



THE DUNKIN' DONUTS CASE: DOUGHNUTS AND COFFEE FOR 11 MILLION \$

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In April 2015, the Court of Appeal of Quebec ordered the Dunkin' Brands Canada Ltd franchisor (Dunkin' Donuts) to pay its franchisees close to 11 million dollars, more than 10 years after the initiation of the proceedings against it [*Dunkin' Brands Canada Ltd. c. Bertico inc.*, 2015 QCCA 624].

In this case, 21 franchisees operating 32 Dunkin' Donuts stores in Quebec sued the franchisor, ADRIC, for failure to fulfill its obligations as a franchisor, between 1995 and 2005, (which were to protect and promote the Dunkin' Donuts network, applying security and cleanliness norms according to the Dunkin' Donuts standards, providing resources to franchisees, etc.), which was outright denied by the franchisor. This decision is a reminder that the franchisor is bound to obligations that go beyond those strictly stipulated by the franchise agreement. This article aims to answer some of the many questions that will inevitably be raised by franchisors following this decision.

Why would a franchisor be bound to additional obligations that are not mentioned in the franchise agreement?

According to the Court of Appeal of Quebec's interpretation, the franchise agreement establishes a cooperative and collaborative relationship between the franchisor and its franchisees that reflects both common and divergent interests over a long period of time. The parties thus have contractual obligations that are implicit, which means that those obligations could be deduced from the agreement and its intention rather than explicitly stipulated in it.

By which implicit obligations could a franchisor be bound?

Providing technical and commercial assistance: Every franchisor has an obligation of good faith towards its franchisees, from which ensues an obligation for the franchisor to support the brand that it represents and to collaborate with its

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franchisees to respond to market conditions. This implies that the franchisor must constantly provide them with technical and commercial assistance, whether it is in the form of training or permanent aid resources.

Ensuring the protection of the network's reputation: The franchisor must ensure that the value and the appealing elements of the network are preserved for its franchisees to benefit from its reputation during the contract. The franchisor has the obligation to protect the network's reputation as a whole so as not to see its value depreciate in the eyes of the public.

Assisting the franchisees in facing competitors: The obligation to protect the franchise network also includes the obligation to take reasonable measures to assist the franchisees in facing the competition and promoting the network's development as a whole. A franchisor must therefore be up to date with its competitors' progress and must be able to address its franchisees' concerns. However, this does not mean that the franchisor must do this alone, as the franchisees also have the obligation to address these changes by participating in the efforts of the franchisor and the network.

Intervening with the franchisees that harm the network: Any right that the franchisor reserves for itself within the franchise agreement is accompanied by an obligation which mirrors that right. When a franchisor reserves a right to oversee its network and to impose certain norms, the franchisor can enforce these norms and standards on the franchisees, but he must also oversee their concrete application. For example, in the Dunkin' Donuts case, the Court of Appeal recognized that the franchisor should act against the franchisees causing it prejudice, especially when they don't respect the quality and cleanliness standards that are imposed within the network.

Concretely, what should a franchisor do to protect its network and assist its franchisees?

For a franchisor to be considered supportive enough of its franchisees and protective of its network, the Court ascertained, with this decision and the preceding *Provigo* case [*Provigo Distribution Inc. v. Supermarché A.R.G. Inc.*, 1997 CanLII 10209] the following actions for the franchisor:

- If they are imposed, the control measures of cleanliness and quality standards must be supervised and enforced;
- Operational and commercial support must be brought to the franchisees;
- The franchisor must avoid repetitive changes in the franchisor's management in order to ensure good business development for the network;
- The franchisor must also avoid hastily withdrawing new products offered to the clients within the network in order to diminish the impact of the product variation on the clientele;

- A drastic change in commercial strategy must be paired with an assistance program for the franchisees;
- In case of financial, commercial or competitive difficulties, the franchisor must act as quickly as possible and organise a re-launch or its failure to act could constitute a fault.
- In case of difficulties caused by market changes, the re-launch plans should be realistic and should offer both short-term and medium to long-term solutions.

If a franchisor breaches any of its obligations, what type of proceedings will it expose itself to?

A franchisee can require that the franchisor comply with the obligations that involves it personally, but also with the obligations concerning the network in general. In other words, if the franchisor does not enforce the norms on franchisee A, the sheer fact of being a member of the network grants franchisee B the right to require that the franchisor take these measures and intervenes. When this lack of compliance causes injury to franchisees, the franchisees can pursue remedies against the franchisor like in the Dunkin' Donuts case. The loss of profits will be evaluated according to a comparable company's return or according to the profits that the franchisees would have made had the franchisor not breached its obligations.

On June 15th 2015, Dunkin' Donuts filed an application for leave to appeal this decision at the Supreme Court of Canada. It appears that the last chapter of this legal saga is not written yet...Franchisors, be warned!



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