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MAY 2000

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IOWA REFORMS FRANCHISE RELATIONSHIP LAW

On April 14, 2000, the governor of Iowa signed a new law that makes substantial changes to the Iowa Franchises Law, which governs the relationship of a franchisor and franchisee in areas like encroachment, termination and transfer. Prior to these changes, the Iowa relationship law was widely viewed as one of the most onerous of its kind from the franchisor's perspective. Although the revised statute still substantially restricts a franchisor's rights to enforce its franchise agreement, some of the most objectionable provisions of the law have been eliminated.

Substantial changes were made to statutory provisions regarding the parties rights on a franchisee's transfer of the franchise. The general rule on franchisee transfers remains: a franchisor may refuse to approve a franchise transfer only if the transferee fails to satisfy the franchisor's reasonable current qualifications and the refusal is not arbitrary or capricious. However, under the old statutory scheme, many events that are ordinarily defined as "transfers" in franchise agreements (such as succession on a franchisee's death or disability, transfer among owners of a corporate franchisee, and transfer to a franchisee's spouse or children) were exempt from the franchisor's approval powers. The new law removes this provision, as well as sections prohibiting the use of releases, non-competition covenants and new forms of contract.

The new law also revised some provisions relating to encroachment. A franchisor may be liable for damages if it opens or franchises a new outlet under the same brand name that adversely impacts an existing franchised location, but only if (a) the new outlet is in unreasonable proximity to the existing location, and (b) the existing franchisee's gross sales over the 12 months following the new outlet's opening decrease by 6% or more (up from 5% under the old law) from the outlet's gross sales over the previous 12 months. Also added is a provision denying claims by franchisees who have already

been granted reasonable territorial rights. The new law does require that franchisors establish a formal dispute resolution procedure for franchisee encroachment claims, which must include a mediation process.

Other changes in the law also increase the likelihood that a franchise agreement's provisions will be enforced as written. The statute allows franchisors to terminate franchise agreements only for "good cause" and provides franchisees an opportunity to cure defaults. Despite this provision, under the old law, a franchisor could not terminate an agreement unless it could show that all franchisees had been treated alike, a standard that would straitjacket enforcement efforts. The new law also removes a restriction on enforcing non-compete clauses after the franchise term ends. With a few narrow exceptions, the former statute required franchisors to allow franchisees to obtain equipment, supplies and services from any source they desired, as long as the franchisor's quality standards were met. The new provision removes this restriction but franchisors (except in a few circumstances) still may not require franchisees to buy merchandise from only one designated supplier. A franchisor can, however, require franchisees to buy items only from approved suppliers and may reasonably reject suppliers that the franchisee proposes.

Finally, the good faith section has been supplemented by a provision that applies good faith duties to encroachment situations but also subjects such claims to the standards already detailed in the encroachment section of the statute.

Although this presents merely a summary of the important changes in the Iowa franchise relationship law, clearly progress has been made in reforming this anti-franchising legislation. Note, however, that the new law applies only to franchise agreements signed after July 1, 2000; prior law will govern existing agreements.

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