BEYOND CONTRACT AND ORGANIZATION? THE EXTERNAL LIABILITY OF FRANCHISING SYSTEMS IN GERMAN LAW*

GUNTHER TEUBNER** [1]

Contents

I. Piercing the "Contractual Veil"?

Franchising systems are hybrid structures between "market and hierarchy"[2]. Their hybrid character causes problems concerning the balance of power within the relationship. German private law tries to solve them with the help of the equally hybrid category of a contractual organization — long-term obligations and relational contracts[3]. In addition to these internal problems, the external liability of franchise systems, which in German law until now has hardly been analysed, is not easy to deal with in legal terms since they vacillate irritatingly between contract and organization. On the one hand, franchise networks operate in the form of highly organized distribution systems; they possess not only a strictly coordinated hierarchical organization but also a strong corporate identity[4]. On the other hand, they take the form of harmless individual contracts between a number of sales outlets (franchisees) and one central sales headquarters (franchisor). This breaking-down of the organization into a number of individual

---

* Translation by Viviane Ahlborn.

** Professor of Law, University of Bremen and European University Institute, Florence.

1 For helpful criticism I would like to thank Amadeu Abril y Abril, Andreas Schwartze and Sean Smith.

2 The title of Oliver E. Williamson's book, Markets and Hierarchies, New York 1975, has become the impetus for innumerable studies dealing with the area between contract and organization.

3 Cf. on this subject the national reports by T. Daintith, St. Macaulay, S. Sciarra and E. Schanze, the economic analysis of franchise contracts by A.W. Dnes and the general report by Ch. Joerges in this volume.

4 An excellent analysis of organization research on franchising is to be found in M. Martinek, Franchising: Grundlagen der zivil- und wettbewerbsrechtlichen Behandlung der vertikalen Gruppenkooperation beim Absatz von Waren und Dienstleistungen, Heidelberg 1987, 75 et seq.

contracts results more or less automatically in a breaking-down of the liability of the organization as a whole into the liability of each individual member. And this, notwithstanding that franchise systems produce externalities like any other formal organization. Franchisors and franchisees make internal agreements to the disadvantage of third parties. Franchising organizations collectivize action without simultaneously collectivizing responsibility. They increase and shift risks to third parties, without measures being taken to ensure their absorption[5]. Polemically speaking, we find in franchising contracts the same organized lack of responsibility as in many other formal organizations[6].

This becomes clearer if we look at the "external relations" of franchise systems. Consumer interests are primarily affected[7]. The technical instructions of the franchisor to the franchisees frequently contain mistakes "in the system" which lead to considerable damage, despite the utmost care being taken by the franchisor. This is especially true for service industries, the area in which franchising is most often used. Can the contractual liability of each individual franchisee guarantee sufficient consumer protection if the mistake lies not in the individual performance of the franchisee but "in the system"? Similar problems involving consumer protection are posed when some customer services are organized by the franchise headquarters itself, as is the case in hotel franchising or transportation franchising with central logistics. Is there a need here for "piercing the contractual veil", a legal instrument making the central office directly liable?

Competition interests are also affected. The marketing and advertising strategies adopted by the franchisor sometimes contain statements which discredit com-

5 Cf. G. Teubner, in: R. Wassermann (ed.), Alternativkommentar zum BGB, Vol. 3, Neuwied-Darmstadt 1980, § 242, no. 58. As a concrete example of organized lack of responsibility in the setting-up of a distribution network, see the decision of OLG Karlsruhe, Neue Zeitschrift für Verkehrsrecht 1989, 434.

6 On the (lack of) responsibility of formal organizations, J. Coleman, Power and the Structure of Society, New York 1974; J. Coleman, The Asymmetric Society, Syracuse 1982, 79 et seq.; J. Coleman, Responsibility in Corporate Action: A Sociologist's View, in: K. Hopt/ G. Teubner (eds.), Corporate Governance and Directors' Liabilities: Legal, Economic and Sociological Analysis on Corporate Social Responsibility, Berlin-New York 1985, 69, 75 et seq.; J. Coleman, Foundations of Social Theory, Cambridge 1990, 421 et seq.; U. Beck, Risikogesellschaft: Auf dem Weg in eine andere Moderne, Frankfurt/M 1987, 35, 76 et seq.; U. Beck, Gegengifte: Die organisierte Unverantwortlichkeit, Frankfurt/M 1987 & 1988, 96 et seq.; P. French, Collective and Corporate Responsibility, in: LIB New York 1984; K. Röhl, Die strukturelle Differenz zwischen Individuum und Organisation, in: Festschrift für Stiefel (1987), 573 et seq.; H. Geser, Organisationen als soziale Akteure, Zeitschrift für Soziologie 1990, 401 et seq.

7 On the subject of franchise systems' liability towards consumers see E. Körner, Die Produzentenhaftung des Lizenzgebers bei der Lizenz über gewerbliche Schutzrechte und Know-how, Neue Juristische Wochenschrift 1985, 3047-3052; Ch. Joerges, Franchiseverträge und Europäisches Wettbewerbsrecht: Eine Kritik der Pronuptia-Entscheidungen des EuGH und der Kommission, Zeitschrift für das gesamte Handelsrecht und Konkursrecht 151 (1987), 195, 210; W. Bauder, Der Franchise-Vertrag: Eine systematische Darstellung von Rechtstatsachen, Tübingen 1988, 10. The dangers for consumer protection that are inherent in franchise systems have led the European Commission to intervene in the terms of guarantee of franchise systems. Cf: Regulation no. 4087/88, 30 November 1988 on the application of Art. 85 (3) of the Treaty on groups of franchise agreements, OJ L 359/1988, 46-52, WuW 1989, 306 et seq.

petitors, who then suffer losses when the franchisee enforces them. To what extent is the franchise organization as a whole responsible for actions of a member of the system who acts contrary to the rules of fair competition[8]? What is the situation regarding liability if the advertising strategy is not imposed unilaterally by the franchisor, but is agreed upon by an internal "advertising committee" which decides on basic policies for advertising and marketing plans and on which franchisees' representatives have a seat and a vote?

Furthermore, creditors' interests are affected. If, as is often the case, the bookkeeping and accounting of the franchisees are done centrally, any mistakes made can have an effect on the basis for decision-making adopted by (potential) lenders. Credit is granted where it would otherwise be withheld. The franchisee is unable to make the repayments. Should the central office also be made liable?

Finally, the interests of the general public are also affected if the franchise package provides for a course of action which might endanger public goods, such as the environment. Here, the internal division of labour is such that we might well question whether the individual liability of a franchisee is an adequate way of trying to prevent environmental damage[9].

In all these cases we must ask whether the franchisor and the franchisee should not both be made liable, especially where the franchisee has limited liability (e. g. if the franchisee is a GmbH — private limited company) or if he cannot fulfil his obligations due to insolvency or bankruptcy. These problems are always rendered more serious when the defective action of the franchisee is based on a decision made by a franchise committee (product policy committee or advertising committee)[10], i. e. by all the franchisees. In this case the question of the liability not only of the franchisor but of all the franchisees must be raised.

How can the law cope with the organizational peculiarities and risks of contractual networks like these, especially with regard to their external responsibility? The mere individual liability of the franchisees which, because of the "legal nature" of franchising, is not "allowed" to take the tight organizational structure of the distribution system into consideration is open to the following points of criticism:

(1) *Extent of duty*: Is it sufficient to concentrate liability in the contractual duties of the individual franchisee while imposing less extensive tortious duties on the other members of the franchise system? Or should the franchisor as the central office or even other franchisees be subject to increased contractual duties towards third parties?

---

8 A decision by the Bundesgerichtshof, Neue Juristische Wochenschrift 1980, 941, deals with a similar constellation involving an authorized dealers' network.

9 Cf. on the subject of the control of behaviour by means of liability for damage to the environment G. Brüggemeier, Deliktsrecht, Baden-Baden 1986, 452 et seq.; id., Umwelthaftungsrecht, Kritische Justiz 1989, 209 et seq.

10 See W. Bauder, op. cit. (note 7), 214 et seq.; P. Müller-Graff, Franchising — a Case of Long-Term Contracting, 144 Journal of Institutional and Theoretical Economics 122, 135 (1988).

(2) *Division of labor*: Customer services are organized partly decentrally and partly centrally by the head office. Is there not, then, a need to take account of any third party effects ("Drittwirkung")[11] of the franchise contract? This would give the customer a contractual claim not only against the franchisee but also against the franchisor?

(3) *Attributing liability to the organization*: German law on vicarious liability in § 831 BGB[12] allows rather generously for exemptions. This raises questions of whether this regulation is sufficient to deal with the franchisor's liability for the actions of franchisees, bearing in mind the organizational nature of the franchising network. Is there a need for a special type of organizational liability which would also cover the close coordination of actions between the central office and branch offices?

(4) *The arbitrariness of legal form*: Some franchising systems are organized as a single company (central office with branches), as a group of companies or as a quasi-franchising system in the form of a cooperative society[13]. All of them are subject to corporate liability in the broadest sense. By comparison, franchisees organized on a contractual basis are privileged as far as liability is concerned. Can this be justified, or does it represent an illegitimate saving in transaction costs? Can liability law be used to eliminate functionally irrelevant differences among franchising systems?

---

11 J. Gernhuber provides a systematic analysis of the effects of contractual obligations on third parties, Das Schuldverhältnis: Begründung und Änderung, Pflichten und Strukturen, Drittwirkungen, Tübingen 1989, 460 et seq.

12 § 831 BGB: Whoever orders another to do something is bound to compensate any damage which the other illegally inflicts on a third party in the execution of the order. If, in the choice of agent, and if, insofar as he has to provide equipment or tools or has to supervise the carrying out of the order then in that provision or supervision, the principal has observed the standard of care required in practice, or if the damage would have been produced by an application of this standard, then the duty does not arise.The same responsibility applies to those who contract with the principal to take over the handling of the affairs described in paragraph 1, clause (2)".
In a more modern drafting style:
(A) "Whoever orders another to do something is bound to compensate any damage which the other illegally inflicts on a third party in the execution of the order.
(B) The duty does not arise;
  (i) if the principal has observed the standard of care required in practice,
    (a) in the choice of agent, and
    (b) insofar as he has to provide equipment or tools or has to supervise the carrying out of the order, then in that provision or supervision; or (ii) if the damage would also be produced by an application of the above standard of care.
(C) The same responsibility applies to those who contract with the principal to take over the handling of the affairs described in paragraph 1, clause (2)".

13 On various forms of franchising and their differences see M. Martinek, op. cit. (note 4), 33 et seq., 75 et seq.; W. Bauder, op. cit. (note 7), 42 et seq.

(5) *Deterrence*: If we take the deterrence rationale of liability law seriously[14], then the mere individual liability of the branch offices would entail an inefficient allocation of distribution operations because the regulatory targets would have been wrongly chosen. The regulatory signals of liability law either do not reach the franchisor at all, as the center of self-regulation in the franchising system, or only indirectly; in any event, they have no direct effect on his cost/benefit calculations[15].

(6) *Risk shifting*: Splitting the franchise organization into a multitude of independent contracts has the effect of shifting liability risks from the central office to the sales outlets. Is this acceptable from the standpoint of liability policy? Do we not face a situation similar to the limiting of liability within a group enterprise ("Konzern")? Does not this similarity justify — and if so on what conditions — a piercing of the "contractual veil" which would exclude negative external effects on customers and creditors?

These questions which occur in franchising and other distribution systems are similar to those appearing in the grey area of "contorts" as well as in the law of group enterprises. This is not purely coincidental, since all these phenomena can be seen as hybrid structures between "market and hierarchy". They all contain aspects of the interpenetration of contract and organization. Not for nothing do contemporary economists and organization theorists concentrate on this area[16]. These intermediate organizations have become so important in the USA and Western Europe and above all in Japan, that the "third arena of resource allocation" (in addition to market and organization) is already being spoken of[17]. In the face of this remarkable economic and social dynamism, all those disciplines involved — organizational, legal and economic — have only been able to look on, in a rather helpless way, with their institutional separation of market and organization. Only very recently have attempts been made to cope with the hybrid structure using more sophisticated concepts and theories. Franchising is just one small part of this whole problem area. But its high degree of centralization and its economic dynamism make it particularly suitable as a way to illustrate the legal problems concerned with this kind of hybrid structure.

---

14 E. Deutsch, Haftungsrecht I, Köln 1976; H.-J. Mertens, in: Münchener Kommentar zum BGB, Intro. to § 823, nos. 41 et seq.; K. Larenz, Schuldrecht I, Munich 1987, 421 et seq., 423; J. Esser/ H.-L. Weyers, Schuldrecht II, Heidelberg 1984, § 53, 4.

15 For the German discussion on the regulatory opportunities presented by liability law see J. Adams, Ökonomische Analyse der Gefährdungs- und Verschuldenshaftung, Heidelberg 1985, 88 et seq.; P. Behrens, Die ökonomischen Grundlagen des Rechts, Tübingen 1986, 174 et seq.; G. Brüggemeier, Deliktsrecht, Baden-Baden 1986, 47 et seq.; G. Brüggemeier, Produkthaftung und Produktsicherheit, 152 Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht 511, 512 et seq.(1988); H.-B. Schäfer/ C. Ott, Lehrbuch der ökonomischen Analyse des Zivilrechts, Berlin 1986, 85 et seq.; H. Kötz, Deliktsrecht, Frankfurt/M 1988, no. 36-41; H. Kötz, Ziele des Haftungsrechts, in: Festschrift für Steindorff (1990), 643 et seq.

16 On this subject see infra part III.

17 K. Imai/ H. Itami, Interpenetration of Organization and Market, 2 International Journal of Industrial Organization 285, 296 (1984).

The problems involved in providing a legal definition of the economic phenomenon of franchising — as a nexus of contracts ("Vertragsverbindungen")[18], as a partnership or as mere tortious "transactions" — reflect real trends in the evolution of the interpenetration of market and organization[19]. The external effects of this interpenetration become relevant in law. How can the law cope adequately with the structural peculiarities of organized distribution systems? Should the law provide for liability under partnership law ("Verband"), contractual liability of the interlinked business enterprises ("Verbund") or liability under the law of torts for harm caused as a result of risks associated with this type of transaction ("Verkehr")?

II. Contract or Organization?

In the history of German civil law doctrine, the organizational elements of distribution systems have always resisted being labelled as mere contracts. At first the Reichsgericht and some authors had indeed taken the organizational nature of the distribution system into account, and had qualified authorized dealers' networks as being "similar to partnership" and thus, analogously, subject to the law of associations[20]. However, in subsequent developments of German legal doctrine, the organizational nature of certain distribution systems (commercial agent ("Handelsvertreter"), authorized dealer ("Vertragshändler"), commission agent ("Kommissionsagent") and more recently the franchisee) has been suppressed. However, as is so often the case with suppression, the disturbing elements return through the back door.

The process of suppression was carried out primarily with two legal constructions. The emphasis on the dominance of the central office and the extremely one-sided orientation to its interests made it possible to remove the distribution systems from the context of civil law partnership ("BGB-Gesellschaft"), which presupposes equality among partners and a common objective. Within the newly discovered trinity of "Tauschhand", "Gesamthand" and "Treuhand" (exchange, joint ownership and fiduciary relationship)[21], distribution systems could be clas-

---

18 German doctrine defines "Vertragsverbindungen" (nexus of contracts) as a multiplicity of bilateral or multilateral contracts which are referring to each other. Examples are subcontracts in the construction area or credit sales which are financed by a bank. For an extensive discussion, see J. Gernhuber, op. cit. (note 11), 710 et seq.

19 On this subject see G. Teubner, Recht als autopoietisches System, Frankfurt/M 1989, 160 et seq. (English translation: Blackwell, London, forthcoming).

20 E.g. Reichsgericht RGZ 65, 37; 78, 385; 92, 201; 95, 166; cf. also RGZ 95, 66; RGZ 145, 275; E. Ackermann, Eigenhändler als "Generalvertreter", Wissenschaft und Recht 1929, 31 et seq.; this can occasionally be found today, e.g. M. Löwisch, Die Stellung der Produzentenhändler im Wettbewerbsbeschränkungenrecht, Tübingen 1965, 145 et seq.; W. Schluep, Der Alleinvertriebsvertrag, Bern 1966, 25.

21 F. Beyerle, Die Treuhand im Grundriß des deutschen Privatrechts, Weimar 1932, 16 et seq.; H. Würdinger, Gesellschaften I, Karlsruhe 1937, 9 et seq.

sified as fiduciary relations since it emphasises safeguarding interests[22]. In this way their contractual nature was made clear — paradoxically by reason of their hierarchical organization. Organizational elements were compensated for with the legal concept of "integration" ("Eingliederung") of the distribution agent into the distribution organization[23]. The second legal construction stressed the residual autonomy of the sales outlets, that is, the independent pursuit of their own profits. This made it possible for the distribution systems to set clear limits against employment relationships on the one hand and partnership relationships on the other?[24]

However, the back door could not be kept shut in either of these constructions. Once again it is franchising and the hybrid nature of distribution systems which pushes it open in a legally disturbing way. This should not surprise us, since "[t]he central feature of franchise organizations is the presence of both market-like and firm-like qualities"[25]. Or even: "Franchising is more like an integrated business than a set of independent firms"[26]. On the one hand, in contrast to the traditional authorized dealers, a franchise system is highly centralized. This tightly organized internal coordination as well as its external appearance as a single competitor, and as a marketing unit with a uniform image, make it increasingly difficult to speak, in this context, of a mere bundle of contracts between autonomous units[27]. On the other hand, there appears to be a phenomenon of "partnership franchising" ("Gleichordnungs-Franchising") where we simply cannot talk of a dominance of central office, of its interests and its powers of management. This arrangement seems to be the European equivalent to the American franchising systems of the third generation, the "partners for profit", especially franchised hotel chains and also franchising in the transport and fashion industries[28]. So, in this context, the difference between safeguarding the in-

22 P. Ulmer, Der Vertragshändler, Munich 1969, 321 et seq.; H. Stumpf, Der Vertragshändlervertrag, Heidelberg 1979, 25 et seq.; C.T. Ebenroth, Absatzmittlungsverträge im Spannungsverhältnis von Kartell- und Zivilrecht, Konstanz 1980, 32 et seq.; K. Schmidt, Handelsrecht, Köln 1982, 567; A. Baumbach, K. Duden/ K. Hopt, Kommentar zum Handelsgesetzbuch, Munich 1989, Intro. to § 373, no. 5a. Constant court practice since Bundesgerichtshof BGHZ 54, 340.

23 P. Ulmer, op. cit. (note 22), 206.

24 P. Ulmer, op. cit. (note 22), 322; M. Mack, Neuere Vertragssysteme in der Bundesrepublik Deutschland: Eine Studie zum Franchising, Bielefeld 1975, 100; H. Weber, "Franchising" — ein neuer Vertragstyp im Handelsrecht, Juristische Ausbildung 1983, 347, 351.

25 S.W. Norton, An Empirical Look at Franchising as an Organizational Form, 61 Journal of Business 197, 198 (1988).

26 A.W. Dnes, The Economic Analyisi of Franchising, in this volume (at 133 et seq.).

27 M. Martinek, op. cit. (note 4), 123 et seq. gives a particularly convincing intepretation of the findings of organization theory (214 et seq.), criticizing solutions which are purely contractual in nature.

28 M. Martinek, op. cit. (note 4), 378 et seq. in reference to the American third generation franchising systems ("partners for profit", cf.60 et seq.) and German organization literature at 159 et seq.; W. Bauder, op. cit. (note 7), 97 et seq. disputes, on the basis of empirical studies, the existence of franchise systems based on partnership principles. He states that in practice only a subordination franchising ("Subordinationsfranchising") exists which has elements of sales promotion duties imposed by the franchisor. Ch. Joerges, in his contribution to this volume (at 11 et seq.), also takes this as a basis for his thoughts on the general need for some kind of social protection for the franchisee.

terests of the franchisor and having a community of interests can no longer in itself exclude an interpretation in terms of the law of associations.
Findings in comparative law support this interpretation to a certain extent. In the USA, court practice and legislation often use the term "community of interests" to describe the above-mentioned third generation of franchise systems which are organized as "partners for profit". These franchise systems are not actually being called partnerships but they are subject, in certain aspects, to the law of partnerships[29]. There is a tendency, especially in France, to view franchise systems as associations. Not only is the "groupement d'intéret économique" held to be the most suitable legal form[30], but there have also already been legislative proposals that franchise systems should be granted an independent legal personality[31]
In Germany it is Martinek, in particular, who has recently demanded in a painstaking study, containing a wealth of material from organization research, that the law should take more account of organizational elements. Martinek suggests the application of the law of partnerships to (some) franchising arrangements. According to Martinek, franchising systems become organizations governed by partnership law when a certain level of cooperation has been exceeded. He distinguishes four constellations: subordination, coordination, coalition and confederation. The terms are self-explanatory. He suggests that contract should be kept for "subordination franchising" and also for the relatively loose ties in "coordination franchising". However, because of the intensity of their cooperation, the two other constellations cannot be classified as anything other than communities of interest ("Zweckgemeinschaften"), governed by partnership law: "coalition franchising" as a bundle of partnerships and "confederation franchising" as one large partnership, covering the central office and the sales outlets[32]. Indeed, Martinek even goes so far as to make strictly organized forms of franchi-

---

W. Bauder's empirical arguments appear problematic because he bases them exclusively on the formal wording of contracts which say relatively little about the interest and power structures described by M. Martinek. In this context, M. Martinek's empirical basis, which takes account of market power between industry and trade, appears more convincing. Of course, whether the phenomenon of partnership franchising requires a company law interpretation as M. Martinek suggests, is a different matter. In the meantime even the Federal Cartel Office ("Bundeskartellamt", BKA) appears to be considering franchising on an equality of power basis. Cf. BKA WuW 1986, 87; BKA WuW 1987, 1051; BKA WuW 1989, 850. For transport franchising this seems reasonable if independant transport firms join their efforts to provide a complete parcel service. Even if the individual transport enterpreneur thus acquires the "status" of a franchisee, the application of socially protective principles seems to be inappropriate.

29 Cf. the description of franchising law in the USA in V. Behr, in: M. Martinek, Der Franchise-Vertrag. Eine Untersuchung zum Recht der USA mit vergleichenden Hinweisen zum deutschen Recht, Frankfurt/M 1976, 52 et seq.; M. Martinek, op. cit. (note 4), 60 et seq., 178 et seq.

30 J. Guyénot, Les contrats de concession commerciale, Paris 1968, 340 et seq.

31 See, on this subject, M.-P. Piriou, Selektiver Vertrieb und Wettbewerbsregeln der Europäischen Gemeinschaft, GRUR Int. 1980, 321 et seq., 327.

32 M. Martinek, op. cit. (note 4), 231 et seq. Also P. Müller-Graff,, op. cit. (note 10), 141 argues for a company law classification of some franchise systems.

sing subject to the German law concerning group enterprises[33]. He distinguishes between highly centralized forms of "subordination franchising" which become subject to the law of subordinate group enterprises ("Unterordnungskonzerne") and those of "confederation franchising" which are assigned to the law of coordinate group enterprises ("Gleichordnungskonzerne")?[34]

This interpretation of closely coordinated franchising networks as partnerships (or even as corporate groups) has consequences not only under the law of associations and antitrust law, but also, of course, for their external liability. An analogous application of the general principle of liability under the law of associations in § 31 BGB[35] seems possible for coalition franchising, which is interpreted as a civil law partnership, and even more so for confederation franchising as a large civil law partnership[36]. As far as extremely hierarchical forms of subordination franchising are concerned, external liability based on the principles of a "qualified" group of companies "a la Autokran & Tiefbau"[37] is unavoidable, to say nothing of "piercing the corporate veil"[38] as a means of direct liability of corporate groups under German law?[39]

However striking this construction may appear at first sight, on closer inspection we would want to ask whether this contract/organization dichotomy can really do justice to the hybrid nature of the franchising networks? Turning one form into the other does not prevent suppression. On the contrary — it doubles it! When Martinek says "organization", he suppresses contract; when he says "contract", he suppresses organization.

---

33 German legislation and case law have developed an extremely complex law of group enterprises. For a useful English language summary see H. Wiedemann, The German Experience with the Law of Affiliated Enterprises, in: K. Hopt (ed.), Groups of Companies in European Laws, Berlin 1982, 21 et seq.; M. Lutter, The Law of Groups of Companies in Europe: A Challenge for Jurisprudence, Forum internale 1983, 1, 5 et seq.; H.-D. Assmann, Microcorporatist Structures in German Law on Group Enterprises, in: D. Sugarman/ G. Teubner (eds.), Regulating Corporate Groups in Europe, Baden-Baden 1990, 317 et seq. For the law of liability governing group enterprises, see M. Lutter, The Liability of the Parent Company for the Debts of its Subsidiaries under German Law, Journal of Business Law 1985, 499 et seq.

34 M. Martinek, op. cit. (note 4), 633 et seq.

35 § 31 BGB is the fundamental rule governing liability of an association for the actions of its organs: "The association is responsible for the damage which the board, a member of the board, or another constitutionally appointed representative in the exercise of his powers, has caused to a third party as a result of an action requiring compensation".

36 Cf. P. Ulmer, in: Münchener Kommentar zum BGB, § 705, no. 189 et seq. for a discussion of the liability of civil law partnership according to § 31 BGB. Its analogous application to marketing systems (authorized dealers) is considered by W.-H. Roth, Comment to OLG Karlsruhe, Neue Zeitschrift für Verkehrsrecht 1989, 435.

37 These are landmark decisions of the German Federal High Court concerning external liability of highly centralized groups of companies: Bundesgerichtshof BGHZ 95, 330 — Autokran; BGH Zeitschrift für Wirtschaftsrecht 1989, 440 — Tiefbau. For a brief discussion, see H.-D. Assmann, op. cit. (note 33), 337.

38 As established in the leading cases of, e.g. D.H.N. Ltd. v. Tower Hamlets [1976] 1 WLR 852, C.A., and Firestone Tyre/ Rubber Co. v. Llewellyn [1967] 1 WLR 464, H.L.

39 See G. Teubner, Die "Politik" des Gesetzes im Recht der Konzernhaftung, Festschrift für Steindorff (1990), 261 et seq.

When Martinek qualifies loosely coordinated franchising systems as contracts he contradicts the criticism that he himself developed with the help of organization theory. He does exactly what he accuses prevailing academic opinion among the lawyers of doing: he ignores the organizational elements[40]. The common objective of sales-promotion, the system's objective of organizing distribution, as it is so clearly defined by Martinek himself, is merely "economic" and of no legal relevance at all. In legal terms only the individual objectives of the parties to the contract exist. There is no duty on the part of the members to further sales. There is simply a one-dimensional duty to safeguard the interests of central office[41]. This construction is particularly strange in the case of "coordination franchising", i. e. where franchised hotel chains or transport franchising with central logistics are concerned. According to Martinek, the franchisees do not have a duty to further the common objective but only reciprocal duties of dealing in good faith based on the law of exchange contracts.[42]

When Martinek turns more closely coordinated systems into civil law partnerships he does the same thing but in reverse. He suddenly plays down, in legal terms, the individual objectives of the parties to the contract which can still be found, even in the case of very close coordination, in the siphoning off of residual profits. For him, the common purpose is now relevant, not only economically but also legally, expressed in terms of a common objective under § 705 BGB[43]. However, the individual interests of the parties, by contrast, are no longer legally relevant but are merely "economic" motives.[44]

It seems as if neither a purely contractual classification nor a capsizing of contract into organization can do justice to the hybrid nature of franchising. One should therefore try to mix the types[45]. For example, a simple combination[46] could then be broken down into areas of contractual and company law. But this would not help us any further with franchising contracts, where the fields of action are so intermingled that a splitting up according to areas of exchange and cooperative cannot be undertaken. The result would be a thoroughly hybrid contract in which these elements are inseparably combined.[47] However, there is a

---

40 On the one hand M. Martinek, op. cit. (note 4), 196, 214 et seq. (criticism of jurisprudence oriented towards individual contracts), on the other hand at 247, 251 (common interest in subordination franchising and in coordination franchising is only economically, not legally relevant (!)) and at 256 et seq., 378 et seq.

41 M. Martinek, op. cit. (note 4), 280 et seq.

42 M. Martinek, op. cit. (note 4), 378 et seq., especially 386.

43 § 705 BGB: "Through the partnership contract, the partners mutually bind themselves to promote, in the manner defined in the contract, the achieving of a common purpose, in particular to make the agreed contributions".

44 M. Martinek, op. cit. (note 4), 251 et seq., 391 et seq., 412, 420 et seq.

45 See P. Ulmer, in: Münchener Kommentar zum BGB, Intro. to § 705, no. 70 et seq.; W. Hadding, in: H.T. Soergel/ W. Siebert, Kommentar zum BGB, Intro. to § 705, no. 17 et seq.; more general M. Wolf, in: Soergel-Siebert, Kommentar zum BGB, § 305, no. 27 et seq.

46 RGZ 69, 127, 129 et seq.; BGHZ 60, 362.

47 M. Wolf, in: Soergel-Siebert, Kommentar zum BGB, § 305, no.22.

noticeable hesitation in academic opinion. These contracts are usually classified as being sui generis or at least as being similar to those governed by company law, apart from the increased duties of loyalty, common to long-term contracts.[48] As far as distribution systems are concerned, in German legal doctrine every associational element is rejected[49]. While each party does have a sales interest, this does not necessarily amount to a common objective in legal terms. Here too, we can see a curious picture developing. As soon as a common objective is assumed, then the contractual elements are played down. As soon as exchange elements are assumed, then there is a tendency to deny any common objective. At this point, the following question springs to mind. Is it impossible, as a matter of legal construction, to conceive of action being oriented simultaneously towards both common and individual objectives?

If one examines the treatment of distribution networks under the German law of torts one is confronted with a similar uncertainty. The classification of branch offices as vicarious agents ("Verrichtungsgehilfen") gives rise to a peculiar oscillation between dependence and independence. On the one hand their duty to comply with instructions is emphasized, a duty which turns distribution agents who are independent businessmen into "vicarious agents"[50]. On the other hand their individual responsibility as independent economic actors is emphasized in order to exclude vicarious liability according to § 831 BGB[51]. Even under the law of torts, then, the hybrid nature of distribution organizations becomes apparent.

III. Network

Are we facing here the paradoxes of unitas multiplex which appear in distribution systems just as they do in group enterprises[52]? Perhaps the legal suppression of either organizational or contractual elements, the hesitation in the field of hybrid contracts, and the oscillation in the treatment of distribution networks under the law of torts do not result from the usual legal problems of definition, but from the real contradictions in organized distribution itself? Could it be that eco-

48 M. Löwisch, in: J. v.Staudinger, Kommentar zum BGB, § 305, no. 22.

49 P. Ulmer, op. cit. (note 22), 321 et seq.; H.-D. Köhler, Über die Anwendbarkeit von Gesellschaftsrecht auf die sog. gesellschaftsähnlichen Rechtsverhältnisse, Münster 1974, 134 et seq.

50 BGH 33 Neue Juristische Wochenschrift 941 (1980), expresses this opinion but only if a sales agent (in this case an independent commercial agent) had assumed duties within the direct business area of the central office (in this case the supervision of a stand at an exhibition). In contrast, OLG-Karlsruhe Neue Zeitschrift für Verkehrsrecht 1989, 434, 435, refuses to apply § 831 BGB because of the independent status of the commercial agent. Critical comments by W.-H. Roth Neue Zeitschrift für Verkehrsrecht 1989, 435. Cf. also G. Schröder, Recht der Handelsvertreter (1973), § 86 HGB, no. 50, with further sources.

51 See note 12; A. Zeuner, in: Soergel-Siebert, Kommentar zum BGB, § 831, no. 21.

52 See G. Teubner, op. cit. (note 19), 149 et seq., 172 et seq.

nomic actors have invented organizational arrangements which, in the form of literal coincidentia oppositorum, cannot be grasped with conventional legal terminology? In what follows I would like to adopt the thesis that franchising, as one particularly extreme type of closely coordinated distribution system, represents the creation of a new kind of "network organization", and that this allows their legal treatment, their juridical classification, and their external liability to appear in a new light.

At present, many disciplines are fascinated by "networks". Organization theory first dealt with them in the study of inter-organizational relations, the so-called organization sets. This covered relations between formal organizations which were primarily based on cooperation and not on competition[53]. In group sociology the term found its way into "personal networks", loose forms of cooperation which show neither the intensity nor the bureaucratic disadvantages of formal organization[54]. In political science, "policy-networks" is the name given to a decentrally-organized order of political actors, and which is used particularly in the analysis of neo-corporatist phenomena[55]

The term was used juridically in the German public law discussion of whether legal persons possess constitutional rights and especially in the context of the constitutional right of assembly[56]. The idea of a "net contract" was used in contract law to describe banks' payment transactions[57]. And in company and labour law the concept of a network was used to deal with the external liability and internal constitution of decentrally-organized group enterprises[58]. Recently the

---

53 W. Evan, The Organization Set, in: J. Thompson (ed.), Approaches to Organizational Design, Pittsburgh 1966; H. Aldrich/ D.A. Whetten, Organization-sets, Action-sets, and Networks, in: P.C. Nistrom/ W.H. Starbuck (eds.), Handbook of Organizational Design, Oxford 1981.

54 N.M. Tichy, Networks in Organization, in: P.C. Nistrom/ W.H. Starbuck (eds.), Handbook of organizational Design, (1981); S. Birley, The Role of Networks in the Entrepreneurial Process, 1 Journal of Business Venturing 107 (1985); R.K. Mueller, Corporate Networking, New York 1986; I. Kaneko/ K. Imai, A Network View of the Firm, First Hitotsubashi-Stanford Conference (1987).

55 K. Hanf/ F. Scharpf, Interorganizational Policy-making, London 1977; M. Trasher, Exchange Networks and Implementation, 11 Policy and Politics 375 (1983); G. Lehmbruch, Concertation and the Structure of Neo-Corporatist Networks, in: J.H. Goldthorpe, Order and Conflict in Contemporary Capitalism (1985), 60; J. Sharpe, Central Coordination and the Policy Network, Political Studies 1985, 361 et seq.; V. Schneider, Politiknetzwerke der Chemikalienkontrolle: Eine Analyse der transnationalen Politikentwicklung, Berlin 1988, 9, 42 et seq.

56 K.-H. Ladeur, Ein Vorschlag zur dogmatischen Neukonstruktion des Grundrechts aus Art. 8 GG als Recht auf "Ordnungsstörung", Kritische Justiz 1987, 150; Th. Blanke's criticism of this text: Kritik der systemfunktionalen Interpretation der Demonstrationsfreiheit, Kritische Justiz 1987, 157; cf. also K.-H. Ladeur, Zu einer Grundrechtstheorie der Selbstorganisation des Unternehmens, in: Festschrift für Ridder (1989), 179 et seq.

57 W. Möschel, Dogmatische Strukturen des bargeldlosen Zahlungsverkehrs, Archiv für die civilistische Praxis 186 (1986), 211 et seq.

58 G. Teubner, op. cit. (note 19), 168 et seq., 176; G. Teubner, Unitas Multiplex, Zeitschrift für Unternehmens- und Gesellschaftsrecht 1991, 189 et seq. (forthcoming); G. Teubner, op. cit. (note 39); S. Sciarra, A Labour Law Perspective on Group Enterprises in Italy: Networks versus Hierarchies; G. Vardaro, Before and Beyond the Legal Person: Group Enterprises and Industrial Relations, both in: D. Sugarman/ G. Teubner (eds.), Regulating Corporate Groups in Europe, Baden-Baden 1990, 226 et seq., 413 et seq.

term has also caused a sensation in economics. While the sharp dichotomy of market and hierarchy had long prevented a suitable analysis, economists can now no longer resist the fascination of Japanese suppliers' networks and other, similar institutional arrangements. The new solution is as follows: "strategic networks" have a definite competitive advantage over both contractual relations and integrated organizations (advantages concerning specialization within the firm, and at the same time production outside the firm of other components with low transaction costs and constant cost pressure due to existing alternative solutions on the market).[59]

If one wants to go beyond a mere metaphorical use of the image of a "net" and its "knots", then one usually makes the following theoretical statements. By network one generally means a decentrally organized order of cooperation among autonomous actors[60]. Networks are seen as loose forms of cooperation which do not possess the same intensity as formal organizations. Economists like using suggestive formulae like "something between markets and hierarchies"[61], "managed economic systems"[62], "complex arrays of relationships among firms"[63]. Oliver Williamson's theory of hybrid arrangements can be taken as representative. Williamson pictures a sliding scale of "Economic Institutions of Capitalism", from spot-market transactions via long-term contracts to integrated firms, which only differ from one another by governance structures. Franchising and other hybrid arrangements are to be found at a point on this scale somewhere between market and organization, arising from concrete calculations of transaction costs by the resource owners concerned.[64]

Even if these ideas aim in the right direction they still have not grasped the crucial point. Networks should not be seen as institutions "between" contract and organization, but as institutions "beyond" contract and organization. Network arrangements are only possible if the distinction upon which they are based is firmly institutionalized. The starting point is in the recognition of both "market failure" and "organization failure"[65]. In each case it is a question of the precari-

---

59 K. Macmillan/ D. Farmer, Redefining the Boundaries of the Firm, 27 The Journal of Industrial Economics 277 (1979); I. Kaneko/ K. Imai, op. cit. (note 54); J.C. Jarrillo, On Strategic Networks, Strategic Management Review 1988, 9.

60 V. Schneider, op. cit. (note 55), 9.

61 H.B. Thorelli, Networks: Between Markets and Hierarchies, 7 Strategic Management Journal 37 (1986).

62 K. Macmillan/ D. Farmer, op. cit. (note 59), 284.

63 J. Johanson/ L.G. Mattson, Interorganizational Relations in Industrial Systems: A Network Approach Compared with the Transactional Approach, International Journal of Management and Organization (1988).

64 O.E. Williamson, The Economic Institutions of Capitalism: Firms, Markets, Relational Contracting, New York 1985.

65 K. Imai/ H. Itami, op. cit. (note 17), 298 et seq., offer a diagnosis of market and organization failures in this area and suggest certain cures of "interpenetration".

ous relationship between variety and redundance[66]. Contractual relations are extraordinarily flexible, adaptable and innovative; however they show little long-term orientation, coherence, endurance or accumulated experience. The invention of the formal organization was able to solve these problems of redundance, but only rather one-sidedly and at the expense of variety. Rigidity, bureaucracy, motivation problems, lack of innovation and high information costs are not only a problem of state organizations but specifically of private firms. The sense of "missed opportunities" provides the driving force behind a new experimentation with institutional arrangements which can be described as the "re-entry" of a distinction into the area the distinction has itself distinguished[67]. Networks, then, result from a re-entry of the institutionalized distinction between market and hierarchy into the area which the market/hierarchy distinction itself distinguishes. In the words of the Japanese teachers Imai & Itami:

> Market principles penetrate into the firm's resource allocation and organization principles creep into the market allocation. Interpenetration occurs to remedy the failure of pure principles either in the market or in the organization[68].

In this way two types of network can be distinguished depending on which side of the distinction the reentry is made — market or organization. "Organization networks" arise when organizations repeat in themselves the internal differentiation of the economy into a formally organized area and a spontaneous area. Decentralized group enterprises in the famous "multidivisional form" are the most significant innovation in this area. In comparison with this, "market networks" arise in areas organized on a market basis. Contractual relations repeat within their limits the distinction between market and hierarchy by including organizational elements in the contract. Networks such as these can rarely organize themselves spontaneously. A hub firm, a focal firm or an "impresa guida" regularly plays the key role in the construction and running of coordination. This specialization of one of the firms in the field of strategy and coordination can, but need not, be based on a presupposed difference in market power (e. g. between different levels of the market: industry-trade, or industry-supplier); network-centres on the basis of an equal division of power are just as widespread[69]

The result of this re-entry of organization into contract are:

> Strategic Networks'. In them, a 'hub' firm has a special relationship with the other members of the network. Those relationships have most of the characteristics of a 'hierarchical' relationship: relatively unstructured tasks, long-term

---

66 N. Luhmann, The Coding of the Legal System, in: A. Febbrajo/ G. Teubner (eds.), State, Law, Economy as Autopoietic Systems, Milano 1991.

67 G. Spencer Brown, Laws of Form, New York 1972.

68 K. Imai/ H. Itami, op. cit. (note 17), 285.

69 J.C. Jarrillo, op. cit. (note 59). This idea of a non-hierarchical centralization seems to cause problems for lawyers in the franchising field who want to restrict franchising conceptually to hierarchical subordination. Cf. W. Bauder, op. cit. (note 7) and Ch. Joerges, op. cit. (notes 3 and 7). Experience from other network relations should give cause for thought.

> point of view, relatively unspecified contracts. These relationships have all the characteristics of 'investments', since there is always a certain 'asset specificity' to the know how of, say, dealing with a given supplier instead of a new one. And yet, the 'contracting parties' remain as independent organizations, with few or no points of contact along many of their dimensions[70].

In this way contractual networks make use of the interaction between mechanisms which increase variety and those which increase redundance. It is not a question of a precarious compromise between, or weighing up of, the two principles but a dialectical increase in both. This could be the secret of the their success, a success which economists, however, can only appreciate as a transaction costs advantage.

IV. Double Attribution in the Network

This dialectical relationship is the key to a legal definition of networks. Market networks are not "intermediate forms" between market and hierarchy, between exchange contracts and civil law partnerships. They do not make a precarious compromise between exchange and cooperation but are a combination of both. They do not transform contract into organization but are and remain contractual relations which, however, stimulate the development of hierarchical forms of organization.

In this way the simultaneous strengthening of contractual and organizational elements becomes possible. We are used to regarding the relations between contractual and company law elements as a zero sum game in which one side always wins at the expense of the other. In the transition from the spot-market transaction via the long-term contract, civil law sub-partnership ("Innengesellschaft"), collective ownership ("Gesamthand", "Außengesellschaft") to fully-fledged corporations, we regularly notice that collective elements become more important in the same measure as individual elements become less important[71]. Networks, however, cannot be included in this scale because individual and collective elements both increase in importance at the same time. As the example of franchising clearly shows, in networks the collective characteristics (systemic character, marketing unit, collective image, coordinated competition) as well as the individual characteristics (orientation of the franchisees toward their own profit-making, their individual responsibility) can, at one and the same time, be greatly

---

70 J.C. Jarrillo, op. cit. (note 59), 6.

71 Cf. e.g. the comments in W. Hadding, in: Soergel-Siebert, Kommentar zum BGB, Intro. to § 705, nos. 7 et seq., 17 et seq.

increased[72]. The "many-headed hydra" is an excellent metaphor for this constellation[73].

This simultaneous increase of contradictory principles results in a peculiar self-regulation which is based on a double orientation of action. From an economic point of view, all transactions have both the network's profit and at the same time the profit of the individual actor as objectives ("profit sharing"). This double orientation works as a constraint since every transaction has to pass the double test, and it works as an incentive since network advantages are connected to advantages for the individual[74]. From a juridical point of view, the simultaneous coexistence of individual objectives and of common objectives in one and the same institutional arrangement must be assumed. This is in clear contradiction to the widespread idea that interests either compete with one another (we then have an exchange relation) or they have the same end (we then have an association ("Gesellschaft"))[75]. From both an economic and a juridical point of view, the behaviour of the actors is simultaneously orientated, on a company law basis, towards the common objective and, on a contractual law basis, towards the individual objectives, without according any priority to the one or the other. In this respect it differs decisively from both the long-term contract and civil law partnership where priority is given to individual and common objectives respectively.

The same applies to the attribution of action. Any action within the network is attributed simultaneously to the network as a collective and to the individual actor. This double attribution distinguishes network from association on the one hand and from contract on the other in which actions are attributed either to the individual or to the collective. Even if the law is a long way from treating contractual relations as legal subjects, in economic practice, closely organized fran-

---

72 See M. Martinek, op. cit. (note 4), 121 et seq.

73 H. Wiedemann, Die Unternehmensgruppe im Privatrecht, Tübingen 1988, 10, describes the group of enterprises ("Konzern") as a "many-headed monster". Marketing systems can evoke similarly horrifying visions.

74 The economic point of franchising compared with other marketing nets belonging to firms (even those with their own incentive programmes) lies in the residual claim for the franchisee. For an especially clear, empirically-supported examination cf. S.W. Norton, op. cit. (note 25). Due to saved monitoring costs, the residual claim for franchisees is usually higher than comparable incentives in integrated firms. Cf. P.H. Rubin, The Theory of the Firm and the Structure of the Franchise Contract, 21 Journal of Law and Economics 223 (1978); J.A. Brickley/ F.H Dark, The Choice of Organizational Form: The Case of Franchising, 18 Journal of Financial Economics 413 et seq. (1987).
The double orientation of profit sharing which has the effect of a constraint and an incentive, is analysed there in economic language as "principal-agent incentives" and "information incentives" (at 202 et seq.). Cf. also B. Klein/ L.F. Saft, The Law and Economics of Franchise Tying Contracts, 28 Journal of Law and Economics 345 (1985); G.F. Mathewson/ R.A. Winter, The Economics of Franchise Contracts, 28 Journal of Law and Economics 503 (1985); A.W. Dnes, The Business Function of Franchising, 1 Business Studies 33 (1988) and in this volume.

75 Cf. W. Hadding, in: Soergel-Siebert, Kommentar zum BGB, Intro to § 705, no. 8; § 705, no. 44 et seq.; K. Larenz, Schuldrecht II, Munich 1981, § 60 I b; F. Kessler, in: J .v.Staudinger, Kommentar zum BGB, § 705, nos. 6 et seq.

chising systems are "observed" as a paradoxical unitas multiplex, i.e. as an organizational unit and simultaneously as a plurality of actors[76]. This economic practice makes possible that which seems contradictory in the law; namely the simultaneous attribution of one and the same action to both the organization and the individual unit.

This double attribution which is made in "practice", and which combines organizational self-regulation with external regulation by the market, ought to become the legal model for a notion of liability which does justice to the peculiarities of the network. Indirect regulation via liability law can only "hit" the self-regulatory nerve of the network if it can "irritate" the double orientation of network behaviour[77]. It is only the simultaneous influencing of cost-benefit calculations of "net" and "knot" that gives liability law certain chances to control the behaviour of the network. A type of liability "beyond" the "individualistic" joint obligation ("Gesamtschuld") and the "collectivistic" collective obligation ("Gesamthandschuld") should be established — a type of liability which would allow the decen-tralized liability of the whole network[78]

As an interim result of this discussion on network structures we can note that franchise systems cannot be one-sidedly qualified as contract or as organization without neglecting important structural features. Merely to say that a certain intensity of coordination marks the transition from contractual to company law franchising is of little assistance. No better is the idea of a sliding scale which allows collective elements to increase at the cost of individual ones. However, the idea of a dialectical accumulation of contractual and organizational elements, of individual and collective behaviour orientation, and of individual and common objectives seems promising. And it suggests a model of "network liability" which is based on simultaneous collective and individual liability.

V. Tort Liability

We can now turn to the question of which among the different fields of liability law in Germany — the law of torts, the law of contract or the law of associations — can best guarantee an adequate external liability of franchising systems. At

---

76 See M. Martinek, op. cit. (note 4), 121, who is very informative on this subject.

77 Cf. N. Luhmann, Die Wirtschaft der Gesellschaft, Frankfurt/M 1988, 345 et seq. on the "indirect" control of systems. On the problems of network control in groups of enterprises, cf. G. Teubner, op. cit. (note 39); G. Teubner, Die vielköpfige Hydra: Netzwerke als kollektive Akteure, in: W. Krohn/ G. Küppers (eds.), Emergenz und Selbstorganisation, Frankfurt/M 1991.

78 This liability model is closest to the construction of the collective obligation ("Gesamthandschuld") with simultaneous liability of the partners. However, problems are caused on the one hand by "overshooting", and on the other by the relation of both obligations to each other. Cf. W. Flume, Allgemeiner Teil des bürgerlichen Rechts. Vol. 1.1 (Die Personengesellschaft), Berlin 1977, 282 et seq. More precise remarks on this are to be found infra (V. et seq.)

the same time we shall ask which changes in the existing German liability law appear necessary in order to take account of their network character.

The law of torts is, of course, a particularly flexible instrument. The simplest starting point is that of § 831 BGB[79]. With these comments on the structural features of "networks" in mind, we can readdress the problems regarding the "oscillation" in the frachisees' position which are caused by the application of § 831 BGB. It seems that the emphasis on the franchisees' interest in their own objectives, on their economic independence and on their professionalism is no longer a sufficient reason for questioning their status as "vicarious agents" ("Verrichtungsgehilfen") of the franchisor. For, in keeping with the hybrid nature of the franchising net, any increased autonomy of the franchisees does not necessarily lead to a change in legal status. On the contrary, they remain integrated in the organization — in spite of, or perhaps because of, their high degree of autonomy. The principles of the Federal High Court, which applies § 831 BGB to commercial agents ("Handelsvertreter") in those clear cases where they are dependent on instructions[80], should therefore be extended to include franchise nets. Their independence, on the other hand, is taken into account under the law of torts where they have their own role-specific liability running parallel to the liability of the principal ("Geschäftsherrnhaftung"). Unlike the case of employees, who are completely integrated in the hierarchy of a firm, it makes sense, where franchisees are concerned, to talk of their independent liability[81]. Where, as above, the franchisee is involved in unfair competition, which nevertheless can be seen to be "caused" by the system, then we would have to reckon with the liabilities of both franchisee and franchisor.

But how can we solve the problems that extend beyond the scope of § 831 BGB and which concern the inclusion of the franchisor, as the head of the organization, within the ambit of heightened standards of negligence ("Schutzpflichten")? These problems are of a particularly pressing nature in franchising organizations because of the close interconnection of behaviour? For some constellations, product liability under German tort law and also under the terms of the new Product Liability Act ("Produkthaftungsgesetz" according to the European Directive on product liability) can serve as a flexible and effective instrument. Product liability burdens the franchisor directly with increased duties, i. e. the typical duties of the producer, without there being any need for complicated "piercing the veil" constructions under the law of contracts or associations[82]. In this case it is irrelevant whether or not the franchise relationship is publicly dis-

---

79 See note 12.

80 BGH Neue Juristische Wochenschrift 1980, 941; G. Schröder, op. cit. (note 50) § 86.

81 G. Brüggemeier 1986, op. cit. (note 9), 887, correctly distinguishes between employees who are integrated in the hierarchy on the one hand and "professionals" on the other. According to him, only in the latter case does independent tortious liability running parallel to that of the principal make sense.

82 E. Körner, op. cit. (note 7), 3056; Ch. Joerges, op. cit. (note 7).

closed. It is purely and simply the producer's "duty of care" ("Verkehrspflicht") which is decisive.[83]

Even in those forms of franchising in which the franchisee rather than the franchisor produces the product (hamburgers!), the franchisor is directly liable according to the principles of product liability, inasmuch as the production process is subject to his instructions. Unlike producers' licences, the franchisor's influence is so far-reaching that he would have to be included in any extension of product liability to include "further persons" who are deemed to be taking part in the production process under the three relevant heads of supervision, contributory causation and identification[84]. Under the new Product Liability Act, the same result is reached by means of the extremely broad definition of the producer to be found in § 4 which would include any franchisor "who, by putting his ... distinguishing feature on the product presents himself as its producer".[85]

The franchisee, however, according to the case law principles for various distribution agreements is burdened with duties relating to production, examination or information, depending on how concretely he is integrated into the production and distribution process.[86]

On the whole, the instrument of product liability shows many features which are "network adequate". It imposes increased duties of care on the head of the organization, and makes it liable for the organization as a whole as far as this is subject to its supervision. At the same time it is decentralized insofar as "net" and "knot" are burdened with complementary duties of care according to the internal division of labour. The sharing of tortious duties of care means that product liability reflects exactly the internal division of labour within the network. In this way it would seem that product liability "hits" the self-regulation of the network with sufficient precision. Finally, product liability is neutral in regard to legal form. It imposes duties of care on the actors according to their factual competence, independently of whether franchising is clothed with the laws of contract, company or group enterprise.

However, this must not mislead us into thinking that product liability does more than cover one aspect of the liability problem. There are plenty of cases, where there is no compensation to be had from the franchising organization, in which the shortcomings of the law of torts make themselves very noticeable. Cases like these have led the EC-Commission to ensure in their decisions on exemptions an

---

83 Ch. Joerges, op. cit. (note 7), 210.

84 E. Körner, op. cit. (note 7); cf. also A. Lüderitz, Produzieren in und unter fremden Namen — Zurechnungskriterien in der deutschen und US-amerikanischen Produkthaftpflicht, in: Festschrift für Pleyer (1986), 553.

85 H. Thomas, in: O. Palandt, Kommentar zum BGB, (Munich 1990) ProdHaftG § 4, no. 3; Ch. Joerges, op. cit. (note 7), 210.

86 H.-J. Mertens, in: Münchener Kommentar zum BGB, § 823, nos. 289 et seq.; A. Zeuner, in: Soergel-Siebert, Kommentar zum BGB, § 823, no. 15; G. Brüggemeier, op. cit. (note 9), 1986, 361 et seq.; Ch. Joerges, op. cit. (note 7), 210.

adequate measure of consumer protection, e. g. by means of a compulsory insurance scheme for franchisees or of a sufficient guarantee in the franchise-system[87]. Today, it is a condition of the new group exemption regulation that obligations under guarantee terms be fulfilled everywhere in the system — a remarkable innovation which represents a kind of "network liability"![88]

Since product liability is limited to industrially produced goods, it does not cover the whole field of service franchising[89]. Neither does it address secondary duties which do not refer to products. Apart from the exception under §§ 14 III, 13 III UWG[90] ("Gesetz gegen den unlauteren Wettbewerb" or the Law Against Unfair Competition) which establishes, to a limited extent, the liability of the agent in cases of unfair competition[91], there remains only liability in tort for franchise-systems which, since it is in the form of individual liability of the system's members, does not deal adequately with their highly-organized nature.

This might be remedied with the further development of the case law concerning "duties of care" ("Verkehrspflichten")[92]. The basic idea is that setting up a dangerous set of transactions ("Verkehr") should attract special duties aimed at avoiding risks. This idea would also apply to the setting up of a distribution organization like franchising — over and above the scope of application which has

---

87 Cf. EC-Commission, OJ L 8/1978, 49, paras. 17, 62 — Yves Rocher.

88 Art. 4 b of Commission Regulation no. 4087/88 of 30 November 1988 on the application of art. 85 para. 3 of the Treaty for groups of franchise agreements, OJ L 359/1988, 46-52, Wirtschaft und Wettbewerb 1989, 306 et seq. On the same subject D. v.Schultz-Schäfer, Franchising im Lichte der neuen EG-Gruppenfreistellungsverordnung, Gewerblicher Rechtsschutz und Urheberrecht. Internationaler Teil 1989, 515 et seq.

89 Cf. J. Schmidt-Salzer, Kommentar zur EG-Richtlinie ProdHaftG, Art. 2, no. 9.

90 § 13 UWG: "(1) By providing written notice, and for significant cause, each participant may terminate, effective immediately, the agreements and resolutions of the types described in paras. 2 to 8. Significant cause is deemed to exist in particular if the freedom of economic action of the terminating party is unfairly restricted or impaired in relation to the other parties by unjustified unequal treatment. The ineffectiveness of the termination due to a lack of significant cause may only be asserted by instituting legal proceedings within four weeks after receipt of the notice of termination.
(2) As long as the Cartel Authority has not granted permission for agreements and resolutions of the types described in paras. 4, 5 (2) and (3), 6 (2), 7 and 8, each participant may withdraw for significant cause. Sub-paragraph 1, second and third sentence, apply correspondingly. If an application for permission has already been made to the Cartel Authority prior to the withdrawal, the declaration of withdrawal should be communicated to the Cartel Authority."
§ 14 UWG: "(1) Collateral securities provided in connection with agreements and resolutions of the types described in paras. 2 to 8 may only be realized to the extent the cartel authority has granted permission therefore upon aplication by the cartel. Permisssion shall be refused if such measures unfairly restrict the freedom of economic action of the party concerned or impair such party in relation to the other participants by unjustified and unequal treatment.
(2) The permission may be subject to time limitations, restrictions, conditions and requirements." (Translation from: Riesenkampff/ Groß, Gesetz gegen Wettbewerbsbeschränkungen, Köln 1977, 47 et seq.

91 Liability of the agent ("Beauftragtenhaftung") only applies under certain restrictions: BGH Neue Juristische Wochenschrift 1980, 941; J. Schulze zur Wiesche, Gewerblicher Rechtsschutz und Urheberrecht 1980, 117.

92 Cf. G. Brüggemeier 1986, op. cit. (note 9), 313 et seq. who is most persuasive on this subject.

until now been accepted[93]. The distribution organization of goods and particularly of services would then be a set of transactions in this sense and the franchisor, through heightened duties of care and with no possibilities of exculpation, would be directly liable under the law of torts for its defective functioning[94]. In this way, there might be eliminated any arbitrary differences in the treatment of product liability and services franchising. Perhaps one should even go so far as to impose tortious duties of care on the establishing of a contractual network as such, and not take any account of the technical questions of "distribution".

Of course this is an extremely delicate area in German private law. There is the danger of an overlapping of the "organizational duties" under tort law ("Verkehrspflichten") with those under the law of associations ("Organisationspflichten")[95]. There is also the problem of the unsolved territorial claims of "contorts": How can these "distribution duties" in the sense of tortious duties of care be distinguished from quasi-contractual protective duties of good faith ("Schutzpflichten")[96]? In each of these fields — contracts, torts, associations — German case law has developed "organizational duties" which differ in their legal premises and legal consequences. In the case of franchising these case law developments coincide and a clear doctrinal delineation is not in sight.

An in-depth examination of this is not possible here, but I would like to base the rest of my considerations on the following distinction. Encouraged by the differentiation between production costs and transaction costs, I would like to differentiate between the way liability law deals with production and transaction risks. Tortious duties of care should concentrate on compensating production risks in the broadest sense, i. e. the technical risks of organization, the operational risks of design, production and distribution activities ("Verkehr"), independently of the legal form chosen. Transaction risks, on the other hand, i. e. those risks which stem from the legal arrangement chosen — contract, partnership, corpo-

93 Cf. e.g. A. Zeuner, in: Soergel-Siebert, Kommentar zum BGB, § 823, no. 182.

94 Certain formulations of OLG Karlsruhe Neue Zeitschrift für Verkehrsrecht 1989, 435, tend in this direction: If somebody establishes a marketing network with certain inherent risks, he is burdened with certain duties of organization and supervision. Similarly W.-H. Roth, op. cit. (note 36).
For a similar tortious responsibility for risks stemming from the establishment of a set of transactions i.e. the marketing of capital shares, see H.-J. Mertens, in: Münchener Kommentar zum BGB, § 826 no. 196; Ch. v.Bar, Vertrauenshaftung ohne Vertrauen, Zeitschrift für Unternehmens- und Gesellschaftsrecht 12 (1983), 476 et seq., 504 et seq.; H.-D. Assmann, Prospekthaftung, Köln 1985, 252 et seq., 273 et seq.; id., Gläubigerschutz im faktischen GmbH-Konzern durch richterliche Rechtsfortbildung, Juristenzeitung 1986, 320 et seq.

95 See H. Heinrichs, in: O. Palandt, Kommentar zum BGB, § 31, no. 2; A. Zeuner, in: Soergel-Siebert, Kommentar zum BGB, § 823, no. 184.

96 E.g. H.-J. Mertens, Deliktsrecht und Sonderprivatrecht — Zur Rechtsfortbildung des deliktischen Schutzes von Vermögensinteressen, 178 Archiv für die civilistische Praxis 227 (1978), 227 et seq.; Ch. v.Bar, Verkehrspflichten: Richterliche Gefahrsteuerungsgebote im deutschen Deliktsrecht, Köln 1980, 220 et seq., 312 et seq.; K. Hopt, Nichtvertragliche Haftung außerhalb von Schadens- und Bereicherungsrecht, Archiv für die civilistische Praxis 183 (1983), 608 et seq.; G. Brüggemeier 1986, op. cit. (note 9), 70 et seq.

ration, group enterprise — cannot be treated independently from the legal rules governing the specific arrangement. On the contrary, transaction risks should be treated in the context of the general legal attribution of risks within the appropriate area of law under consideration. "Tort imperialism" thus stops just short of the point where risks specific to the legal form — e. g. the limitation of liability through incorporation — are concerned. At this point we must introduce a type of liability which is specific to the legal form being considered, e. g. in group enterprises the group-specific liability, piercing the corporate veil and the principles established in the "Autokran" case. For liability in franchising this would mean that the "technical" risks of the distribution system (transport, storage, information) would be internalized by the tortious duties of care (production risks), while risks stemming from the choice of the institutional arrangement itself (transaction risks) would be solved by transaction-specific liability rules. These transaction risks would include the contractual shifting of liability from the franchisor to the franchisees, and limiting liability of the whole franchise net by choosing the group-enterprise form or that of a contractual nexus which changes liability by agreement. Since all these risks are specific to the legal form itself, their internalization should be a matter of contractual liability, corporate liability or group liability. Where production risks and transaction risks are brought about simultaneously, then the rules of tort liability law and those governing the specific transaction would have to be applied cumulatively. Such a cumulative application of liability rules from different fields is generally accepted in German law[97], and would compensate here for the factual accumulation of risks.

VI. Corporate Liability

Contract or organization? Since franchise systems, in spite of their formally contractual nature, are in fact highly centralized and hierarchical organizations, a functional view, an "economic viewpoint", would treat franchise-systems according to the law of associations. As was observed above, the Reichsgericht and some older academic opinions applied partnership law provisions to distribution systems which were similar to partnerships. And more recently, after a period of suppression, there has been a plea, especially from Martinek, for an application of partnership law which is more sensitive to differences in the level of coordination. So where does the structural analysis of franchising-systems as "networks" lead us now?

97 For example W. Hadding, in: Soergel-Siebert, Kommentar zum BGB, Appendix to § 328, no. 25.

Of prime importance for a liability based on the law of associations is the legal principle of § 31 BGB[98]. Under this principle, the franchising system itself is seen as an association which is legally responsible for the behaviour of its "organs", i. e. the behaviour of the franchisor and the franchisees. Various doctrinal constructions lead to this result. If one agrees with Martinek, and classifies franchising with its tightly-organized structure as a coordinate group enterprise ("Gleichordnungskonzerne")[99], then the liability of those members could be considered in analogy to § 31 BGB. If one accepts further Martinek's construction of "coalition franchising" as a bundle of partnerships[100], and his construction of "confederation franchising" as one large partnership[101], then § 31 BGB comes into focus once again. Of course, there are still considerable doctrinal objections to be overcome. Firstly, there is the analogous application of § 31 to civil law partnerships, which is generally accepted today by academic opinion in Germany[102]. Not to mention the application of § 31 BGB to sub-partnerships ("Innengesellschaft") and to partnerships without joint capital ("Gesamthandsvermögen") which is much more problematic[103]. Of course the tight internal organization of franchising systems suggests that joint capital and corporate structures are irrelevant for liability purposes. The actual collective behaviour within the system is decisive, in the face of which a legal attribution of actions to individuals appears difficult and artificial.

However, quite apart from a possible classification of franchising as a partnership, § 31 BGB still springs to mind. On the one hand, we must see whether the famous "organizational duties" of German case law can be extended to cover contractually organized distribution systems[104]. If so, then can we justify the different treatment of the franchisor firm, depending on whether it is organized under company law or whether it is a sole-trader[105]. On the other hand, the question must be examined of whether the constant extension of the liability of associations under § 31 BGB to cover unincorporated associations, business partnerships, civil law partnerships, and even special assets which have become separate entities, such as inheritances or bankrupts' estates, can stop short of orga-

98 In a case of an authorized dealers' system, W.-H. Roth, op. cit. (note 36) considers an analogy to the associational liability of § 31 BGB. He fears, however, that the associational foundation of § 31 BGB would get lost.

99 M. Martinek, op. cit. (note 4), 648.

100 M. Martinek, op. cit. (note 4), 389 et seq.

101 M. Martinek, op. cit. (note 4), 410 et seq.

102 Cf. P. Ulmer, in: Münchener Kommentar BGB, § 705, no. 190, with further sources.

103 First and foremost H.-D. Assmann, Zur Haftung von Konsortien für das rechtsgeschäftliche Handeln ihrer Vertreter, Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht 152 (1988), 371 et seq., 379, who pleads the case for a dispensing with the joint capital requirement ("Gesamthandsvermögen") in the application of § 31 BGB to bank consortia.

104 Similar arguments can be found in OLG Karlsruhe, Neue Zeitschrift für Verkehrsrecht 1989, 434, 435, and W.-H. Roth, op. cit. (note 36).

105 D. Reuter, in: Münchener Kommentar zum BGB, § 31, no. 13; H. Heinrichs, in: O. Palandt, Kommentar zum BGB, § 31, no. 2.

nized nexus of contract ("Vertragsverbindungen")[106]. This question would be particularly appropriate if distribution systems are classified not as civil law partnerships, but rather as "mixed contracts" (exchange contracts with strong co-operative elements).

Group enterprise law must not be forgotten. An analogy is often drawn between distribution systems and group enterprises — and with good reason. In both cases we have a decentralized organization with quasi-autonomous subdivisions and a coordinating central office. In both cases we face the paradoxes of the unitas multiplex. And in both cases we find the interpenetration of market and organization. The application of group law depends on how to interpret the term "controlling influence" in § 17 German Aktiengesetz[107]. Does this also cover a contractual dependency[108]? If one agrees with Martinek and admits — at least for the extremely centralized forms of franchising — the existence of the group enterprise characteristic[109], then the application of liability according to the law of group enterprises becomes inevitable. For constellations of "qualified" franchise groups this would mean a general liability of the franchisor for all the franchisees' debts under the principles of the "Autokran" case[110], and in less extreme examples, a selective liability under the principles of direct liability of the group enterprise[111].

But just how network-adequate is liability under the law of associations, especially under § 31 BGB? The "model" form of § 31 BGB is an integrated organization with the following elements: common objective, unity of collective action, legal personality, and thus also a uniform responsibility for the actions of all its "organs" (Organe)[112]. But does this model not fail to take account of sig-

---

106 W.-H. Roth, op. cit. (note 36) also asks this question in regard to authorized dealers. In general for the expansion of § 31 BGB on non-corporate forms D. Reuter, in: Münchener Kommentar zum BGB, § 31, no. 9 et seq.; H. Heinrichs, in: O. Palandt, Kommentar zum BGB, § 31, no. 2; H. Schultze von Lasaulx, in: Soergel-Siebert, Kommentar zum BGB, § 31, no. 12.

107 § 17 Aktiengesetz: "(1) Controlled enterprises are legally independent enterprises over which another enterprise (the controlling enterprise) can exercise, directly or indirectly, a controlling influence.
(2) In the case of a majority-owned enterprise, it is presumed that it is dependent on the enterprise which forms that majority".

108 Case law and academic opinion demand a company law integration: LG Düsseldorf, Zeitschrift für Wirtschaftsrecht 1981, 601; H. Würdinger, in: Großkommentar AktG, § 17, no. 3; R. Scholz/ V. Emmerich, GmbHG, (1986) app., no. 45; A. Sura, Fremdeinfluß und Abhängigkeit im Aktiengesetz, Konstanz 1978, 54 et seq.; K. Schmidt: Unternehmen und Abhängigkeit, Zeitschrift für Unternehmens- und Gesellschaftsrecht 1980, 227 et seq., 284 et seq. A mere economic dependence is enough for: v. Godin/ H. Wilhelmi, AktG § 17, no. 2; J. Dierdorf, Herrschaft und Abhängigkeit einer Aktiengesellschaft auf schuldvertraglicher und tatsächlicher Grundlage, Munich 1978.

109 M. Martinek, op. cit. (note 4), 644 et seq.; cf. also B. Nagel, Der faktische Just-in-Time-Konzern — Unternehmensübergreifende Rationalisierungskonzepte und Konzernrecht am Beispiel der Automobilindustrie, Der Betrieb 1989, 1505, who assumes the existence of an actual group enterprise for the parallel constellation of suppliers' nets which are organized according to the "just in time" concept.

110 BGHZ 95, 330 — "Autokran"; BGH 1989 Zeitschrift für Wirtschaftsrecht 440 — "Tiefbau".

111 See G. Teubner, op. cit. (note 39), 261 et seq.

112 Cf. D. Reuter, in: Münchener Kommentar zum BGB, § 31, nos. 7 et seq.

nificant features of the "network" mentioned above: decentralization, autonomy of the subsidiary units, double attribution of action? Of course, § 31 BGB solves the problems which a purely tortious regime of liability poses for franchising. The franchisor as the head of the organization is subject to heightened duties of care, even to all the contractual duties. He is also liable for any mistakes made by "organs" of the franchising organization. The possibility of risk-shifting, through the principle of privity of contract, or through special agreements made between the franchisor and franchisee which impose burdens on third parties, is compensated for by liability. But if the liability instrument of § 31 BGB is used for decentralized networks it will "overshoot" the mark. Since all behaviour is attributed to the central office, it does not do justice to the real, decentralized coordination of behaviour and the actual division of competences. Its regulatory effect is not precise enough since it aims, in a general way, at the whole association, and not simultaneously at the concrete centre of action.

A network perspective makes us aware of the "category mistakes" involved in applying the law of liability for associations in such circumstances. Franchising nets are not simply organizations clothed in contractual forms which can be dealt with by means of "piercing the contractual veil". While, as "market networks" in the sense presented above, they repeat within their limits the distinction between market and organization, they do so without losing their fundamentally contractual features. They are still contracts, and their peculiarity exists in the fact that they build on their contractual features in order to constitute a formal organization. Their liability in law must also build on this double structure. The system's members are indeed "organs" of the franchising organization; they remain however, at the same time, "actors" as autonomous units of action.

Similar statements can be made about the liability law of group enterprises. If the instruments of the "Autokran" case are applied by analogy to cases of "qualified" franchising, it would involve a rather insensitive treatment of situations where the attribution of responsibility is in fact rather difficult

VII. Contractual Liability

For these reasons it is the law of contracts and not that of associations that is the correct systematic place to deal with the peculiarities, risks and dangers of "market networks" such as franchising. It makes sense, then, to deal with the organizational aspects of contracts not with company law — the turning of contracts into associations — but rather with an area of law which, while still only in its embryonic stages, we might provisionally call "controrgs"[113].

113 I owe this conceptual innovation to Sean Smith. For the dogmatic development and the contemporary problems of "controrgs" see E. Schanze, Symbitic Contracts, in this volume at 67 et seq.

Its deficits cannot be overlooked. In German law there are only three dogmatic approaches which take into account, if only to a minimal degree, the organizational elements in contractual law — long-term contracts, "mixed arrangements" and nexus of contracts. (1) Long-term contracts are, to a certain extent, the legal expression of formal organizations on a contractual basis[114]. However, their emphasis on the time dimension, i.e. the long-term nature of the obligation, the adaptation to changed circumstances, termination rights at any time where there are important reasons, can be seen as rather one-sided. Their further development to a fully-fledged doctrine of relational contracts would require that their organizational character is stressed, not only in the dimension of time, but more particularly in their substantive and social dimensions[115]. (2) Mixed arrangements, or, to use an older term, "contractual relations similar to partnerships" ("gesellschaftsähnliche Verhältnisse"), are contracts in which the pure exchange relation is elaborated with cooperative elements. (3) Finally, in the definition of nexus of contracts ("Vertragsverbindungen") there can be found a quite different, but still weakly-formed consideration of the organizational nature of contractual systems. The basic problem with nexus of contracts is in the artificial splitting up of a uniform organization into individual contracts which are supposed to be separate from one another in law[116]. Attempts have been made, using the notion of implied terms and by setting up duties of good faith with respect to organisational goals, to transfer aspects of the general organization to the individual contracts. Should it be the case that hybrid contractual organizations are becoming increasingly more important economically, then the attempts made up till now in those three areas — long-term contracts, mixed arrangements and nexus of contracts — should be systematically extended to form a law of contractual organization or "controrgs". Such a hybrid law would differ from the law of associations in three aspects. It would recognize not only the common objective, but also the individual objectives of the members. It would determine that the system's members are not only "organs" of the organization but also autonomous "actors", and that the attribution of behaviour and responsibility takes place both centrally and decentrally. In short: the law of relational contracts should do justice to the network character of the contractual organizations.

---

114 On the doctrine of long-term contracts see J. Gernhuber, op. cit. (note 11), 377 et seq. with further sources.

115 On relational contracts cf. I. Macneil, The New Social Contract: An Inquiry into Modern Contractual Relations, New Haven 1980; I. Macneil, Relational Contract: What We Do and Do Not Know, 1985 Wisconsin Law Review 483; J. Köndgen, Selbstbindung ohne Vertrag. Zur Haftung aus geschäftsbezogenem Handeln, Tübingen 1981; W. Schmid, Zur sozialen Wirklichkeit des Vertrages, Berlin 1983; T. Daintith, The Design and Performance of Long-Term Contracts, in: T. Daintith/ G. Teubner (eds.), Contract and Organization, Berlin 1986, 164; Ch. Joerges, op. cit. (note 7); F. Nicklisch (ed.), Der komplexe Langzeitvertrag, Heidelberg 1987.

116 J. Gernhuber, op. cit. (note 11), 708 et seq. For an organizational law interpretation, cf. G. Teubner, in: Alternativkommentar BGB, § 242, no. 92.

In some ways, liability law is a test case for these attempts. The liability of networks, which means, at the same time, a decentralized liability, can probably not be attained with the means which have so far been at our disposal. Up to now, the bravest attempt to do justice to the network character of certain contractual arrangements, was that of Möschel with his proposal for a "net contract" in the field of bank transfers[117]. This is an area which can be developed further.

This matter can be related to German case law developments in the area of contracts to the benefit of a third party ("Vertrag mit Schutzwirkung für Dritte"). This institution has been expanded in order to take into account the external effects of bilateral contracts for third parties. Under certain circumstances the partners to the contract can become contractually liable to third parties[118]. In the case of networks, and in contrast to other contracts to the benefit of third parties, the typical third-party risk comes not from the performance but from the organizational arrangement itself. In both bank transfer nets as well as franchising nets, a service is provided which involves the activities of many parties. However, at the same time it is so decentralized and involves such a division of labour, that only part of the system (the customer's bank or franchisee) has contractual relations with the customer. This justifies the ascription of responsibility for third party effects to the contracting members of the coordination system (relations between banks, and between franchisor and franchisees).

The governing principle of responsibility must be this. Where the internal division of labour involves all the members of the system in the performance of the contract, then all such members and not only those who happen to have contractual relations with third parties, should come within the ambit of the heightened duties of care.

Particularly relevant are those above-mentioned constellations in which a franchising system causes injury or damage to consumers because of defective services, and compensation cannot be obtained at all or only insufficiently from the franchisee who performed the contractual obligation. The franchisor, as the organizational centre, is contractually liable if the "defect" lies "in the system", perhaps because of a defective instruction from the franchisor or because of a defective handbook which is used for the whole system. Other franchisees are contractually liable as well if a decision made by the franchise committee had intro-

---

117 W. Möschel, Dogmatische Strukturen des bargeldlosen Zahlungsverkehrs, Archiv für civilistische Praxis 186 (1986), 211 et seq., 217 et seq. A skeptical view is provided by J. Köndgen, Bankhaftung — Strukturen und Tendenzen, in: id., Neue Entwicklungen im Bankhaftungsgesetz, Köln 1987, 133, 144 et seq.; I. Koller, Grundstrukturen des Bankhaftungsgesetzes unter besonderer Berücksichtigung des Zahlungsverkehrs, in: J. Köndgen, Neue Entwicklungen im Bankhaftungsgesetz, Köln 1987, 21, 25; U. Hüffer, Die Haftung gegenüber dem ersten Auftraggeber im mehrgliedrigen Zahlungsverkehr, Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht 151 (1987), 93 et seq., 106 et seq.; J. Schröter, Bankenhaftung im mehrgliedrigen Zahlungsverkehr, Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht 151)1987), 118 et seq.

118 J. Gernhuber, op. cit. (note 11), 529.

duced the defect into the system. The attribution of liability to the franchisor is necessary where, due to the nature of the system, part of the customer services are provided centrally (hotel franchising, franchising of transport of goods). As has been discussed above, a tortious allocation of liability under § 831 BGB fails, due to the well-known problems of § 831 BGB; product liability cannot be considered because it can only be applied to industrially produced goods and not services; liability based on the law of associations can also be excluded because of the above-mentioned problems. In a distribution system which is not networked and which is based on the market autonomy of the participants, the isolation of defects in this way can be tolerated; but not in a highly-organized distribution system based on close cooperation and division of labour. The reason for the inclusion of the head of the system or (in the case of a decision of the committee) of the other members of the system in the contractual liability is to be found here: in the closely-interwoven net of individual contributions. Accordingly, other participants in the system must be included within the ambit of the duties provided for in the contract. Whether the traditional construction of the contract with a protective character for third parties or the generalized idea of a "net contract" is used is irrelevant to the result obtained — the liability of other members of the system in proportion to their internal responsibility.

VIII. Result

The result of this discussion of franchising liability under German law is as follows. On the one hand, the growth of tightly-organized franchising systems is a reason for questioning their doctrinal treatment in discrete contractual categories which suppresses their organizational character. On the other hand, the analysis of their structure as "networks" makes it doubtful as to whether the law of associations can be of meaningful assistance. Their nature as decentrally-organized, but at the same time closely-coordinated networks, means that it seems more appropriate to employ the more flexible instruments offered by the law of torts and the law of contractual organizations. A well-considered consolidation of tortious duties of care taken together with the protectionary and secondary duties available under contract can better achieve a network liability which is both decentralized and comprehensive. The technical risks of these distribution organizations can be met with a further development of product liability and tortious duties of care. The typical transaction risks on the other hand should be dealt with in a way which is specific to their legal form, i.e. with a consolidation of the "hybrid" law of contractual organization and its liability law effect on third parties.