

### Franchising Agreements - Standard Form Agreement or Individual Contract?

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#### Background

In many areas of business, contracts are concluded the contents of which are largely preformulated. These standard form agreements are drawn up in advance by one of the contracting parties in order to standardize future agreements with other contracting parties. They contain preformulated terms and conditions which the drafter imposes on the other party upon conclusion of the agreement. Such terms and conditions are imposed unilaterally by the drafter. Generally, standard form agreements are used to avoid negotiating the terms and conditions of each individual agreement. Instead, the contracting party is usually induced to accept the standard form agreement in its entirety.

In franchising, where the franchisor authorizes and obliges its franchisees to establish and operate a business in accordance with standardized terms and principles, the use of standard form agreements is obviously advantageous, and such agreements are therefore regularly used.

#### Legal Implications

On the basis of Swiss court decisions and jurisprudence, various rules and principles have been developed to protect the weaker party to a standard form agreement. These range from the courts' interpretation of unclear contractual provisions to the disadvantage of the drafter, to the invalidity of individual provisions in the standard form agreement. For franchisors, awareness of the following rules is thus especially important:

- The terms and conditions of a standard form agreement are binding only insofar as they have been explicitly or tacitly agreed to by the contracting parties.
- The terms and conditions of a standard form agreement are not binding if:
  - the parties have entered into an individual agreement which deviates from the standard form;

- a party which has agreed overall to the contract did not have an opportunity to review the terms and conditions in a reasonable manner, and to understand them;
  - the terms and conditions include unusual provisions which the other party, while agreeing overall to the contract, did not expect and had no reason to expect (such provisions are not binding);
  - the law or the contracting party requires a particular form (eg, written form or certification) and this is not followed; or
  - the provisions, in a misleading way and to the disadvantage of the contracting party, imply a distribution of rights and obligations that largely runs counter to the nature of a franchising agreement and must therefore be qualified as unfair.
- Terms and conditions of a standard form agreement may subsequently be challenged and are not binding upon the other party if there is an obvious imbalance between consideration and performance, and if the agreement was concluded by exploiting the financial position, inexperience or irresponsibility of the other party. The agreement as a whole may subsequently be challenged and is not binding upon the other party if, at the time the agreement was concluded, one of the parties was in error on a material point of the agreement.
  - In case of doubt, unclear terms and conditions will be interpreted to the disadvantage of the drafter and in favour of the other party.

#### **Criteria for Individual Contract**

In an as-yet unpublished November 2002 decision on a franchise agreement, the Swiss Federal Supreme Court listed several criteria that must be met in order for an agreement to be considered as an individual contract rather than a standard form agreement. In such case the rules applicable to standard form agreements do not apply.

The criteria established by the Federal Supreme Court are as follows:

- If the preformulated text is individually modified, it no longer constitutes preformulated standard business terms and conditions, but is rather an individual agreement.
- An agreement is also not considered a standard form agreement if the text has been drawn up jointly by the two parties.
- The decisive criterion in determining whether an agreement is a standard form agreement is whether the agreement, without negotiation of its content, was retained largely in the version created by the drafter, or whether the drafter negotiated the content with the other party to such extent that the results of the negotiation can be considered an individually negotiated individual contract.

In the case at hand the draft agreement was presented to the franchisee in a meeting and discussed with him. The agreement was not signed until over a month later, after it had been discussed again in another meeting and after the franchisee successfully demanded, in writing, several changes to the draft agreement.

The Federal Supreme Court considered that the various changes to the draft agreement made at the franchisee's request and the adaptation of the agreement to fit the franchisee's circumstances were sufficient to consider the agreement not as a standard form agreement, but rather as an individually negotiated individual contract.

As a result, the court decided, it was to be understood that both contracting parties knew all clauses of the contract and had examined them.

**Comment**

For the franchisor, the rules that protect franchisees when standard form agreements are used carry a risk that where a suit is brought by one or more franchisees, the court may find that:

- the agreement was not concluded in such a way as to be legally binding;
- individual clauses of the agreement are invalid; or
- the agreement is to be interpreted to the disadvantage of the franchisor.

In accordance with the Federal Supreme Court's decision, this latent risk of court intervention in the contractual relationship can be minimized if:

- the potential franchisee is given enough time prior to the conclusion of the agreement to examine the draft agreement and to seek legal advice on the matter;
- the franchisee is given an opportunity to voice questions and request changes to the draft agreement - preferably in written form;
- contractual negotiations are conducted on the requested modifications - preferably, such negotiations should also be documented; and
- the agreement is adapted to the circumstances of the franchisee and - to the extent that this does not impair the uniformity of the system - individual requests for changes are taken into consideration as much as possible.

While these concessions may seem undesirable at first glance, in a potential legal action on the validity and content of the agreement they can be of great advantage to the franchisor.

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