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The Higher Court in Ljubljana provides guidance on statutory rules applicable to franchise agreements

A franchise agreement allows the franchisee to operate a business using the franchisor's trademark and know-how. Although franchising is used in practice, it is not regulated under Slovenian legislation. Slovenian courts interpret franchise agreements as so-called mixed agreements, which contain elements of both an agency agreement and a sale and purchase agreement.

In October 2024, the Higher Court in Ljubljana (the 'Court') (Judgement no. VSL Sodba I Cpg 74/2024, dated 21 October 2024.) ruled on a case concerning the validity and enforceability of non-compete clauses and the applicability of statutory provisions otherwise applicable to agency agreements in the context of a franchise agreement.

Case summary

The parties (both commercial companies) entered into a point of sale (POS) management agreement for the sale of automotive spare parts. The agreement included a non-compete clause prohibiting the seller from engaging in competitive activities after the termination of the agreement.

After less than a year the plaintiff (the principal) withdrew from the agreement, whereupon the defendant's (the seller's) legal representative immediately started working for competing companies. The issue in dispute concerned the validity of the non-compete clause in the agreement.

The court of first instance held that the agreement in question was a mixed agreement containing essential elements of an agency agreement, under which the agent was authorised to sell the relevant goods in the name and on behalf of the principal. Therefore, the issues pertaining to the termination of the agreement are to be regulated by the statutory rules applicable to termination of an agency agreement.

On appeal, the plaintiff argued that the agreement was not an agency agreement, but rather a franchise agreement. The Court upheld the judgment of the first judge, confirming that the agreement in question was indeed an agency agreement. The Court explained that the most important distinctive element of a franchise agreement is that the franchisee acts in its own name and on its own account. In the relevant case, however, the agreement clearly stated that the defendant was acting in the name and on behalf of the plaintiff. The Court further clarified that the provisions on the termination of an agency agreement apply to franchise agreements as well.

The Court held that in the context of an agency agreement a non-compete clause shall be enforceable if upon the termination of the agreement the principal pays to the agent an appropriate compensation and a severance payment (also known as indemnity). Such requirement is mandatory, and the parties are not able to agree otherwise. In the relevant case, the plaintiff did not pay the defendant either of those sums, thereby effectively waiving the non-compete clause.

Severance payment

In the relevant case, the Court dealt with the question of the existence of a severance payment, to which the agent is entitled upon termination of his agency agreement. Since the plaintiff did not pay any indemnity at all, the Court did not address the appropriateness of the indemnity amount. Nonetheless, the Court confirmed that the statutory rules on termination and indemnity for agency agreements also apply to franchise agreements.

Slovenian statutory provisions do not explicitly determine the indemnity amount for agency agreements. A specific formula for calculating indemnity is also not determined by court practice. Under the law, the indemnity amount depends on the circumstances of each case but should reflect the advantages that the agent created for the principal. Additionally, the commission obtained by the agent for contracts concluded after the termination of the agency agreement and any non-compete obligations should also be considered when setting the indemnity amount. The only limitation foreseen by the law is that the indemnity shall not exceed the average annual commission over the last five years or the relevant shorter period of the validity of the agency agreement.

Final commentary

Franchise agreements are not explicitly regulated under Slovenian law and the recent ruling by the Higher Court in Ljubljana highlights some of the elements relevant for distinguishing between different types of commercial agreements, such as agency, distribution and franchise agreements. It also provides some additional (though limited) guidance on issues like non-compete clauses and severance payments for different types of vertical agreements.