise agreements contained a clause pursuant to which ADRIC agreed to take certain measures to protect and enhance the reputation of the brand and the demand for its products.

However, the Court also found that franchise contracts contain an implicit obligation on the part of the franchisors to act in good faith and loyally toward their franchisees. As an extension of this duty, a franchisor has an implicit contractual duty to protect its

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ROBIC, LLP
www.robic.ca
info@robic.com

MONTREAL
1001 Square-Victoria - Bloc E - 8th Floor
Montreal, Quebec, Canada H2Z 2B7
Tel.: +1 514 987-6242 Fax: +1 514 845-7874

QUEBEC
2828 Laurier Boulevard, Tower 1, Suite 925
Quebec, Quebec, Canada G1V 0B9
Tel.: +1 418 653-1888 Fax.: +1 418 653-0006

brand. Failure of a franchisor to do so may result in civil liability toward its franchisees.

Considering ADRIC's delay in responding to the declining reputation of its brand, the failure of the remodelling plan and the failure to contain Dunkin' Donuts' main competitor, the Court found that ADRIC had indeed failed to fulfill both its explicit and implicit obligations under the franchise contracts.

Unfortunately, though the case illustrates a series of facts which, in the aggregate, may be taken to constitute a breach, it does not provide a principled approach to determining whether a breach has occurred. The case also gives few clues as to what positive actions a franchisor can take to ensure it fulfills its obligation to protect the brand. Is a franchisor obliged to take aggressive action to defeat the competition? Or does it only need to take reasonable actions to respond to it? Had ADRIC proposed the remodelling project back in 1995, would it have been found liable? Would ADRIC be in breach of its obligations had it made timely but unsuccessful efforts in good faith to enhance the brand's reputation in Quebec? To what extent might franchisors be held liable for poor decisions or unsuccessful efforts made in good faith order to protect or enhance their brand?

Hopefully, other courts may provide additional answers to these questions in the future.



ROBIC, LLP
www.robic.ca
info@robic.com

MONTREAL
1001 Square-Victoria - Bloc E - 8th Floor
Montreal, Quebec, Canada H2Z 2B7
Tel.: +1 514 987-6242 Fax: +1 514 845-7874

QUEBEC
2828 Laurier Boulevard, Tower 1, Suite 925
Quebec, Quebec, Canada G1V 0B9
Tel.: +1 418 653-1888 Fax.: +1 418 653-0006