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This article was first published in Getting the Deal Through – Franchise 2009, (published in September 2008 – contributing editor Philip F Zeidman).

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Franchise

in 33 jurisdictions worldwide

Contributing editor: Philip F Zeidman

2009



Published by
GETTING THE DEAL THROUGH
in association with:

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Overview

- 1 What forms of business entities exist that would be relevant to the typical franchisor?

The predominant form of business enterprises are private or public limited liability companies. An international franchisor may also consider opening a branch in Sweden.

- 2 What laws and agencies govern the formation of business entities?

The formation of a limited liability company is governed by the Swedish Companies Act (2005:551). Registration of a limited liability company as well as a branch is made with the Swedish Companies Registration Office (SCRO). The SCRO website contains information in English and is very informative (www.bolagsverket.se).

- 3 Provide an overview of the requirements for forming and maintaining a business entity.

The forming of a limited liability company in Sweden requires that one or more persons or business enterprises draw up a memorandum of association, appoint a board (minimum one person with a deputy board member) and an auditor, adopt articles of association and pay the share capital to a bank. The company must be registered with the SCRO. The SCRO provides forms in English for registration on its website. The minimum share capital for a private limited liability company is 100,000 Swedish krona (approximately €10,400) and the minimum share capital for a public limited liability company is 500,000 Swedish krona (approximately €52,200). A limited liability company must file its annual report and auditor's report for every fiscal year with SCRO.

Forming a branch requires a registration with the SCRO, along with copies of a certificate of registration or similar, of by-laws, copies of the last two annual reports and a certificate that the international company has not been declared bankrupt. The branch also needs to appoint a special person authorised to receive service of process. That person must be a resident of Sweden. If the international company is not from a European Economic Area (EEA) member state, the branch as well as the international company must file its annual report with the SCRO. If from a member state, only the international company must file the annual report.

- 4 What restrictions apply to foreign business entities and foreign investment?

In general, there are few restrictions to foreign business entities wishing to establish or invest in Sweden. A few restrictions that need to be mentioned are that at least one of the founders of a company must be either a resident of the EEA or a legal person founded and with its domicile within this area. Also, at least half of the members of the

board of a limited company must be residents of the EEA. The managing director must be a resident of EEA. The same applies to at least one of the persons with signatory power. If none of the members of the board is resident in Sweden, the company must appoint a special person authorised to receive service of process.

- 5 Briefly describe the aspects of the tax system relevant to franchisors. How are foreign businesses and individuals taxed?

Value added tax (VAT)

In general, all fees payable from franchisee to franchisor are subject to VAT. The general VAT rate is 25 per cent but reduced rates of 12 and 6 per cent apply to certain sectors and some sectors are even VAT exempt (2008). The VAT from purchases of goods or services, or both is generally deductible against VAT from fees and sales.

Dividends

In general, dividends to stockowners that are Swedish residents are subject to 30 per cent tax. Any person resident outside of Sweden or a foreign legal person is subject to 30 per cent coupon tax unless there is a lower percentage stated in a double tax treaty. Under domestic law, no withholding tax is imposed on dividend distributions except coupon tax. In general, business-related shares, shares that are direct investments, dividends from companies in a parent–subsidiary relationship are exempt from tax on dividends. For such exemption if the recipient is a foreign entity, the entity must be resident in a country with similar taxation on corporate income as Sweden. This condition is considered met if the net corporate income is taxed at a rate of at least 10 to 15 per cent.

Corporate tax

Companies in Sweden pay a national corporate tax of 28 per cent on their profits (2008). There are ways to defer taxation on profit by allocating up to 25 per cent of the net profit tax allocation reserves, which makes for lower effective tax rates. Foreign entities operating a branch in Sweden are also subject to 28 per cent tax but only in respect of the income derived from the branch.

Salaries

Statutory employer social security contributions amount to 32.42 per cent (2007) of total salary and benefits paid to the employee. These contributions are deductible from taxable corporate income. An employee resident or permanently staying in Sweden is obliged to pay income tax on his or hers salary. Such income is taxed mainly by municipality of residence, at rates ranging from about 29 to 35 per cent.

Tax treaties

It shall be noted that taxation of foreign entities and individuals are often subject to tax treaties which may affect the above.

- 6 Are there any relevant labour and employment considerations for typical franchisors? What is the risk that a franchisee or employees of a franchisee could be deemed employees of the franchisor? What can be done to reduce this risk?

There are no labour considerations that franchisors in particular need to observe. The franchisor and franchisee are generally deemed two separate business entities, and as a main rule no employment situation derives from the franchise arrangement. However, Swedish employment law is rigid and formal, making it difficult for a franchisor (or franchisee) to terminate employees other than for good cause. It should also be noted that the labour market in general is governed by collective bargaining agreements.

- 7 How are trademarks and know-how protected?

Trademarks

Trademarks are either protected by registration or by use of the trademark, if such use results in it becoming generally established in the applicable business or consumer circle.

Registration is made at the Swedish Patent and Registration Office (SPRO). The registration is valid for a period of 10 years. It can be renewed for subsequent 10-year periods.

Sweden has ratified the Protocol Relating to the Madrid Agreement concerning the International Registration of Marks and acknowledges European Community trademarks.

Know-how

Know-how is protected through patent protection for products and processes or by non-disclosure clauses in agreements.

Know-how is also protected to some extent by the Act on the Protection of Trade Secrets. This Act offers protection of business information from which a divulgence, if considered a secret, would be likely to cause damage to the protected from the point of view of competition. The term 'information' comprises both information documented in some form, including drawings, models and other similar technical prototypes, and the knowledge of individual persons about specific circumstances, even where it has not been documented in some form.

- 8 What are the relevant aspects of the real estate market and real estate law?

Lease of commercial premises is governed by the Tenancy Act, which is compulsory in favour of the lessee in a number of aspects such as governing the length of notice periods, providing for effects if the agreement is not made out in writing and security of tenure, etc. Lease agreements vary between being concluded until further notice or for a definite period, normally between three and five years. The normal notice period is nine months.

An important factor to bear in mind with Swedish tenancy law is that commercial lessees have an indirect security of tenure, meaning that a landlord can refuse to prolong a lease agreement only if the tenant refuses to pay a reasonable rent or if the landlord pays damages corresponding to one year's rent. In cases where location is important to the franchisor, the general practice is that the franchisor enters into the lease agreement with the landlord and sub-leases the premises to the franchisee. However, the compulsory law is also applicable to the sub-lease arrangement. To avoid the negative impacts on termination of such sub-lease arrangement, the franchisee can waive the security of tenure. In most cases, such waiver must be registered by the regional rent tribunal.

From a practical point of view, it should be pointed out that it may be difficult for a landlord (or sub-lessor) to make a tenant vacate its premises and it is not uncommon for disputes to carry on

for several years. Also, certain aspects of a tenancy dispute may not be tried before an arbitration board.

Laws and agencies that regulate the offer and sale of franchises

- 9 What is the legal definition of a franchise?

There is no legal definition of a franchise under Swedish law. A franchise agreement is defined as an agreement whereby one business entity (franchisor), against remuneration, allows another business entity (franchisee), to use the franchisor's unique business concept regarding marketing and sales of products or services. Such agreement shall be construed a franchise agreement under the Act only if the franchisee is obliged to use the franchisor's trademark or other intellectual property rights and is obliged to participate in recurring checks of compliance of the agreement.

- 10 Which laws and government agencies regulate the offer and sale of franchises?

The most important laws are the Act on Franchisors' Obligations to Inform Franchisees (2006:484), the Contract Act (1915:218), the Sale of Goods Act (1990:931), the Competition Act (1993:20) and the Contract Terms between Entrepreneurs Act (1984:292).

No agencies regulate offer and sale of franchises.

- 11 Describe the relevant requirements of these laws and agencies.

The Act on Franchisors' Obligations to Inform Franchisees is a disclosure law, which deals with pre-contractual disclosure. The Act contains only six articles. It requires of a franchisor that it, in due time prior to a franchisee entering into a franchise agreement, provides information in writing needed to understand the agreement, considering all circumstances with respect to the implications of the agreement and other conditions.

The Contract Act is a set of basic rules on how agreements are entered into (and when they are invalid). The Competition Act ensures free competition and is based on EU Law. The Sale of Goods Act is applicable on transfer of movables but may also be applicable by analogy on other kinds of transfers, such as the sale of franchises.

- 12 What are the exemptions and exclusions from any franchise laws and regulations?

The Act on Franchisors' Obligations to Inform Franchisees is a disclosure law, with no specific exemptions.

- 13 In the case of a sub-franchising structure, who must make pre-sale disclosures to sub-franchisees? If the sub-franchisor must provide disclosure, what must be disclosed concerning the franchisor and the contractual or other relationship between the franchisor and the sub-franchisor?

The sub-franchisor must provide disclosure. To the extent the specific agreement between the franchisor and the sub-franchisee is considered a franchise agreement under the Act on Franchisors' Obligations to Inform Franchisees, the franchisor is also required to provide disclosure. This question is, however, not expressly covered by the act and is a matter of interpretation.

- 14 What is the compliance procedure for making pre-contractual disclosure in your country? How often must the disclosures be updated?

The Act on Franchisors' Obligations to Inform Franchisees (2006:484) requires that precontractual disclosure is made in due time before the fact. This is most likely two or three weeks, but may be longer (or even shorter), depending on the franchise arrangement and the parties thereto.

- 15 What information must the disclosure document contain?

The information must be clear and understandable and at least contain the following:

- a description of the business that the franchisee will operate;
- information about other franchisees with which the franchisor has entered into franchise agreements, within the same franchise system and the scope of their businesses;
- information on the remuneration that the franchisee shall pay to the franchisor and other financial terms for the business;
- information on intellectual property rights that will be licensed to the franchisee;
- information on the products or services that the franchisee is obliged to purchase;
- information on all limitations on competition during and after termination of the franchise agreement;
- information on terms of the franchise agreement, terms for amendments and renewal of the franchise agreement as well as termination and the financial consequences for the franchisee upon termination; and
- information on how disputes are resolved and how costs resulting from disputes will be divided and other relevant information (such as other agreements required by the franchisor, etc).

These disclosure requirements also apply when a franchise agreement is transferred to a new franchisee, if the transfer is made with the franchisor's approval.

The disclosure requirements represent the minimum information that a franchisee should receive prior to entering a franchise agreement. A franchisor's disclosure requirements for a particular franchisee must be assessed by applying general principles and industry practice, taking all relevant circumstances into consideration.

- 16 How do the relevant government agencies enforce the disclosure requirements?

There is no government control of compliance of the disclosure requirements. The Market Court has jurisdiction over all disputes concerning the Act on Franchisors' Obligations to Inform Franchisees and will act only upon proceedings brought by a franchisee, an association of entrepreneurs, or another association which has a legitimate interest to represent entrepreneurs.

- 17 What actions can franchisees take to obtain relief for violations of disclosure requirements? What are the legal remedies for such violations? How are damages calculated? If the franchisee can cancel or rescind the franchise contract, is the franchisee also entitled to reimbursement or damages?

A franchisor that has entered into a franchise agreement without having fulfilled its disclosure obligation may, with reference to that agreement and future agreements, be subject to an injunction under penalty of a fine by the Market Court to disclose the required information. Such an injunction may also be directed towards someone who is employed by the franchisor or who acts on its behalf. The Act

on Franchisors' Obligations to Inform Franchisees does not allow the injured party to seek reimbursement, damages or other remedies. No case law is available to support the fact that the Act could be applied, by analogy, to any cases involving damages or cancellation. The fine is payable to the government and not to the franchisee.

- 18 In the case of sub-franchising, how is liability for disclosure violations shared between franchisor and sub-franchisor? Are individual officers, directors and employees of the franchisor or the sub-franchisor exposed to liability? If so, what liability?

Any potential fine or injunction would apply to the respondent named in the claim to the Market Court. Hence, a fine may be directed against the franchisor, its officers, directors, employees and anyone else acting on the franchisor's behalf.

- 19 In addition to any laws or government agencies that specifically regulate offering and selling franchises, what are the general principles of law that affect the offer and sale of franchises? What other regulations or government agencies or industry codes of conduct may affect the offer and sale of franchises?

General principles of law include the principles of freedom of contract, *pacta sunt servanda*, acting in good faith and loyalty between parties.

The Swedish Franchise Association is a member of the European Franchise Federation and as such has adopted the European Code of Ethics (www.eff-franchise.com).

Under the Code of Ethics, material intended for the recruitment of franchisees may not include misleading information or expressions with ambiguous meanings. If there are references to expected earnings in such material, such references must be objective and not misleading. The franchise agreement must be translated to the official language of the franchisee. In order for a franchisee to be fully informed when entering into a binding franchise agreement, the franchisee must have received a copy of the Code of Ethics, as well as detailed and correct written information pertaining to the relationship between the parties, in reasonable time before the franchise agreement is signed. The Code of Ethics also provides that certain principles be observed if the franchisor requires that the franchisee enter into a preliminary agreement, and that a franchisor may select and accept as franchisees only those who, upon reasonable investigation, appear to possess the basic skills, education, personal qualities and financial resources sufficient to carry on the franchised business. The Code of Ethics does not apply to master franchise relationships.

- 20 What other actions may franchisees take if a franchisor engages in fraudulent or deceptive practices in connection with the offer and sale of franchises? How does this protection differ from the protection provided under the franchise sales disclosure laws?

One of the purposes of the Act on Franchisors' Obligations to Inform Franchisees is to deter offenders from fraudulent and deceptive practices. Hence, all proceedings relating to such practices would be tried under this Act. In case of criminal fraud or similar, the relevant prosecution authority may instigate proceedings before the public courts.

Legal restrictions on the terms of franchise contracts and the relationship between parties involved in a franchise relationship

- 21 Are there specific laws regulating the ongoing relationship between franchisor and franchisee after the franchise contract comes into effect?

No.

Update and trends

The Act on Franchisors' Obligations to Inform Franchisees has been in force for a short time. The Act is not directly applicable to the relationship between franchisor and franchisee, but when the Bill was to be passed by parliament, it was mentioned that the law could be applied by analogy in a franchise relationship dispute. Possibly as a result of this, we have

learned that franchisees have argued that the franchisor party has not complied with the intents and purposes of the Act and claimed damages in franchise relationship disputes. To our knowledge, no decisions have yet been reported, supporting the argument. It remains to be seen if franchisees will have any luck.

22 Do other laws affect the franchise relationship?

The Contracts Act, the Competition Act, the Sale of Goods Act, the Contract Terms between Entrepreneurs Act, the Agency Act and the Commissionaire Act all affect the franchise relationship, to some extent, depending on the franchise relationship and the system.

Specifically, articles 36 and 38 of the Contracts Act are often argued to support that certain clauses should be mitigated on grounds that the carrying out of the contract is unreasonable (article 36) or that a certain clause restricts competition to an extent which is unreasonable.

23 Do other government or trade association policies affect the franchise relationship?

As mentioned above, the Swedish Franchise Association has adopted the European Code of Ethics. Any member of the Swedish Franchise Association is obliged to comply with the Code of Ethics, any of the association's decisions in ethical matters, and to comply with instructions that may be laid down by the Swedish Franchise Association's board of ethics. If a member does not comply with the Code of Ethics, it may be expelled from the association.

There are no reported cases involving a party arguing that franchise ethics should be considered trade practice. In other words, it is unclear whether or to what extent a court (or arbitration board) would take an ethical argument under consideration. It is not unlikely that a breach of the Code of Ethics could be considered a breach of the franchise agreement.

24 In what circumstances may a franchisor terminate a franchise relationship? What are the specific legal restrictions on a franchisor's ability to terminate a franchise relationship?

The circumstances under which a franchise relationship can be terminated are not regulated by law. In practice, the conditions for termination are agreed upon in the franchise agreement. Generally speaking, franchise agreements provide for termination when the agreement's term ends, and also provide the right for an aggrieved party to terminate in material breaches of agreement, assignment, bankruptcy, etc.

25 In what circumstances may a franchisee terminate a franchise relationship?

See question 24.

26 May a franchisor refuse to renew the franchise agreement with a franchisee? If yes, in what circumstances may a franchisor refuse to renew?

There are no general principles that require the franchisor to offer the franchisee a right to renew the agreement. Hence, a franchisor may refuse to renew a franchise agreement if the agreement does not contain an option for renewal.

27 May a franchisor restrict a franchisee's ability to transfer its franchise or restrict transfers of ownership interests in a franchisee entity?

As previously mentioned, Sweden allows for freedom of contract. Hence, a franchisor may restrict transfers of the franchise or in a franchisee entity. In fact, it is probably market practice to do so. Having said that, a franchisor is required to act in good faith and a restriction to transfer may in certain cases be deemed unreasonable.

28 Are there laws or regulations affecting the nature, amount or payment of fees?

Other than possible tax restraints on such payments, there are no laws.

29 Are there restrictions on the amount of interest that can be charged on overdue payments?

The Swedish Interest Act (1975:635) stipulates that late payments are subject to penalty interest, corresponding to the reference rate with an addendum of 8 per cent. A higher interest rate may be agreed upon (however, not usury).

30 Are there laws or regulations restricting a franchisee's ability to make payments to a foreign franchisor in the franchisor's domestic currency?

No.

31 Are confidentiality covenants in franchise agreements enforceable?

Yes.

32 Is there a general legal obligation on parties to deal with each other in good faith? If so, how does it affect franchise relationships?

Yes, in accordance with general principles and policies the parties have a loyalty duty in respect of one another. If either party is deliberately not acting at its best or acting disloyally, this could be considered a material breach of and grounds for termination of an agreement by the other party. It could also be invoked as unethical behaviour.

33 Must disclosure documents and franchise agreements be in the language of your country?

The Act on Franchisors' Obligations to Inform Franchisees does not specifically provide that the disclosure document should be in Swedish. However, the Act stipulates that the disclosure information shall be clear and understandable, so it is recommended to provide the disclosure document in Swedish.

As mentioned above, the European Code of Ethics requires that the franchisee receive a translation of the franchise agreement in its language.

34 What restrictions are there on provisions in franchise contracts?

There are no specific restrictions as to what can be regulated in the franchise agreement. The parties are free to regulate dispute resolutions forms, governing law, geographical areas, non-competition, etc, as long as such provisions are not in breach of national or EU competition law. Under competition law, franchisors may provide recommended prices and maximum end-user prices, as long as they in effect do not result in price-fixing.

Under an EC Directive, Sweden has, as of 1 July 2008, adopted a new Marketing Act. The new Marketing Act expressly prohibits marketing of 'circa prices' and 'prices starting from'. Hence, the Marketing Act and competition law seem to be contradictory to one another.

35 Describe the aspects of competition law in your country that are relevant to the typical franchisor. How are they enforced?

Swedish Competition law is based on EU competition law and the EC Regulation for vertical agreements and concerted practices has been implemented in Sweden. Hence, agreements between undertakings are prohibited if they have as their object or effect the prevention, restriction or distortion of competition in the market to an appreciable extent. This applies in particular to agreements that directly or indirectly:

- fix purchase or selling prices or any other trading conditions;
- limit or control production, markets, technical development or investment;
- share markets or sources of supply; or
- make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations, which by their nature or according to commercial usage, have no connection with the subject of such contracts.

A prohibited practice is not in breach of competition law if the affected market share is less than 15 per cent, provided that the practice is not one that is particularly restrictive. Competition issues are supervised by the Swedish Competition Authority.

It should be noted that provisions that are in place strictly to ensure that the know-how and assistance provided by the franchisor do not benefit competitors, and to protect the franchisor's identity

and reputation, do not fall within the scope of competition law. The Competition Authority can itself order injunctions combined with a fine because of infringements of the Competition Act. The Competition Authority may also issue an interim order. On petition a company may also have a fine imposed for infringements which have already taken place.

36 Very briefly describe the court system. What types of dispute resolution procedures are available relevant to franchising?

The general courts comprise district courts, courts of appeal and the Supreme Court. The general courts are competent to deal with all civil law matters as long as a special court does not have jurisdiction over a particular area. Special courts are, for example, the Labour Court and the Market Court. The regional rent and tenancy tribunals decide disputes between tenants and landlords.

In general, a losing party is free to appeal to the court of appeal, which makes a full review of the district court's decision. An appeal to the Supreme Court requires that the Supreme Court grants a leave to appeal. The main objective for the Supreme Court is to create precedents.

Any action directly based on the Act on Franchisors' Obligations to Inform Franchisees must be brought before the Market Court. The Market Court's decision may not be appealed.

Because of the general courts' heavy work load, dispute resolution in the courts is time consuming. It is not uncommon that a business dispute remains in dispute for more than five years until the courts render a final decision.

Perhaps in part because of the long turnaround times, franchise agreements in Sweden often provides for arbitration, or in some cases, even mediation, instead of submitting disputes to the general courts. The Arbitration Institute of the Stockholm Chamber of Commerce (the SCC Institute) administers arbitration proceedings under its arbitration rules and its rules for expedited arbitrations. The SCC Institute also has established rules of the Mediation Institute of the Stockholm Chamber of Commerce. The parties may also agree on ad-hoc arbitration. Such arbitration proceedings are governed by the Swedish Arbitration Act.

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