

FRANCHISING

LEGAL UPDATE

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Protecting confidential information

In order to effectively run any business, it is necessary that employees be given access to information that is commercially sensitive and confidential. Such information has often been developed or acquired at considerable expense and effort, and is of significant value to the business and to its competitors.

Key message

Franchisors face unique challenges with respect to confidential information, which means it is even more important to have the right protections in place.

For a franchisor, the issue of confidential information is particularly relevant given that much of the value of a franchised business lies in the proven methods and procedures of the business. Customer lists, unique methods or recipes, technological advances, specific ways of doing business, and many other types of inside knowledge must all be kept secret in order to safeguard the commercial edge that they provide.

General duty of confidence

Not everything that an employee learns or is told while working for a business will be subject to a duty of confidence. Information is not a trade secret merely because the business says it is. For example, the 'know-how' acquired in the course of a career, being the manner in which a skilled worker performs their job and the techniques that may be used, is not a trade secret, and it may be that an employee is not prevented from legally divulging information that an employer presumed would be deemed confidential.

Protective measures

To guard against this risk, employers should ensure that all employees have written employment contracts. This is essential in the case of senior employees who invariably have access to information that could greatly damage the business if secured by competitors.

Broadly, there are two types of clauses that should be included in a contract of employment:

- » a Confidential Information clause; and
- » a Restraint of Trade clause.

Confidential Information

This clause should expressly state the information or classes of information that the employee must not reveal or use in any way on termination of his or her employment (eg, sales and marketing information, names and details of customers, information on prospective franchise sites etc). While this is often no more than a restatement of the employee's legal obligation, it should still be included for a number of reasons:

- » procuring the employee's express agreement to keep secret certain specific information alleviates any need to later prove that the information in question qualifies as a 'trade secret';
- » drawing the employee's attention to the obligation should prevent any innocent disclosure of information; and
- » an action against the employee in contract – with the document itself as evidence – is likely to be significantly easier to prosecute and prove than an action relying on the general legal obligation alone.

Restraint of Trade

A restraint of trade provides a second layer of protection for a business, in that it prohibits an employee from working for a competitor at all (for a specified period and in a defined area) after the termination of his or her employment.

As a result, even the 'know-how' of that employee, which can be extremely valuable in the case of highly skilled persons, cannot be utilised by a competitor. However, it is

important to note that while common in employment contracts such clauses will not be enforced against the employee unless they provide for restrictions of time (eg, 6 months) and area (eg, within a radius of 10km of the business) that are no more than are reasonably necessary to protect the interests of the business.

An employee cannot be indefinitely prevented from working for a competitor, and any restraint of trade must be carefully drafted to be effective.

Conclusion

Given the increasing mobility of the workforce, a carefully drafted employment contract, including both of the clauses mentioned above, will provide substantial protection to any franchise business, and is a measure that should be considered by all such businesses.

Chris Nikou | Partner
Martin Richardson | Senior Associate

Green means BP

If you are driving along the highway and see a service station up ahead which is predominantly 'green', who do you believe the proprietor of the service station is? The answer, according to the Federal Court, should be BP.

Key message

*The Federal Court's recognition of green with respect to BP service stations proves it is willing to recognise the importance of colour in branding, **providing a level of uniqueness can be proven.***

In 1991 and 1995 BP applied for the colour green as a trade mark in respect of its service stations. After some time, these applications were accepted for registration, however Woolworths (which at the time was just about to commence its own service station business) opposed the applications. Woolworths opposition was upheld by the Trade Marks Office and BP then appealed to the Federal Court.

The Federal Court's decision in October 2004, held that BP had used the colour green in respect of its service stations for a substantial period of time and had therefore acquired distinctiveness in the colour, such that people recognised green (in relation to service stations) as indicating BP. Put simply, BP had established that the colour green operated as its badge of origin. BP also used the BP name and shield logo as badges of origin, however the green colour was found to also be a key indicator of BP on its own.

Colour can form a very important part of a business' branding and provided a business can show that it has used a colour, or combination of colours, over a substantial period of time (BP had adopted green and yellow as its corporate colours in Australia in 1956, and green became adopted as the primary colour in 1988 worldwide) such that the public associates the colour with their product or service, the colour can be registered as a trade mark.

This is a powerful right as it allows the trade mark owner a monopoly in respect of a specified colour when used in relation to specified goods or services. While substantial evidence of use will be required for colour trade mark applications, it is clear that colour is now becoming a more accepted form of branding and is another crucial element of marketing and advertising that needs to be accounted for, particularly in determining the elements of branding which are worthy of protection.

Lisa Egan | Solicitor

Is Your Re-Sale Policy Going to Cost You?

A large wholesaler of premium skin care products recently learnt a very important lesson - that imposing minimum prices on retailers can be very costly. Costly to the tune of fines totalling \$250,000. And it got worse - the press coverage on the decision was substantial and damaging to its reputation. Clearly, attempting to fix or maintain prices in the supply chain can be a very expensive business.

Key message

Re-sale price maintenance can be costly, and for any business that wants to set Recommended Retail Prices it is critical you have a clear understanding of the legal requirements. Even a small retailer can land a complaint with the ACCC that has severe repercussions.

So, what was the Problem?

The imposition of minimum prices on those that you supply goods/services to is known as 're-sale price maintenance'. In effect, re-sale price maintenance is a vertical type of price-fixing and is prohibited under the Trade Practices Act. In fact, the prohibition is a strict one - it is prohibited regardless of the effect it has on competition in the market. The reason for the prohibition is that competition is supposed to be free and unrestricted - and imposing minimum prices inhibits that freedom.

Factual Background

Dermalogica Pty Ltd is a premium brand skin care product wholesaler who sells to more than 700 retailers Australia wide. Yet, it was complaints by only 2 of the beauty salons it supplied that resulted in the \$250,000 fine. The two beauty salons provide a range of beauty services to individual consumers and sell Dermalogica products from their websites at prices below Dermalogica's RRP. It was Dermalogica's response to the salons' discounting that gave rise to the allegations of re-sale price maintenance.

In essence, Dermalogica threatened to cut off supplies of its products to both salons if they did not revert to Dermalogica's RRP. When one of the salons queried: "I am not sure about the legalities of what you're doing to me. Can you control prices?" The response from Dermalogica was "Yeah, we can even cut off supply and close your account."

Another visit from a Dermalogica representative took the following tone "Look Georgio, I would hate to see this problem cause Dermalogica to cancel your account," the response to which was

"I am not just some little therapist who will get scared or back off". And the salons did not back off, it continued with its policy of discounting.

At this point, the salons attention was drawn to Dermalogica's website which clearly stated that "In order to maintain Dermalogica's premium brand image and consistent pricing strategy, we strongly discourage the selling of Dermalogica products for more or less than their suggested retail prices. Deviating from suggested retail prices is strongly discouraged.... A violation of this policy can result in account termination and legal action."

Unfortunately, Dermalogica had the threat of 'legal action' the wrong way around - it was its behaviour in attempting to control price that gained the attention of the ACCC.

And so, it was the 'little therapist' who didn't get scared and back-off who triumphed over the multi-national corporation. And this is an important lesson to remember - an aggrieved person need only contact the ACCC and report complained of conduct. The ACCC can then chose to pursue the matter at its own expense. In this case, it was the complaint of a self-described 'little therapist' that resulted in fines totalling \$250,000 (not to mention the negative publicity and other associated costs).

What are the Penalties?

A corporation guilty of re-sale price maintenance can be fined up to \$10 million. Individuals involved in the breach face fines of up to \$500,000. Injunctions can be obtained to stop the breach and if a person has suffered loss, they can apply for damages. So, in all, attempting to increase profit margins by fixing re-sale prices can prove to be very costly.

In the Dermalogica case, the Court noted that the size of the penalty is determined by a number of factors, including the deliberateness of the conduct, whether the conduct was brought about by senior management and whether the company has a corporate culture conducive to compliance with the Act. In this case, the conduct was found to be deliberate (illustrated by it being published by their website), the result of an attitude generated at the senior level within Dermalogica's management and occurred in the absence of a compliance program.

Indeed, the court found Dermalogica's behaviour to be 'deliberate, bold and somewhat aggressive'. And, despite Dermalogica's conduct causing no significant economic loss or damage to the salons, the judge found this to be of little weight, finding that 'an attempt to distort the market must be nearly as blameworthy and as proper an object of the Act's deterrent penalty regime as is an actual distortion of the market'.

Lessons to be Learnt

Things You Can't Do

- » If you are a corporation, or a person supplying a corporation, you cannot engage in re-sale price maintenance.
- » You cannot:
 - » attempt to induce a person not to sell your products or services at less than a price specified by you;
 - » make it known that you will not supply a person unless that person agrees not to sell below the price specified by you;
 - » enter into an agreement for the supply of goods or services which provides that the person will not sell below the price specified by you; and
 - » withhold supply because a person has not agreed not to sell below your minimum price, or because they have sold below your minimum price.
- » You cannot provide a formula which in essence results in a minimum price. To be

in breach of the TPA a dollar value need not be specified, it is enough that a formula be provided for a breach to be constituted.

- » You cannot seek justification in your motives. It is no excuse that you were persuaded or coerced into re-sale price maintenance by other stockists (ie stockists who are unhappy with their competitors offering goods/ services for sale at a lower price).
- » It is no excuse that you are simply passing on a price that was stipulated to you.

Things You Can Do

- » You can have suggested RRP's, however persons to whom you supply must be free to sell below that price point.
- » You can instigate, maintain, regularly update and communicate a compliance program. This is particularly important, as anything done on your instructions or on your behalf is deemed to have been done by you.
- » You can have an informed point of contact within your organisation. In this case, the judge was particularly damning on Dermalogica's corporate culture and noted that: "A person had been designated as Dermalogica's 'compliance officer'. However, under cross-examination it became apparent that this person had not significant awareness of the stipulations of the Act." Ensure that your contact is appropriately trained.

Conclusion

Dermalogica learnt a very costly lesson. As Graeme Samuel, Chairman of the ACCC noted 'suppliers engaging in this conduct who come to the attention of the ACCC can expect prompt and rigorous enforcement action which at the end of the day may involve a potentially substantial monetary penalty'. The judge noted that there was 'at least, a rash disregard by Dermalogica to there being any legal problem with its conduct, and at most a dogmatic belief that all was fair in business'.

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