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Pronuptia de Paris v. Schillgalis: Permissible Restraints of Trade on Franchising in the EEC

I. INTRODUCTION

The international franchising community breathed a collective sigh of relief when the Court of Justice of the European Communities ("Court" or "Court of Justice") issued its decision on distribution franchising agreements, *Pronuptia de Paris v. Pronuptia de Paris Irmgard Schillgalis*,¹ in January 1986. The decision had been eagerly awaited because it was the Court's first opportunity to rule on the restraint of trade

¹ *Pronuptia de Paris GmbH v. Pronuptia de Paris Irmgard Schillgalis*, [1986] 1 Comm. Mkt. L.R. 414. The text of the original decision is in German. The case has not yet been officially reported in the Report of Cases Before the Court of Justice of the European Communities. An official English translation, Judgment of the Court, is available from the Court of Justice of the European Communities ("Court" or "Court of Justice"). The Common Market Law Reports contains an unofficial translation, as does 4 Common Market Reporter (CCH) ¶ 14,245 (1986). An abbreviated, provisional translation is contained in the Proceedings of the Court of Justice of the European Communities No. 3/86 (Jan. 27-Feb. 7, 1986). Quotations used in this Note are from the Common Market Law Reports to the extent that the meaning corresponds to the Court's translation. References to the Judgment of the Court are noted.

Professor René Joliet was the judge-rapporteur for *Pronuptia*, and Professor Pieter VerLoren van Themaat was the advocate general. "The judge-rapporteur and the advocate general follow the development of the case throughout and consider themselves responsible for the progress of the proceedings and the preparation of a basis for a solution." P. PESCATORE, COURT OF JUSTICE OF THE EUROPEAN COMMUNITIES, INFORMATION FOR LAWYERS 21 (1983). Professor Pescatore further explains the role of the judge-rapporteur:

For the purposes of the oral hearing, the judge-rapporteur has the responsibility of establishing a 'report for the hearing' which is a public document . . . set[ting] out all the particulars of the case, indicating the parties, the facts alleged or established, the submissions presented to the Court and a concise summary of the legal arguments. Parties may make any observations on this report which will finally reappear as the introductory part of the judgment itself ["Facts and Issues"].

After hearing the advocate general, the Court deliberates on the matter in private session. The discussion is opened by the judge-rapporteur who presents the Court with a written introductory note, or an oral statement as he thinks fit; he may also introduce immediately a draft judgment or reserve the right to formulate his draft after a first round of discussion According to the degree of difficulty of the case, there may be two or more successive readings of the drafts presented by the judge-rapporteur.

Id. at 22-23.

Professor Pescatore, with experience at the Court as both judge-rapporteur and President of Chamber, also notes that the "majority decision constitutes the opinion of the Court. The Court rules do not provide for the expression of any sort of individual opinions, dissenting or concurring."

Id. at 11.

aspects of franchise contracts.² The Court held that franchising³ was a legitimate business activity in its own right, distinct from exclusive distribution systems, and that restrictive contract clauses strictly necessary to preserve franchising's unique nature were justified. Further, by its comments on the types of clauses usually contained in franchise agreements, the Court recognized the "practical importance of many of the normal franchising practices to the successful operation of a franchising network."⁴ The decision cannot be seen as the foundation for an application of a "rule of reason" for the European Economic Community ("EEC"), but it is an advance in the use of ancillary restraints which promote competition within the Common Market.

In its decision, the Court of Justice recast an economic phenomenon as an independent legal concept. Before *Pronuptia*, franchise contracts were evaluated by examining separate aspects of the franchisor-franchisee relationship, an unsatisfactory process at best. Commentators have long recognized the hybrid nature of franchising, "which typically partakes of a number of . . . relationships, while not totally embracing

² *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 442, ¶ 13.

³ In his opinion in *Pronuptia*, Advocate General VerLoren van Themaat supplied the following general description of franchising:

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.

Id. at 422 (quoting Kneppers-Heynert, *Franchising en de handelsnaam: What's in a name?*, 1984 BIJBLAD INDUSTRIELE EIGENDOM No. 10 at 251).

The role of the advocate general has been explained as follows:

'[A]cting with complete impartiality and independence, to make, in open court, reasoned submissions on cases brought before the Court, in order to assist the Court in the performance of the tasks assigned to it.' These duties should not be confused with those of a public prosecutor or similar kind of functionary such as the advocate-general in a French court. The advocates-general do not represent the Communities and cannot initiate proceedings themselves.

THE COURT OF JUSTICE OF THE EUROPEAN COMMUNITIES, PERIODICAL 4/1983 8 (1983). P. PESCATORE, *supra* note 1, at 10, comments that the role of public prosecutor is entrusted to the Commission of the European Communities ("Commission").

Albert Van Houtte, former Registrar of the Court, asks, "Might it be said that the opinion of the Advocate General is equivalent to a judgment given at first instance? . . . [H]is independence and the publicity given to his opinion constitute an important safeguard for parties whose cases are dealt with by a court of first and last instance." A. VAN HOUTTE, THE COURT OF JUSTICE OF THE EUROPEAN COMMUNITIES 9 (1984).

⁴ B. Harris, *Franchising in Europe: The Judgment in the Pronuptia Case* (Remarks at the Meeting of the European Franchising Federation, Mar. 25, 1986, Brussels, Belgium—a one day conference on "The *Pronuptia* Judgment and Its Impact on Franchising, Distribution and Licensing") [hereinafter *Pronuptia* Conference].

any of them.”⁵ The marketing relationships include: “(1) employer and employee; (2) distributorship; (3) licensor and licensee; (4) agency; or (5) vendor and purchaser, to varying degrees, depending upon individual transactions.”⁶ The Court in *Pronuptia* acknowledged that franchising is more than the sum of its parts, giving legal recognition to the synergy present in franchising components.

The *Pronuptia* decision can best be understood by examining the extent to which it furthers Common Market economic goals. Franchising breaks down territorial barriers by making widespread use of single trademarks, thereby encouraging the concept of a single common market. Further, franchise networks increase the free movement of goods within the Common Market, thereby enhancing competition by providing additional sources to compete for the consumer's attention. *Pronuptia* thus recognizes and endorses franchising as a vehicle for promoting economic unity and progress, and to a great extent the decision provides legal certainty for the use of this new economic force.⁷ In its decision, the Court noted that franchise agreements are very diverse and carefully limited the judgment to distribution franchise agreements.⁸

⁵ Pengilly, *International Franchising Arrangements and Problems in Their Negotiation*, 7 NW. J. INT'L L. & BUS. 185, 186 (1985).

⁶ *Id.*

⁷ Goebel, *The Uneasy Fate of Franchising Under EEC Antitrust Laws*, 10 EUR. L. REV. 87 (1985)[hereinafter *Uneasy Fate*]. In an article written about the *Pronuptia* case while it was pending before the Court, Goebel recites the benefits of franchising. It provides new market entry, because in many franchising networks the “retail franchise outlet provides the products and services of a number of different manufacturers, in competition with existing department stores, independent retailers and in many cases with the manufacturer's own outlets.” Further, franchising exerts a downward pressure on price without affecting quality standards and expands rapidly to cover large areas of the EEC. “This means that consumers in many different EEC countries have a greater opportunity to obtain the same type of products and services on an easy and convenient basis.” *Id.* at 92.

The Commission has also commented favorably on the positive effects of franchising. Those effects include: 1) enabling small retail outlets to compete with large distribution firms; 2) letting the franchisor establish a uniform distribution network without building its own retail outlets; 3) helping new competitors enter the market and thus increasing interbrand competition; and 4) aiding in the creation of a single European market due to the effect on cross-frontier development. COMMISSION OF THE EUROPEAN COMMUNITIES, FIFTEENTH REPORT ON COMPETITION POLICY 40, ¶ 25 (1986).

For an examination of franchising and its antitrust implications in the EEC written several years before the *Pronuptia* decision, see Adams, *Franchising and Antitrust in the United Kingdom and European Community*, 26 ANTITRUST BULL. 815 (1981). For an analysis of the business community's reaction to the EEC's goal of a unified market, see Waelbroeck, *Competition, Integration and Economic Efficiency in the EEC From the Point of View of the Private Firm*, 82 MICH. L. REV. 1439, 1442-44 (1984).

⁸ Service franchise agreements and production franchise agreements were specifically excluded from the Court's decision. The Court defined the three types of franchise agreements as follows: 1) distribution franchise agreements are situations in which “the franchisee restricts himself to the sale of certain products in a shop carrying the mark of the franchisor;” 2) service franchise agreements are situations in which “the franchisee offers services under the sign and the trade name, or

Why is franchising so popular among franchisors and franchisees alike? The Court noted that a distribution franchise system similar to the one used by *Pronuptia de Paris* has benefits for both sides. The franchisor can financially exploit its commercial knowledge without investing its own capital. The franchisee lacking the necessary experience gains ready access to commercial methods which it "could otherwise only acquire after prolonged effort and research and [is] allow[ed] also to profit from the reputation of the mark."⁹ Thus, the small entrepreneur can enter a larger world of commerce by payment of franchising fees and adherence to the franchising agreement.

Franchising is a recent economic phenomenon. It has caused a rapid revolution in the business community since the 1970s, accounting for \$33 billion of total annual sales in the EEC, or 10% of the total annual EEC retail market.¹⁰ The European Franchising Federation estimates that in 1983 there were approximately 1,904 franchisors with 61,704 outlets in 11 European countries. By 1987, the European Economic Commission ("Commission") noted that there were 85,000 franchised outlets in the EEC, belonging to 1,500 franchise networks.¹¹ Statistics show a similar impact in representative EEC member states: 500 franchisors in France with 25,000 outlets, and 200 franchisors in

indeed the trade mark, of the franchisor and complies with the franchisor's directives;" and 3) production franchise agreements are situations in which "the franchisee himself manufactures, according to the instructions of the franchisor, products which he sells under the franchisor's trade mark." *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 442, ¶ 13. See *infra* note 103 and accompanying text for the Commission's definition of franchising.

⁹ *Id.* at 442, ¶ 15. Van Empel has noted that the core of the franchising concept is:

the finely tuned compromise between outside uniformity and internal independence: . . . after a certain period of time the emphasis is bound to shift in the mind of the franchisee: having grown familiar with the format, and thus becoming more sophisticated himself, he is bound to appreciate less what the system has to offer to him and to resent more what he has to do and pay in return.

Van Empel, *Franchising in the EEC: Pronuptia et Post*, 20 J. WORLD TRADE L. 401, 402-03 (1986)[hereinafter *Franchising in the EEC*].

¹⁰ U. S. DEPT. OF COMMERCE, *FRANCHISING IN THE ECONOMY, 1984-1986* (1986)[hereinafter *FRANCHISING IN THE ECONOMY*], cited in P. Zeidman, *Franchising Around the World*, Remarks at the *Pronuptia* Conference, *supra* note 4.

¹¹ The 11 countries identified by the European Franchising Federation are: Belgium, France, United Kingdom, West Germany, Italy, Portugal, Sweden, Denmark, Greece, Norway, and Spain. Sales of automobiles, trucks, gasoline (service stations), and soft drink bottlers are excluded; this data excludes hotels, except for West Germany. EUROPEAN FRANCHISING FEDERATION, *FRANCHISING IN THE EUROPEAN ECONOMY* (1985), cited in M. Clough, *Franchising in Europe After the Pronuptia Case*, Remarks at the *Pronuptia* Conference, *supra* note 4. See also *Franchising Agreements Exempt from Community Rules on Competition*, 4 Common Mkt. Rep. (CCH) ¶ 10,894 (July 16, 1987)[hereinafter *Agreements Exempt*]; *EC Commission Moves Toward Flexibility in Evaluating Restrictions in Franchises*, 53 Antitrust & Trade Reg. Rep. 96 (July 16, 1987)[hereinafter *Commission Flexibility*].

Germany with 120,000 outlets.¹² United States franchisors have also had a significant impact on the EEC; by 1984, there were 68 franchisors from the United States with 4,427 outlets in continental Europe, and 60 franchisors from the United States with 2,456 outlets in the United Kingdom.¹³

This Note examines the *Pronuptia* decision for the legal definition and substantial support it gives to the franchising concept.¹⁴ When compared to the Court's prior decision in *Établissements Consten SARL and Grundig-Verkaufs-GmbH v. Commission*,¹⁵ *Pronuptia* is seen to promote a more liberal interpretation of the EEC Treaty's competition article, Article 85. However, *Pronuptia* falls short of the advances made in *Nungesser KG v. Commission*,¹⁶ because some territorial restraints allowed under Article 85(1) in that case were not permitted in *Pronuptia*. The Court's approach in *Pronuptia* to the doctrine of ancillary restraints is also discussed. Use of this doctrine is a step forward in a "rule of reason" analysis in which the Court may be engaged in the future.¹⁷ Reactions to the case from the Commission and the international franchise community are reported.¹⁸ Finally, the Note evaluates the *Pronuptia* decision in light of the economic goals that it has advanced, and the legal certainty that it has given to the burgeoning economic force of franchising.

II. THE *PRONUPTIA* DECISION

A. Factual Background

The *Pronuptia* case arose out of a franchisee's failure to pay royalty fees. Mrs. Irmgard Schillgalis was in arrears on the 10% royalty fees owed to her franchisor, the German subsidiary of Pronuptia de Paris (the French world leader in wedding dresses and accessories). Mrs. Schillgalis had franchise agreements with Pronuptia de Paris for the contract territories of Hamburg, Oldenburg, and Hannover, and she owed DM 158,502 (approximately \$93,815) in royalties and interest on her turnover from 1978 to 1980. Mrs. Schillgalis complained that Pronuptia de Paris had not supplied the commercial and technical assistance specified in the

¹² *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 421.

¹³ FRANCHISING IN THE ECONOMY, *supra* note 10.

¹⁴ See *infra* notes 25-42 and accompanying text.

¹⁵ 1966 E. Comm. Ct. J. Rep. 299, [1966] 1 Comm. Mkt. L.R. 418. See *infra* notes 43-57 and accompanying text.

¹⁶ 1982 E. Comm. Ct. J. Rep. 2015, [1983] 1 Comm. Mkt. L.R. 278. See *infra* notes 58-78 and accompanying text.

¹⁷ See *infra* notes 79-92 and accompanying text.

¹⁸ See *infra* notes 93-109 and accompanying text.

franchise agreement.¹⁹

Pronuptia de Paris sued in German court for recovery of the fees, and won at the trial court level. Mrs. Schillgalis appealed, presenting as her defense that the franchise agreement violated Article 85(1) of the EEC Treaty²⁰ and that Council Regulation 67/67—the block exemption for certain exclusive dealing arrangements—did not apply. (Although Regulation 67/67 has been superseded by Regulation 1983/83, the proceedings first arose under Regulation 67/67.)²¹ The Oberlandesgericht (Appeals Court) agreed with Mrs. Schillgalis and quashed the trial court's judgment. The Appeals Court "held that most common franchis-

¹⁹ Venit, *Pronuptia: Ancillary Restraints—Or Unholy Alliances*, 11 EUR. L. REV. 213, 219 (1986).

²⁰ Treaty Establishing the European Economic Community, Mar. 25, 1957, 298 U.N.T.S. 11, art. 85 (entered into force Jan. 1, 1958)[hereinafter EEC Treaty]. This translation is taken from EUROPEAN COMMUNITIES, TREATIES ESTABLISHING THE EUROPEAN COMMUNITIES 285 (1978). Article 85 provides:

1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States, and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which:

- (a) directly or indirectly fix purchase or selling prices for any other trading conditions;
- (b) limit or control production, markets, technical development, or investment;
- (c) share markets or sources of supply;
- (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
- (e) 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.

2. Any agreements or decisions prohibited pursuant to this Article shall be automatically void.

3. The provisions of paragraph 1 may, however, be declared inapplicable in the case of any agreement or category of agreements between undertakings; any decision or category of decisions by associations of undertakings; any concerted practice or category of concerted practices; which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:

- (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;
- (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

See generally Comment, *Article 85 and European Antitrust Litigation: A Search for Economic Balancing*, 27 STAN. L. REV. 1275 (1975)(for an economic analysis of Article 85); Korah, *EEC Competition Policy—Legal Form or Economic Efficiency*, 39 CURRENT LEGAL PROBS. 85 (1986) (encouraging economic analysis of EEC competition policy)[hereinafter *EEC Competition Policy*].

For a current view of EEC competition policy written by Peter Sutherland before his appointment as the Commissioner responsible for competition policy at the Commission, see Sutherland, *The Competition Policy of the European Community*, 30 ST. LOUIS U.L.J. 149 (1985). Sutherland defines the three basic functions of EEC competition: "to allocate factors of production to their most productive uses, to provide an incentive to firms to use their resources in the most efficient way possible and to stimulate innovation by encouraging invention and development of new products, services and processes." *Id.* at 153.

²¹ 10 J.O. COMM. EUR. (No. L 57) 849 (1967), O.J. EUR. COMM. (special 1967 English ed.) 10 (1972). See also *infra* note 27 and accompanying text.

ing contractual provisions were anticompetitive under Article 85(1) of the EEC Treaty,"²² specifically taking issue with clauses in the Pronuptia agreement that the "franchisor could not supply any other trader in the territory covered by the contract and the franchisee had only a limited right to buy and resell other goods coming from EEC countries."²³ Pronuptia de Paris then appealed to the Bundesgerichtshof (German Supreme Court). The Bundesgerichtshof stayed the proceedings when questions arose concerning the application of EEC law to franchise agreements, and it referred several questions on EEC law to the Court of Justice.²⁴

B. The Opinion of the Court of Justice

In its response to the Bundesgerichtshof's questions, the Court established that distribution franchise agreements are unique, because they use a single mark, apply uniform commercial methods, and require royalty payments.²⁵ The agreements therefore go beyond exclusive or selective distribution systems. Had the Court adopted the reasoning of the German lower court, "franchising would have been virtually outlawed in Europe,"²⁶ unless exempted by Regulation 67/67. The Court held that Regulation 67/67, which exempted certain restrictions in exclusive distribution and purchase agreements for sale, did not apply to distribution

²² Crossick & Mendelsohn, *Franchising in Europe: Consequences of Pronuptia*, 14 INT'L BUS. LAW. 220 (1986).

²³ *Franchise Agreement Dividing Market May Run Afoul of EEC Competition Laws*, 50 Antitrust & Trade Reg. Rep. (BNA) 506 (1986).

²⁴ The questions were referred to the Court by use of the procedure established in Article 177 of the EEC Treaty, *supra* note 20. For a discussion of the drawbacks to an Article 177 reference, see generally Ulrich, *The Impact of the "Sirena" Decision on National Trademark Rights*, 3 INT'L REV. INDUS. PROP. & COPYRIGHT L. (IIC) 193 (1972), reprinted in EUROPEAN COMMUNITY LAW AND INSTITUTIONS 857 (E. Stein, P. Hay & M. Waelbroeck eds. 1976).

The manner in which the German Supreme Court phrased its questions to the Court of Justice in the *Pronuptia* case has been criticized because the questions suggested that the German Supreme Court considered franchising "merely as a form of 'distribution system' and fail[ed] to recognize that franchising is *sui generis* and requires treatment as such under EEC competition law." Crossick, *The Pronuptia Case and Its Effect on EEC Franchising Law*, 13 INT'L BUS. LAW. 294, 295 (1985).

The questions were asked within the context of four key clauses in Mrs. Schillgalis's franchise agreement with Pronuptia de Paris. At the oral hearing, the Court of Justice heard arguments on the two most important: "1. the confinement of sales to particular business premises; 2. the franchisee's obligation to buy most of its supplies from the franchisor and the rest from suppliers approved by the franchisor." Of lesser importance to the Court were the two remaining clauses covering "3. controls over advertising; [and] 4. commercial support by the franchisor," and the Court heard no oral argument on them. *Id.*

²⁵ *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 443, ¶ 15.

²⁶ Crossick & Mendelsohn, *supra* note 22, at 220.

franchise agreements.²⁷

The Court determined that there are two essential conditions for the operation of a distribution franchise system: 1) the communication of know-how and franchisor assistance in its application; and 2) the preservation of the identity and reputation of the network symbolized by the mark.²⁸ Restraints of competition imposed on franchisees which are strictly necessary to protect the two essential conditions for operating a distribution franchise system ("ancillary restraints"²⁹) do not constitute serious restrictions of competition within the meaning of Article 85(1) of the EEC Treaty.³⁰ Additionally, the Court held that Regulation 67/67, the block exemption for exclusive dealing agreements, did not apply to

²⁷ See generally Korah, *Group Exemptions for Exclusive Distribution and Purchasing in the EEC*, 21 COMM. MKT. L. REV. 53 (1984)(discussing Regulation 67/67's provisions, *supra* note 21, and how they were modified by its successor regulation, Regulation 1983/83, 26 O.J. EUR. COMM. (NO. L 173) 1 (1983)); V. KORAH, AN INTRODUCTORY GUIDE TO EEC COMPETITION LAW AND PRACTICE (3rd ed.) 73-80 (1986)(for an explanation of Regulation 1983/83). For a description of the policy behind Regulation 67/67, see Downes, *Exclusive Dealing Agreements: A Change for the Worse?*, 4 EUR. L. REV. 166, 171 (1979):

[T]he creation of a common market involves competition across national boundaries without hindrance between undertakings in different Member States; to facilitate this a manufacturer in one Member State should be permitted to enter into an exclusive dealing agreement with a distributor in another Member State so that he may compete more effectively on that market. But this applies only to exclusive dealing agreements across the boundaries between Member States

For an examination of the relationship between Article 85 and exclusive supply agreements, selective distribution systems, and exclusive purchasing agreements, see generally Chard, *The Economics of Exclusive Distributorship Arrangements With Special Reference to E.E.C. Competition Policy*, 25 ANTITRUST BULL. 405, 420-36 (1980).

²⁸ *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 443, ¶¶ 16, 17.

²⁹ The Court did not use the United States term "ancillary restraints" in its decision. Judgment of the Court ¶¶ 16, 17, 27. However, the "strictly necessary" restraints explained by the Court in the *Pronuptia* decision are identical in purpose to the use of ancillary restraints in United States case law. In *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 282 (6th Cir. 1898), *aff'd*, 175 U. S. 211 (1899), Justice Taft explained ancillary restraints:

[N]o conventional restraint of trade can be enforced unless the covenant embodying it is merely ancillary to the main purpose of a lawful contract, and necessary to protect the covenantee in the enjoyment of the legitimate fruits of the contract, or to protect him from the dangers of an unjust use of those fruits by the other party.

. . . [T]he contract must be one in which there is a main purpose, to which the covenant in restraint of trade is merely ancillary The main purpose of the contract suggests the measure of protection needed, and furnishes a sufficiently uniform standard by which the validity of such restraints may be judicially determined.

See *infra* note 80 and accompanying text.

Valentine Korah, a frequent commentator on EEC competition law, has concluded that ancillary restraints as used by the Court of Justice only require a decision "whether the ancillary restraint is necessary to make the principal transaction possible and effective: a task that national courts may find easier [than the limited economic appraisal required by the United States caselaw in balancing pro- and anti-competitive effects. *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977)]." Korah, *Pronuptia Franchising: The Marriage of Reason and the EEC Competition Rules*, 8 EUR. INTELL. PROP. REV. 99, 103 (1986).

³⁰ *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 446, ¶ 28.

franchise agreements. Thus, the Court opened the door to more restraints of trade on franchising than are present in exclusive supply and purchase agreements. The decision also recognized obligations assumed by the franchisor, especially those communicating know-how and requiring assistance to the franchisee.³¹

Permissible restraints of competition include restrictions prohibiting the franchisee from opening a shop with an identical or similar purpose in an area where it could be in competition with one of the members of the franchise network during the term of the franchise or a reasonable period thereafter. The franchisee is further precluded from selling its shop without the franchisor's prior approval, ensuring that a competitor does not indirectly receive the benefit of know-how and franchisor assistance.³² To enable the franchisor to exercise control essential to preserving the identity and reputation of the system, the franchisee may also be obligated to apply the franchisor's commercial methods and know-how.³³ Additionally, to guarantee a uniform image, the franchisee is required to sell the franchised merchandise in establishments set up and decorated according to the franchisor's specifications.

The Court also allowed a franchisor to retain approval rights before a franchisee's move to another location, since a shop's location may affect the reputation of the network.³⁴ Franchisor approval is also necessary before the franchisee may alienate the franchise, to ensure that qualified persons are affiliated with the network.³⁵ Requiring that the franchisee sell only products provided by the franchisor or its suppliers protects the reputation of the network, provides certainty to consumers, and is a practical solution to the problems of enforcing quality specifications with a large number of franchisees. The Court cautioned that this restriction cannot prevent the franchisee from obtaining the same products from other franchisees.³⁶

³¹ *Id.* at 447, ¶ 33.

³² *Id.* at 443, ¶ 16.

³³ *Id.* ¶ 18.

³⁴ *Id.* ¶ 19.

³⁵ *Id.* ¶ 20.

³⁶ *Id.* at 444, ¶ 21. Goebel has criticized the exclusive supply obligation in the Court's decision:

There is also no reference to the possibility that market conditions might make an otherwise appropriate exclusive supply obligation unreasonable and hence a violation of Article 85(1). The Court was presumably motivated in its broad statement by consideration of the particular character of the Pronuptia network *i.e.*, the sale of high fashion articles for specific purposes, weddings, but it seems unfortunate that the ruling gives the impression that exclusive supply obligations, or obligations to buy only from approved suppliers, are generally to be regarded as compatible with Article 85(1). [footnotes omitted]

Goebel, *Case 161/84, Pronuptia de Paris GmbH v. Pronuptia de Paris Irmgard Schillgalis*, 23 COMM. MKT. L. REV. 683, 697-98 [hereinafter *Case 161/84*].

Finally, network reputation is maintained by requiring franchisor approval of the nature of franchisee advertising, since the franchise image is projected through advertising. The Court stressed franchisor control only over the nature of advertising, instead of the ads themselves.³⁷ Franchisor approval of the ads themselves might be viewed as a cooperative effort in setting prices.

The Court found that franchise provisions regarding price competition and market partition are not essential to the preservation of network know-how and reputation. Clauses that restrict the franchisee's complete freedom to set its prices are restrictive of competition. However, communication of recommended prices by the franchisor is not restrictive if there is no concerted action between the franchisor and franchisee, or between franchisees, actually to apply those prices.³⁸

The Court's major attack on practices which are restrictive of competition came in the area of market partition, either between franchisor and franchisee, or between franchisees. At issue was a franchise clause limiting the franchisee to selling merchandise covered by the agreement only at the location specified, thus prohibiting the franchisee from opening a second shop. The Court viewed this clause, in combination with the franchisor's promise to guarantee exclusive use of the mark in a specific territory, as restrictive of competition within the franchise network between franchisor and franchisee, or between franchisees. Market partition arises because the franchisor in this situation must obtain agreements from other franchisees not to open a shop outside their own territories, in addition to the franchisee's own promise of the same.³⁹ This same concern with the effect of intentional restraints on horizontal competition with third parties was present in *Consten and Grundig*.⁴⁰

In a brief analysis, the Court in *Pronuptia* also held that distribution franchise agreements containing clauses partitioning the market between franchisor and franchisees, or between franchisees, are themselves capable of affecting trade between Member States, even if concluded between enterprises in the same Member State. For trade to be affected, the franchisees must be prohibited from establishing themselves in another Mem-

³⁷ *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 444, ¶ 22.

³⁸ *Id.* at 445, ¶ 25.

³⁹ *Id.* at 444, ¶ 24. If the Court had ruled Regulation 67/67 applicable to franchise distribution contracts, location clauses would have been allowed under that group exemption (as well as its successor Regulation 1983/83). Permission to use location clauses can be obtained from the Commission via an Article 85(3) exemption if group exemptions do not apply. See *infra* notes 53-56, 76-78, 99, 103, 108 and accompanying text.

⁴⁰ See *infra* notes 43-48 and accompanying text.

ber State.⁴¹

In summary, the Court held that clauses strictly necessary to protect franchisor know-how and control network identity and reputation are allowable. Clauses which partition markets or restrict the franchisee's ability to fix its own prices are prohibited. Regulation 67/67 does not apply to the distribution franchise agreements involved in *Pronuptia* because of the unique nature of the franchise relationship. That relationship is unique because it goes beyond the exchange of goods for money in an exclusive dealing relationship. It is the transmission of intellectual property, in the form of franchisor know-how, and franchisor assistance in the application of that know-how.⁴²

III. RELEVANT COURT OF JUSTICE DECISIONS

The Court's decision in *Consten and Grundig* supports the proposition that the *Pronuptia* franchise agreement partitioning the market restricts competition within the meaning of Article 85(1).⁴³ That case concerned an appeal from a Commission refusal to grant an Article 85(3) exemption to an agreement between the parties.⁴⁴ Grundig, a German sales company dealing in electronics equipment, granted a French company, Consten, exclusive rights for the sale of Grundig radio receivers, televisions, and other electronics items in France, the Saar, and Corsica.

By granting exclusive rights to Consten, Grundig was obligated to surrender to Consten its retail sales in the territory specified, and to refrain from making deliveries, either directly or indirectly, to other persons established there. Additionally, Grundig prohibited its German wholesalers and its concessionaires appointed in other countries from making deliveries from their contract territories to other contract territories.⁴⁵

⁴¹ *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 445, ¶ 26.

⁴² Adams and Mendelsohn have criticized the decision because "on the whole [it] lacks precision in that it has only provided widely drafted guidelines. The practical application of these guidelines to the present case [*Pronuptia*] is remitted to the National Court." Adams & Mendelsohn, *Recent Developments in Franchising*, 1986 J. Bus. L. 206, 216.

⁴³ *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 444, ¶ 24.

⁴⁴ An Article 85(3) exemption would have allowed clauses restrictive of competition in the distribution agreements. Sutherland, *supra* note 20, at 156, has commented that:

[C]ommunity law has, in Article 85(3) and block exemption Regulations . . . permissive rules, which, based on an analysis of the benefits to which the arrangement gives rise in all the circumstances, provide that the arrangement should be enforceable despite its restrictive impact on competition. The economic contribution to our reasonable approach is governed by the twin goals of efficiency, seen in terms of decentralised decision making and consumer welfare, and integration, based on our conviction that the interests of all Europeans—producer and consumer alike—are best served by the creation of a genuine common market.

⁴⁵ *Consten and Grundig*, 1966 E. Comm. Ct. J. Rep. at 353, [1966] 1 Comm. Mkt. L.R. at 420.

Grundig's territorial restrictions were supported by a trademark arrangement. "Grundig affixed two trademarks on its products, Grundig and Gint. The manufacturer retained ownership of Grundig for itself while enabling exclusive distributors to register the Gint trademark as their own. It set up this arrangement merely to provide exclusive distributors with trademark relief against parallel imports of genuine goods" ⁴⁶ The Court took particular note of the arrangement's effect on third parties:

[G]rundig undertook not to deliver even indirectly to third parties products intended for the area covered by the contract. The restrictive nature of that undertaking is obvious if it is considered in the light of the prohibition on exporting which was imposed not only on Consten but also on all the other sole concessionaires of Grundig, as well as the German wholesalers. ⁴⁷

The Commission found and the Court agreed that the absolute territorial restrictions in the agreement were restraints on competition not needed to obtain the benefits sought. It looked to the "spirit of Article 85" in deciding whether there was an improvement in the production or distribution of the goods, rejecting a subjective standard in which the parties to the agreement gain an advantage from it in their production or distribution activities. Noting that Article 85(3) requires the restriction to be "indispensable" to the improvement, the Court held that the improvement must "show appreciable objective advantages of such a character as to compensate for the disadvantages which . . . [the improvement] cause[s] in the field of competition." ⁴⁸

The *Pronuptia* decision advances a more liberal interpretation of Article 85 than *Consten and Grundig* because the "strictly necessary" provisions in *Pronuptia* do not fall under an Article 85(3) Commission standard of review, but can be implemented immediately without reference to individual or group Article 85(3) exemptions. ⁴⁹ In *Consten and*

⁴⁶ Joliet, *Trademark Licensing Agreements Under the EEC Law of Competition*, 5 NW. J. INT'L L. & BUS. 755, 771 (1983) (the section of the article relating to territorial and exclusive licensing, with somewhat different and less detailed footnotes, was published as *Territorial and Exclusive Trademark Licensing Under the EEC Law of Competition*, 15 INT'L REV. INDUS. PROP. & COPYRIGHT L. (IIC) 21 (1984)). A French version of the article was published as *La licence de marque et le droit européen de la concurrence*, 20 REVUE TRIMESTRIELLE DE DROIT EUROPEEN 1 (1984).

⁴⁷ *Consten and Grundig*, 1966 E. Comm. Ct. J. Rep. at 343, [1966] 1 Comm. Mkt. L.R. at 473. Advocate General VerLoren van Themaat cites this reasoning to underscore the Court's concern in *Consten and Grundig* with "intentional restrictions on horizontal competition." *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 428.

⁴⁸ *Consten and Grundig*, 1966 E. Comm. Ct. J. Rep. at 348, [1966] 1 Comm. Mkt. L.R. at 478.

⁴⁹ For an Article 85(3) exemption, however, the EEC Commission has the sole power to declare Article 85(1) inapplicable. Council Regulation No. 17, First Regulation Implementing Articles 85 and 86 of the Treaty, art. 9, 5 J.O. COMM. EUR. (No. 13) 204 (1962), O.J. EUR. COMM. (special 1959-1962 English ed.) 87 (1972).

Grundig, the Court analyzed the meaning of "indispensable,"⁵⁰ an Article 85(3) term strikingly similar to the "strictly necessary" concept⁵¹ the Court in *Pronuptia* used to determine that the majority of the franchise clauses do not constitute restrictions on competition. The difference between the two cases, however, is that while the Court in *Pronuptia* used an Article 85(3) "strictly necessary" standard to determine if there were restrictions on competition prohibited by Article 85(1), the Court in *Consten and Grundig* used Article 85(3) language for Article 85(3) application. Article 85(3) uses "indispensable" as one of several criteria to determine when Article 85(1) restraints on trade may be allowed. If restraints contribute "to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit," the EEC Treaty allows restrictions that are "indispensable to the attainment of these objectives"⁵²

In *Consten and Grundig* and *Pronuptia*,⁵³ the Court addresses market partition in terms of its effect on third parties. The Court in *Pronuptia* states clearly that market partitioning is not strictly necessary. Any territorial protection to be afforded to a prospective franchisee must be obtained through an Article 85(3) exemption, even though the franchisee "may not want to take the risk of joining the chain and making his investment, paying a relatively high entry fee and agreeing to pay a considerable annual fee."⁵⁴ The franchisor thus incurs a financial risk, because only with market partition can the franchisee "hope that his business would be profitable thanks to a certain amount of protection from competition by the franchisor and other franchisees."⁵⁵ In this decision, the

⁵⁰ The Court explains:

Furthermore, the very fact that the Treaty provides that the restriction of competition must be "indispensable" to the improvement in question clearly indicates the importance which the latter must have. This improvement must in particular show appreciable objective advantages of such a character as to compensate for the disadvantages which they cause in the field of competition.

Consten and Grundig, 1966 E. Comm. Ct. J. Rep. at 348, [1966] 1 Comm. Mkt. L.R. at 478. See also *supra* note 47.

⁵¹ The official English translation, Judgment of the Court, uses "strictly necessary," as do the Proceedings of the Court and the Common Market Reporter. "Indispensable" is used in the Common Market Law Reports. This Note uses the "strictly necessary" terminology. See *supra* note 1.

⁵² EEC Treaty, *supra* note 20.

⁵³ *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 444, ¶ 24.

⁵⁴ *Id.* at 444-45, ¶ 24.

⁵⁵ *Id.* at 445, ¶ 24. Requesting the Commission's approval of an individual Article 85(3) exemption may not be a practical alternative. The Article 85(3) notification process requires "maximum disclosure to the Commission of business practices as they actually [exist], and a maximum role for the Commission in deciding whether these practices [are] acceptable and legal." Forrester & Norall, *The Laicization of Community Law: Self-Help and the Rule of Reason: How Competition Law Is and Could Be Applied*, 21 COMM. MKT. L. REV. 11, 12 (1984). However, the volume of cases notified to the Commission far exceeds the Commission's capacity to process them. Thus, the

Court rejects a subjective standard by which to judge the restriction (though the franchisee's plight is sympathetically stated).⁵⁶ The Court aligns the reasoning here with its reasoning in *Consten and Grundig*, when it stated: "[t]his improvement cannot be identified with all the advantages which the parties to the agreement obtain from it in their production or distribution activities. These advantages are generally indisputable."⁵⁷

*Nungesser*⁵⁸ is another recent case in which the Court dealt with the issue of territorial restrictions in licensing, using a fresh legal concept to address the restrictions. Kurt Eisele, a German seed supplier and majority stockholder in the Nungesser firm, negotiated several agreements concerning the German sale and distribution of French hybrid maize seed and assigned his exclusive rights under the agreement to the Nungesser firm. Eisele's contracts were with the Institut National de la Recherche Agronomique ("INRA"), a French public research institute concerned with improving and developing plant production. INRA's 1965 contract with Eisele gave him the exclusive right to produce and distribute its hybrid maize seed varieties in Germany. INRA also agreed to prevent other suppliers from importing its maize varieties into Germany. In Clause 5 of the contract, INRA "promis[ed] that it and those deriving rights through it [would] do 'everything in their power' to prevent the export of the varieties of seeds in question to Germany." The agreement was notified to the Commission.⁵⁹

In 1973, the Louis David company made a parallel import⁶⁰ despite

notification process has, from a functional point of view, come to be used as a law-making tool rather than as a mechanism for approving individual cases The backlog of unanswered notifications is large: 3,715 in December 1982. The number of exemptions is small: 31 in ten years. The files containing about 2,000 notifications during the same ten year period were closed, some because the agreements had expired, some because one or other group exemption was available, others following informal comments from the Commission. Clearly, notification does not work as a mechanism by which any party to an agreement caught by Article 85(1) can obtain an exemption under Article 85(3).

Id. at 13-14.

Korah has noted that not only can the Commission manage only "a handful of exemptions each year," but also "to obtain an exemption one must notify an agreement to the Commission and may have to spend considerable trouble explaining the industry as well as the merits of the contested clauses to the Commission." Korah, *Critical Comments on the Commission's Recent Decisions Exempting Joint Ventures to Exploit Research That Needs Further Development*, 12 EUR. L. REV. 18, 20-21 (1987). See also McCullough, *The Continuing Search for Greater Certainty: Suggestions for Improving U.S. and EEC Antitrust Clearance Procedures*, 6 NW. J. INT'L L. & BUS. 803, 846-49 (1984).

⁵⁶ See *infra* notes 76-78, 99, 103, 108 and accompanying text.

⁵⁷ *Consten and Grundig*, 1966 E. Comm. Ct. J. Rep. at 348, [1966] 1 Comm. Mkt. L.R. at 348.

⁵⁸ 1982 E. Comm. Ct. J. Rep. 2015, [1983] 1 Comm. Mkt. L.R. 278.

⁵⁹ *Id.* at 2018-20, [1983] 1 Comm. Mkt. L.R. at 282-84.

⁶⁰ A parallel import is the import of a product from one EEC Member State to another.

Eisele's exclusive rights, and was forced to pay Nungesser damages. The company also agreed to refrain from selling INRA maize seeds or putting them into future circulation without Eisele's consent. Subsequently Bomberault, a parallel importer, advertised INRA maize seeds in the German journal *Ernährungsdienst*, which would not allow subsequent advertising because of legal action threatened by Eisele and INRA's commercial agent, Frasema. Eisele used the same journal to warn against importing INRA seeds into Germany without his approval, and he succeeded in warding off several German companies considering dealing with Bomberault.⁶¹ Bomberault complained to the Commission, which found part of Eisele's agreement with INRA in violation of Article 85(1) of the EEC Treaty. The Commission also denied an Article 85(3) exemption.⁶² Eisele appealed to the Court of Justice.⁶³

In determining the validity of Nungesser's arrangement with INRA, the Court referred to the policy it had enunciated in *Consten and Grundig*: "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."⁶⁴ However, the Court in *Nungesser* employed a concept of "open exclusive licenses or arrangements," which it differentiated from "exclusive licenses or assignments with absolute territorial protection" (i.e., closed exclusive licenses). The Court explained the distinction as follows:

[O]pen exclusive licence or assignment and the exclusivity of the licence relates solely to the contractual relationship between the owner of the right and the licensee, whereby the owner merely undertakes not to grant other licences in respect of the same territory and not to compete himself with the licensee on that territory. On the other hand, the second case involves an exclusive licence or assignment with absolute territorial protection, under which the parties to the contract propose, as regards the products and the territory in question, to eliminate all competition from third parties, such as parallel importers or licencees for other territories.⁶⁵

⁶¹ *Nungesser*, 1982 E. Comm. Ct. J. Rep. at 2020-21, [1983] 1 Comm. Mkt. L.R. at 285.

⁶² *Id.* at 2021-24, [1983] 1 Comm. Mkt. L.R. at 285-88.

⁶³ *Id.* at 2024, [1983] 1 Comm. Mkt. L.R. at 289.

⁶⁴ *Id.* at 2070, ¶ 61, [1983] 1 Comm. Mkt. L.R. at 354, ¶ 61.

⁶⁵ *Id.* at 2068, ¶ 53, [1983] 1 Comm. Mkt. L.R. at 352, ¶ 53. Korah has criticized the open exclusive licenses from an economic point of view:

Open exclusivity gives considerable protection for products of little value where freight is an important proportion of the cost or where a manufacturer supplies tailor-made products directly to a consumer, but virtually none where sales are made to dealers and freight costs are unimportant. The degree of protection should depend on the proclivity of other firms to take a free ride and the riskiness of the investment, not on how difficult it is to resell the product.

Korah, *EEC Competition Policy*, *supra* note 20, at 98.

J.D.C. Turner suggests that the open exclusivity concept is compatible with Regulation 67/67,

After explaining this licensing concept, the Court then examined the exclusive nature of the Nungesser license (to the extent it was an open license) to determine if it had the effect of preventing or distorting competition within the meaning of Article 85(1).⁶⁶ It found that Eisele's agreement went beyond restraints necessary for an open exclusive license, and further, that the settlement agreement reached earlier with the Louis David firm was also in violation of Article 85(1).⁶⁷

In an article written before his appointment to the Court, Professor René Joliet criticized the territorial distinction used in the *Nungesser* case because of the Court's view of distributorship and licensing agreements:

[T]he EC Court did not perceive the basic difference between a distributorship agreement and a licensing agreement. As a result, it inadequately transferred to licenses a distinction between open and closed agreements which it had originally devised for exclusive distributorship agreements. The Court apparently equated a licensor's promise not to compete with the licensees with the manufacturer's promise not directly to supply any other distributor in a designated area. It wrongly concluded that unlike territorial sales restrictions imposed upon licensees, the licensor's promise not to compete does not necessarily restrict competition in violation of Article 85(1).⁶⁸

The need to protect new technology (INRA developed the seeds after years of research and experimentation)⁶⁹ and new market entry⁷⁰ persuaded the Court that aspects of the INRA-Nungesser arrangement constituting an open exclusive license were valid as long as the license did not affect the position of third parties, such as parallel importers and licensees for other territories.⁷¹ Especially in the case of market entry of a new technology, a licensee might be reluctant to devote the resources necessary to develop the market if it did not have some protection against competition from licensees in other territories or from the licensor itself. Further, without the dissemination of the new technology, interbrand competition between the new product and similar existing products

Article 2. Turner, *Competition and the Common Market After Maize Seeds*, 8 EUR. L. REV. 103, 109 (1983). Article 2(1)(b) of Regulation 67/67 specifies, inter alia, that a restriction may be imposed upon the exclusive dealer to refrain (outside the contract territory) from seeking customers for the goods to which the contract relates, from establishing any branch, or from maintaining any distribution depot. Regulation 67/67 is now supplanted by Regulation 1983/83; see *supra* note 27 and accompanying text.

⁶⁶ *Nungesser*, 1982 E. Comm. Ct. J. Rep. at 2068, ¶ 54, [1983] 1 Comm. Mkt. L.R. at 352-53, ¶ 54.

⁶⁷ *Id.* at 2073-74, 2076, ¶¶ 77, 91, [1983] 1 Comm. Mkt. L.R. at 356, 358, ¶¶ 77, 91.

⁶⁸ Joliet, *supra* note 46, at 765 (footnotes omitted).

⁶⁹ *Nungesser*, 1982 E. Comm. Ct. J. Rep. at 2069, ¶ 56, [1983] 1 Comm. Mkt. L.R. at 353, ¶ 56.

⁷⁰ *Id.* at 2069, ¶ 57, [1983] 1 Comm. Mkt. L.R. at 353, ¶ 57.

⁷¹ *Id.* ¶ 58, [1983] 1 Comm. Mkt. L.R. at 353, ¶ 58.

would be affected.⁷²

Thus, the Court takes an approach to the issues in *Nungesser* that emphasizes the "economic nature and consequences of the behavior involved."⁷³ Rather than applying an overly legalistic approach, the Court in this case gave more weight to "the actual effect of the agreement on competition. Therefore, it would prefer a factual analysis of the competitive significance of an agreement to the preservation of theoretical competition at all costs."⁷⁴

In *Nungesser*, the Court's application of Article 85(3) language to an Article 85(1) determination is similar to its application in *Pronuptia*. The Court in *Nungesser* used a "new technology" argument to justify directly an Article 85(1) exclusion instead of using it to support an Article 85(3) exemption. Indeed, the language of Article 85(3) cites "technical or economic progress" as a reason to declare the provisions of Article 85(1) inapplicable to an undertaking. In *Nungesser*, the Court appears to be more flexible in its approach than the Commission, which accepted the argument, but used it to grant an Article 85(3) exemption.⁷⁵

Whereas the Court in *Nungesser* balanced the "gains of interbrand competition against the loss of intrabrand competition," and developed the open exclusive license concept, in *Pronuptia* the Court pulled back from an expansion of allowable territorial restrictions. It rejected them "without any realistic economic analysis of the necessity for such provisions."⁷⁶ In *Pronuptia*, the Court looked to the plight of franchisees and noted only that

It is certainly possible that a prospective franchisee may not want to take the risk of joining the chain and making his investment, paying a relatively high entry fee and agreeing to pay a considerable annual fee, if he were not in a position to hope that his business would be profitable thanks to a certain amount of protection from competition by the franchisor and other franchisees.⁷⁷

Having said that, the Court in *Pronuptia* advocated only a resort to Article 85(3) procedures,⁷⁸ whereas such a rationale in *Nungesser* justified partial territorial restraints. It is disappointing that in *Pronuptia* the Court did not apply the new market entry rationale to permit some territorial relief for franchisees as it did for licensees.

⁷² *Id.* ¶ 57, [1983] 1 Comm. Mkt. L.R. at 353, ¶ 57.

⁷³ Forrester & Norall, *supra* note 55, at 39.

⁷⁴ Y. Jeanrenaud, Exclusive Licenses of Patent Rights and Territorial Restraints Under EEC Law 29 (1985)(unpublished LL.M. thesis, Northwestern University Law Library).

⁷⁵ Forrester & Norall, *supra* note 55, at 39.

⁷⁶ Venit, *supra* note 19, at 218.

⁷⁷ *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 444-45, ¶ 24.

⁷⁸ See *infra* notes 53-56, 99, 103, 108 and accompanying text.

IV. PROGRESS TOWARDS A RULE OF REASON?

The Court's use of a "strictly necessary" test in *Pronuptia*, to determine which franchise clauses are necessary to preserve the essential aspects of franchising, might advance the eventual adoption of a modified version of the United States courts' "rule of reason." The rule has been defined as a "consideration of impact on competitive conditions . . . whether the challenged agreement is one that promotes competition or one that suppresses competition."⁷⁹ In his classic 1967 study of reasonableness tests from a comparative perspective, Professor Joliet discussed the rule of reason within the context of the Sherman Act:

The question of reasonableness is a question of degree The judicial discretion only relates to the significance of the restraint. Not every agreement by which a trader limits his freedom and ability to compete is automatically deemed an excessive restriction of market competition. When the agreement under attack falls short of an anticompetitive result, business considerations and good motives can be adduced to show that no wrongful purpose has inspired the conduct.⁸⁰

Similarly in the EEC, in considering whether a rule of reason can be utilized in EEC competition law, it should be noted that not all restraints on competition violate Article 85(1). Article 85(1) is meant to identify those restraints seriously restricting competition in the EEC, as enunciated in the policy statements of the EEC Treaty. Thus, an Article 85(1) exclusion is not necessarily equal in degree to an Article 85(3) exemption.

In *Pronuptia*, the Court's careful analysis, with its explanation that many franchise clauses are strictly necessary to protect know-how and to protect network identity and reputation, supplies the economic context required for a rule of reason application. Unfortunately, the Court did not then go beyond the threshold and actually conclude that some terri-

⁷⁹ See generally *National Soc'y of Professional Eng'rs v. United States*, 435 U.S. 679, 686-92 (1978)(Stevens, J.)(presenting a definition and brief history of the rule of reason). The rule, a concept with its origins in English common law (see *Mitchel v. Reynolds*, 1 P. Wms. 181, 24 Eng. Rep. 347 (1711), the leading case), requires that a restraint be evaluated for its impact on competitive conditions. If the restraint merely regulates, and thus may promote competition, it is considered ancillary and therefore a reasonable restraint on competition. Professor Joliet remarks that in his view, Justice Stevens's opinion in *National Society of Professional Engineers*, 435 U.S. at 687-92, provides the best restatement of the rule of reason. Joliet, *supra* note 46, at 773 n.68. See *Board of Trade of the City of Chicago v. United States*, 246 U.S. 231, 238 (1918)("The true test of legality is whether the restraint imposed is such as merely regulates and perhaps thereby promotes competition or whether it is such as may suppress or even destroy competition.").

Professor Pescatore has commented on guidelines used by the Court of Justice: "The case-law shows that the Court may use as a guideline any rule of law coming under the broad definition of Article 164, i.e., not only rules of Community law but also general principles of law and, where appropriate, rules of international law." P. PESCATORE, *supra* note 1, at 17.

⁸⁰ R. JOLIET, *THE RULE OF REASON IN ANTITRUST LAW* 6-7 (1967). Sherman Act, 15 U.S.C. §§ 1-7 (1982).

torial restraints were necessary to protect the franchisee's investment. Yet, the Court's language set up the possibility for a future application of the rule of reason.

The Court's stress on a "strictly necessary" test for Article 85(1) instead of Article 85(3) could be explained by examining how "restraint of competition" is defined. Professor Joliet has presented the choice thus:

If a restriction on intrabrand competition automatically brings into play the section 1 prohibition, the Commission should consider the favorable effects on interbrand competition only as it examines whether the agreement qualifies for section three exemption. If, however, a restraint of competition is defined as a restraint of market competition at large, as opposed to a mere limitation on intrabrand competition, the section 1 stage of analysis already involves a Rule of Reason approach. The second view has the advantage of freeing the Commission from issuing numerous decisions for cases where the restriction is likely to be exempted under Article 85(3). The Commission could then concentrate its time and energies on those cases where detrimental effects on intrabrand competition are not outweighed by positive effects on interbrand competition.⁸¹

In the *Pronuptia* case, Advocate General VerLoren van Themaat presented a survey of twelve Court decisions, most of which could support a rule of reason approach. Because of the similarities in the cases, the Advocate General also examined the United States Supreme Court case, *Continental T.V., Inc. v. GTE Sylvania, Inc.*⁸² That case concerned the validity of a franchise agreement between a manufacturer of television sets and a retailer; the agreement barred the retailer from selling franchised products from a location other than the one specified in the agreement. The *Sylvania* Court rejected a *per se* rule of illegality on non-price vertical restraints (including location restrictions) as well as absolute territorial restrictions. The *Sylvania* Court held that location restrictions should be judged under the rule of reason standard.

⁸¹ Joliet, *supra* note 46, at 803-04 (footnotes omitted). Sutherland, *supra* note 20, at 155-56, criticizes finding a rule of reason in Article 85(1):

[A]t best, it caricatures and, at worst, it distorts what the Commission does in its decisions . . . [A]rticle 85(3) is, in a way, our rule of reason. We do not have *per se* infringements of Article 85(1), and every case is considered under Article 85(1) on its merits. The reasonable approach under Article 85(1) has already thrown up some areas in which apparent restrictions are revealed on analyses to be innocent after all in competition terms if kept within certain bounds. Community law therefore has a *two stage approach*: under Article 85(1) a market analysis is carried out to determine whether there is a restriction or distortion of competition and, if so, whether it is appreciable; then, and only then, Article 85(3), a statutory, even constitutional, rule of reason, is applied in order to consider whether, in all the circumstances, the arrangement in question presents objective advantages justifying an exemption.

But see Joliet, *infra* note 87; McCullough, *supra* note 55, at 808 n.17 (complex evaluation under Article 85(3) factors creates more uncertainty than does the competition analysis of the United States rule of reason).

⁸² 433 U.S. 36 (1977).

The Advocate General's approach is similar to that advanced by Professor Joliet, who has emphasized the rule of reason's stimulation of interbrand competition by allowing certain territorial restraints.⁸³ The Advocate General concludes that the main issue lies in horizontal effects, that is, "the results of the agreement for third parties."⁸⁴ Based on his analysis of the prior European Court decisions, he sets forth three criteria which he believes the Court should use to judge the validity of franchise contracts: "1) whether parallel imports remain possible; 2) whether, having regard to the market position of the suppliers concerned, access to the market for other suppliers or dealers is restricted; and 3) whether the agreement results in price increases or involves price fixing"⁸⁵ The Court reached a similar conclusion in its judgment, but outlawed territorial restrictions except as exempted under Article 85(3) procedures.

In a discussion of selective distribution systems and the Court's decision in *Metro GmbH v. Commission*,⁸⁶ one commentator characterized the rule of reason as "weigh[ing] the outsider's interest in easy access to the manufacturer's selling network, the manufacturer's interest in commercial goodwill, the dealer's interest in maintaining prices and the consumer's interest in easily available high quality products at low prices."⁸⁷ Such a rule of reason could be directly applicable to *Pronuptia*, and the assessment of what constitutes "strictly necessary" includes sensitivity to these interests. The *Pronuptia* decision is another step forward in the establishment of a rule of reason for the Court of Justice. One commentator has observed that "[a] common tactic [of the Court] is to introduce a new doctrine gradually."⁸⁸ In addition to the Court decisions cited by the Advocate General, this insight is borne out by Commission decisions

⁸³ See generally Joliet, *supra* note 46.

⁸⁴ *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 434.

⁸⁵ *Id.* (footnotes omitted). Van Empel has made the following observation on the difference between the Advocate General's approach and the Court's reasoning:

[I]n the approach of the Advocate General it would seem that all the ordinary cases (either black or white) could be dealt with by the national courts, whilst the Commission would be responsible for dealing with the marginal cases on an individual basis. On the contrary, in the approach of the Court the Commission is made responsible for scrutinizing at least all those franchise contracts containing a "location clause" and/or a "pricing clause."

Van Empel, *supra* note 9, at 413.

⁸⁶ 1977 E. Comm. Ct. J. Rep. 1875, [1978] 2 Comm. Mkt. L.R. 1.

⁸⁷ Van Houtte, *A Standard of Reason in EEC Antitrust Law: Some Comments on the Application of Parts 1 and 3 of Article 85*, 4 Nw. J. INT'L L. & BUS. 497, 502 (1982). Professor Joliet has commented that the decision in *National Soc'y of Professional Eng'rs* "definitely quieted the often made assertion (especially by European writers, see Van Houtte . . .) that the Rule of Reason can justify anticompetitive agreements in the name of expediency." Joliet, *supra* note 46, at 773 n.68 (citing Van Houtte, *A Standard of Reason*, at 498, 498 n.8).

⁸⁸ T. HARTLEY, THE FOUNDATIONS OF EUROPEAN COMMUNITY LAW 60 (1981).

which also support a rule of reason approach.⁸⁹

Professor Joliet has also argued that territorial sales restrictions should not be condemned outright (that is, should not be deemed *per se* illegal). "If they serve the interest of interbrand competition by helping a new entrant, who could not otherwise find investors to put up the capital necessary to manufacture and market the product, they ought to turn out to be legal."⁹⁰ This argument could be transferred almost *in toto* to franchising, with the small business entrepreneur as the party experiencing entry barriers. However, since the Court in *Pronuptia* held that territorial restraints must be addressed by an Article 85(3) exemption, the *per se* prohibition on territorial restrictions established by *Consten and Grundig* remains.

In summary, the *Pronuptia* decision advanced the establishment of a rule of reason by allowing ancillary restraints strictly necessary to preserve the essence of a franchise arrangement to be applied in interpreting Article 85(1).⁹¹ The *Pronuptia* reasoning, in which "anti-competitive effect, actual or intended, [must] be shown before clauses are declared void

⁸⁹ See generally Van Houtte, *supra* note 87.

⁹⁰ Joliet, *supra* note 46, at 803.

⁹¹ But see Korah, *EEC Competition Policy*, *supra* note 20, at 101:

This judgment seems to reject the rule of reason in the United States. . . . When describing the advantages of franchised distribution, the Court did not conclude that it increases competition, merely that it does not, in itself, restrict it, and that the minimal restrictions required to make it viable are outside the prohibition on Article 85(1).

Contra Goebel, *Case 161/84*, *supra* note 36, at 693-94:

The ruling seems to reflect a more flexible approach to the scope of Article 85(1) (whether formally characterized as a "rule of reason" or not). . . .

It is quite surprising that the Court never indicates the need to appraise a franchising agreement, or a franchise network in operation, in its over-all market context Given rather obvious possibilities for abuse of franchising networks under certain market conditions, it might have been better if the Court's virtual "rule of reason" blessing of franchising had been limited by a reference to the need to review market impact before absolutely concluding there is no violation of Article 85(1) at all. The Court appears to have gone further than American precedents and it may be queried whether this was wise in an initial leading precedent.

Van Empel, *supra* note 9, at 411, also argues for a rule of reason in the *Pronuptia* case:

[H]ere (again) the Court has accepted to apply a "rule of reason" similar to the one in regular use in American anti-trust law. Others prefer to see this as a normal application of the *per se* provisions of Article 85(1) under somewhat exceptional circumstances. Be that as it may, what is essential for the present purpose, is that the Court accepts the consideration of contract clauses within the context of the overall relationship of the parties, and what is still more important, accepts that certain negative (from the competition law point of view, that is) clauses are simply the inescapable corollary of certain clauses which constitute the "pith and marrow" of the unique form of cooperation which is franchising.

Goebel further reasons that "[t]he Court appears to imply that franchising is pro-competitive in nature, in that it allows 'independent traders' (presumably small and medium-sized entrepreneurs) to open new retail outlets in competition with more established forms of business." Goebel, *Case 161/84*, *supra* note 36, at 687.

For a discussion of whether Article 85(1) could encompass a rule of reason, see II B. HAWK, U.S., COMMON MARKET AND INTERNATIONAL ANTITRUST 77-87 (2d ed. 1986). For an earlier discussion, see Salzman, *Analogies Between United States and Common Market Antitrust Law in the*

may enable a large number of important contracts to be enforced.”⁹² The deficiencies of the decision lie in the area of territorial restrictions. Absolute territorial restraints are prohibited in the EEC, but *Nungesser’s* open exclusive licenses allowed some flexibility. *Pronuptia* did not reaffirm *Nungesser’s* advance. Thus, territorial restrictions in franchising will continue to be considered only within the context of an Article 85(3) exemption.

V. REACTION TO THE DECISION AND CASE DEVELOPMENTS

Shortly after the Court issued the *Pronuptia* decision, Commissioner Peter Sutherland, who is responsible for competition law policy at the Commission, announced that an Article 85(3) block exemption would probably be prepared approximately two years after the decision (thus a target date of 1988). The block exemption would be based on the Commission’s experience with individual franchise cases.⁹³ The block exemption would likely include an opposition procedure,⁹⁴ and the two essential franchisor clauses cited in the decision must be present for the future block exemption to apply. Resale price maintenance is not a restriction which any future block exemption would include.

Sutherland also noted that the future block exemption might contain restrictive clauses which would make it difficult for parties to the franchise agreements to compete with each other (e.g., selling outside the shop or opening of a second shop forbidden). In specific situations, these clauses could meet the Article 85(3) conditions. The franchisees should be free to buy and sell from each other inside the EEC, and the franchise network must be organized to exercise product warranty throughout the entire EEC. Sutherland noted that the judgment left open the assessment

Field of Distribution, 13 INT’L LAW. 47, 60-66 (1979); see also Schechter, *The Rule of Reason in European Competition Law*, L. ISSUES EUR. INTEGRATION 1 (1982).

⁹² Korah, *EEC Competition Policy*, *supra* note 20, at 103.

⁹³ In his speech, *Franchise Agreements Under EEC Competition Rules*, given at the *Pronuptia* Conference, *supra* note 4.

⁹⁴ Waelbroeck explains the opposition procedure:

The Commission has recently introduced a new “opposition procedure” into various block exemption regulations, with the purpose of *accelerating the procedure* of settlement of a case. According to this procedure, agreements which contain clauses which are neither explicitly exempted, nor on the “black list” of expressly prohibited clauses, are deemed to be exempt if they are notified to the Commission, and no “opposition” is raised within six months. . . .

The importance of this new procedure can hardly be overestimated. The Commission hopes that it will result in more rapid decisions, in increased legal security, and in a lightening of its workload, thus freeing the competent services to deal more quickly and efficiently with the remaining cases.

Waelbroeck, *New Forms of Settlement of Antitrust Cases and Procedural Safeguards: Is Regulation 17 Falling Into Abeyance?*, 11 EUR. L. REV., 268, 272 (1986). Forrester & Norall, *supra* note 55, at 43 n.29, criticize the opposition procedure because it is still a notification procedure.

of franchise agreements under Article 85(3), except for the ruling that they cannot benefit from Regulation 67/67. (Regulation 83/83 replaced Regulation 67/67 relative to exclusive distribution agreements, but in Sutherland's view the difference between them is not such as to justify a different conclusion.)

Since Sutherland's reaction to the *Pronuptia* decision, the Commission has issued three individual Article 85(3) exemptions for franchising agreements and published a draft block exemption on franchising agreements. The three individual exemptions address territorial restraints and other factors cited in the *Pronuptia* decision.

The master franchising agreement for the Pronuptia organization was one of the three individual exemptions granted. While the *Pronuptia* case was pending before the Court, the franchisor Pronuptia de Paris requested an Article 85(3) exemption from the Commission in accordance with Regulation 17 procedures.⁹⁵ At the Commission's request, Pronuptia de Paris amended the standard agreement explicitly to provide certain rights to the franchisee which were implicitly recognized under earlier contracts. These rights included the following: 1) the franchisee may purchase Pronuptia products from other franchisees; 2) the franchisee may purchase goods not connected with the essential object of the franchise from suppliers of its own choice, subject to ex post facto qualitative vetting⁹⁶ by the franchisor; 3) the franchisee may set its own selling prices and is not bound by the franchisor's guidance prices. After receiving comments from interested parties,⁹⁷ the Commission approved the proposed agreement on December 22, 1986.⁹⁸ The Commission permitted the Pronuptia organization to retain clauses giving the franchisee territorial exclusivity, based on its finding that such clauses were indispensable to induce the prospective franchisee to pay the "substantial initial fee to enter the franchise system . . . [and be] provided with some protection against competition from other franchisees and from the franchisor in the allotted territory."⁹⁹

A second individual exemption was granted to the standard franchise agreements of Yves Rocher, a French manufacturer of cosmet-

⁹⁵ See *supra* note 55.

⁹⁶ Vetting is expert examination or appraisal.

⁹⁷ *Franchise Agreement Due for Approval Under Competition Rules*, 29 O.J. EUR. COMM. (No. C 178) 2 (1986), 4 Common Mkt. Rep. (CCH) ¶ 10,799 (July 31, 1986). The Commission published an official notice requesting comments from interested parties on the proposed exception.

⁹⁸ *Exemption From Competition Rules for Pronuptia Franchise Agreement*, 30 O.J. EUR. COMM. (No. L 13) 39 (1987), 4 Common Mkt. Rep. (CCH) ¶ 10,854 (Feb. 26, 1987).

⁹⁹ *Id.* The Commission's rationale for approving the location clauses follows closely the Court's reasoning in the *Pronuptia* decision. *Pronuptia*, [1986] 1 Comm. Mkt. L.R. at 444-45, ¶ 24. See *infra* notes 53-56, 76-78, 103, 108 and accompanying text.

ics, on December 17, 1986.¹⁰⁰ The Commission found that the franchise agreements were more than distribution contracts, because the franchisor undertook to transfer commercial know-how and supply technical and commercial assistance. The agreements required, inter alia, that the franchisor grant an exclusive right to the franchisee to retail the Yves Rocher products within a specified area. Although such restraints fell within the terms of Article 85(1), an Article 85(3) exemption was granted because the combined effect of the franchise clauses promoted interbrand competition. Since the exclusive territory was not large, and since franchisees could sell to any customer, competition between the franchisees was ensured.¹⁰¹

The third individual exemption was granted on July 13, 1987, to Computerland, a system of franchised outlets selling microcomputer products.¹⁰² Like the Pronuptia and Yves Rocher franchise systems, the Computerland system provided for franchisor assistance and allowed for the transmission of know-how to the franchisee. Further, the Computerland franchise agreements contained several clauses falling within the scope of Article 85(1): 1) granting of exclusive territory to the franchisor via location clauses; 2) prohibition of the franchisee's opening another outlet without the franchisor's approval; and 3) allowing sales only to end-users or other franchisees. An individual Article 85(3) exemption was granted, inter alia, because the improved distribution system benefited consumers who could buy from knowledgeable personnel, and because of vigorous competition in microcomputer retail sales.

Based on its experience with the three individual Article 85(3) exemptions, the Commission issued a draft regulation on August 27, 1987, exempting franchising agreements from Article 85(1) coverage. The draft regulation covers industrial franchises (manufacturing goods) and distribution franchises (retailing of goods by a producer or distributor); it does not exempt service franchises (supply of services) because of their unique characteristics. The draft regulation, which also covers third party master franchisors, defines franchising agreements as licenses of "intangible property rights concerning trade marks or signs and know-

¹⁰⁰ *Yves Rocher Franchise Contracts Exempted from Competition Rules*, 30 O.J. EUR. COMM. (No. L 8) 49 (1987), 4 Common Mkt. Rep. (CCH) ¶ 10,855 (Feb. 26, 1987).

¹⁰¹ *Id.* See also *Pronuptia, Yves Rocher Franchises Gain Clearances from EC Commission*, 52 Antitrust & Trade Reg. Rep. (BNA) 138-39 (Jan. 22, 1987); *Competition: By Authorising Pronuptia and Yves Rocher Agreements The European Commission Has Defined Legal Terms for Distribution Franchising*, Europe, No. 4457, Dec. 22-23, 1986, at 8.

¹⁰² *Computerland Franchising System is Exempt Under EC's Competition Rules*, 30 O.J. EUR. COMM. (No. L 222) 12 (1987), 4 Common Mkt. Rep. (CCH) ¶ 10,906 (Aug. 27, 1987). See also *EC Commission Gives Green Light to Computerland Franchise Agreements*, 53 Antitrust & Trade Reg. Rep. 174 (July 30, 1987).

how, which can be combined with restrictions relating to supply or purchase." It notes that franchises are based on a uniform system, know-how, and commercial or technical assistance from the franchisor. Further, the draft regulations allows location clauses granting territorial protection to the franchisee.¹⁰³ The draft regulation's format is similar to other block exemption regulations, and it does include the opposition procedure.¹⁰⁴ Other features of the draft regulation are similar to the three individual Article 85(3) exemptions discussed above. Comments on the draft were accepted until November 1, 1987.

Reaction to the *Pronuptia* decision from the international franchising community has generally been favorable, subject to certain reservations and points that need clarification.¹⁰⁵ One immediate problem for the franchising industry is the Court's treatment of reciprocal exclusivity clauses. Until the Commission issues the final block exemption clarifying its policy on acceptable territorial restraints, requests for individual exemptions under Article 85(3) may have to be notified to the Commission.¹⁰⁶ Another issue concerns the severability of offending franchise clauses by the national courts in the Member States. Some Member States may hold that an offending franchise clause renders the entire agreement void, while other states simply sever the prohibited clauses. Thus, franchisors may be unable to enforce their franchise agreements, including the payment of franchise fees, until the agreements receive specific exemption under Article 85(3).¹⁰⁷ The Commission's interpretation of the judgment will go far to eliminate such uncertainties.

Some issues raised by the Court may prove to be academic in the light of practical experience. For example, although the Court recognizes that a new franchisee will want territorial protection of his investment, the franchisor is unlikely to sell two franchises located close enough to cause one of the franchises to fail due to market concentration. From the franchisee's perspective, a new entrant is unlikely to buy a franchise too close to another franchisee.¹⁰⁸

The structure of franchise systems will affect market sharing and recommended price clauses. The Court correctly noted that franchising

¹⁰³ *Draft Regulation on Application of Article 85(3) to Categories of Franchising Agreements*, 4 Common Mkt. Rep. (CCH) ¶ 10,916 (Sept. 10, 1987). See also *Agreements Exempt*, *supra* note 11; *Commission Flexibility*, *supra* note 11.

¹⁰⁴ See *supra* note 94 and accompanying text.

¹⁰⁵ Clough, *supra* note 11.

¹⁰⁶ *Id.*

¹⁰⁷ *Id.*

¹⁰⁸ M. Mendelsohn, *Pronuptia—Its Legal and Commercial Consequences*, Remarks at the *Pronuptia* Conference, *supra* note 4. See also *supra* notes 53-56, 76-78, 99, 103, 108 and accompanying text.

is more than just the sale of a product, but the Commission and possibly the Court will have to acknowledge that franchising involves a specific method of operation and "trading infrastructure" as well. Rather than competing with each other, the franchisor and franchisees "provide an interdependent trading relationship resembling a multiple network which competes with others offering similar goods and services. The prices of these others are the more likely pricing reference point in market terms."¹⁰⁹ It is to be hoped that the Commission's experience with the three individual Article 85(3) franchising exemptions, its draft franchising regulation, and the business community's comments to the draft regulation will enable the Commission to prepare a final franchising regulation sufficient to address the concerns of the international franchising community.

VI. CONCLUSION

The *Pronuptia* decision is both significant and incomplete. Its obvious significance is its recognition of franchising as an independent legal concept. By defining franchising's terms for its own purposes, the Court has created a legal vehicle to accomplish its goal of a single integrated market, promoting the free movement of goods with no territorial restrictions. Franchising is no longer the stepchild of licensing or exclusive/selective distribution networks.

Also significant is the Court's sanction of ancillary restraints necessary to protect the essential elements of a distribution franchise relationship. The Court defines Article 85(1) coverage in terms of these restraints and thereby liberalizes its earlier policy and previous decisions interpreting Article 85. Though the Court has not adopted a rule of reason by its decision in *Pronuptia*, the decision forecasts a cautious step in that direction.

Since the Court chose this opportunity to recognize the economic force and individual nature of franchise relationships, it has given a powerful tool to the Community to use franchise agreements to further the goal of a single common market. The Court's early recognition of franchising is to be applauded. However, the Court has failed to transfer to franchising the machinery already established in *Nungesser* to give licensing some relief from territorial prohibitions. It is in this respect that *Pronuptia* is incomplete; some territorial protection is needed for economic vitality outside the context of an Article 85(3) exemption.

It is difficult to understand why the Court in *Pronuptia* retreated

¹⁰⁹ *Id.*

from the opportunity to extend territorial protection to another unique economic endeavor. The Court's jurisprudence enunciated in *Consten and Grundig* against absolute territorial barriers would not have been threatened by open exclusive "licenses" for franchisees. However, the Court in *Pronuptia* backed away from the opportunity to extend *Nungesser's* permissive view of territorial restraints, even though both decisions cited *Consten and Grundig* as the basis for their reasoning. It conservatively referred potential franchisees to Article 85(3) exemptions to protect their investments.

For reasons that are not clear, the Court in *Pronuptia* valued licenses as qualitatively superior to franchises, even though franchisees could use virtually the same economic argument that licensees could. By insisting on the 1966 concerns of *Consten and Grundig* instead of the 1982 economic advances of *Nungesser*, the Court in *Pronuptia* emphasizes that its goal of a single common market overrides an equally compelling argument that certain economic arrangements need some territorial protection to function as they should. The decision does, nonetheless, bestow legal certainty on the status of franchise agreements.

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