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Franchising - Japan

Court Rules on Trademark Dispute between Franchisors

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On April 25 2008 the Tokyo District Court rendered judgment in a case concerning a trademark dispute between a master franchisor and a regional sub-franchisor. The sub-franchisor sought damages from the master franchisor due to the latter's alleged use of logos that infringed the sub-franchisor's trademark rights.

Facts

The case was unusual for the following reasons:

The master franchisor had not registered any trademark rights in its name, although such rights are usually essential for engaging in and expanding a franchise business.

For most of the period in question, no written licence agreement existed between the parties regarding the use of the trademarks; and

The sub-franchisor, which was a franchisee of the master franchisor and was granted franchise rights based on a sub-franchising agreement, commenced legal action against the master franchisor seeking damages for trademark infringement.

The master franchisor was one of the largest takeaway meal preparation franchisors in Japan. The sub-franchisor was a regional sub-franchisor.

The sub-franchisor came to own the registered trademark rights as a result of a complex series of events. The initial applications for the rights were submitted by a third-party company, which was incorporated by the founder of the franchise chain. The third-party company applied for one of the trademarks (and thereafter acquired all of the rights) and was the original master franchisor of the chain until the master franchisor (ie, the defendant) was incorporated. However, the third-party company retained the trademark rights. The sub-franchisor later acquired all of the third-party company's shares and rights, including the trademark rights at issue.

Starting from the assumption that the sub-franchisor was the owner of the rights, the main issues to consider were (i) whether an agreement existed whereby the sub-franchisor permitted the master franchisor to use the trademarks, and (ii) if such agreement existed, whether it was terminated.⁽¹⁾

Decision

The court found that an implicit agreement existed that allowed the master franchisor to use the trademarks. It therefore rejected the sub-franchisor's claim of trademark infringement.

This finding was based mainly on the transfer of master franchisor status. The court found that the founder of the franchise business originally established the third-party company as the original master franchisor. However, in light of the development of the franchise, the third-party company's status was transferred to the new master franchisor - which was run by the same founder at that time - notwithstanding that there was no express agreement to transfer such status. At or before this point, the third-party company and the subsequent master franchisor were to be regarded as having entered into an implicit contract regarding the use of the trademarks at issue. The court concluded that the contents of this implicit agreement included the granting of an exclusive licence for use the trademark rights at no cost.

However, the sub-franchisor claimed that even if an implicit agreement existed, such agreement was the result of a special relationship between the master franchisor and the third-party company, which shared a common representative director (ie, the founder of the franchise business). Moreover, the founder and members of his family owned almost all of the shares of both companies. This close relationship between the two companies was the basis for the existence of any such implicit agreement. Nevertheless, the sub-franchisor claimed that the implicit agreement was terminated at the

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time that the founder of the third-party company transferred his interest in its shares to another party. The court disagreed, holding that the implicit agreement survived.

Reaction

Neither party appealed the judgment, but on May 15 2008 the sub-franchisor issued a press release giving three months' advance notice of termination of the implicit licence agreement. The master franchisor responded with a press release stating that the judgment affirmed the existence of an exclusive licence which would continue for the duration of the franchise business. Thus, the court did not fully resolve the dispute between the companies.

Comment

This case attracted significant attention because it involved the largest takeaway franchise chain dispute between a master franchisor and a sub-franchisor. Based on a variety of factors, the court found that an implicit agreement granted an exclusive license to use certain trademarks; it concluded that the master franchisor's exclusive right to use the trademarks would continue in future. The lesson is clear: the master franchisor should have taken more proactive measures to protect its trademark rights. For example, it could have acquired the rights from the third-party company before they were transferred.

However, the duration of such an implicit agreement remains unclear. Moreover, it is uncertain whether such an agreement can continue if the parties maintain an adversarial relationship, which is the fundamental reason that the judgment did not fully resolve the dispute in question. Instead, a new point of contention arose between the parties regarding the termination of the agreement, meaning that a new lawsuit or some other means of dispute resolution may be necessary. The recent expiry of the sub-franchisor's three-month notice period may reignite the dispute.

As master franchisors and regional sub-franchisors are frequently involved in disputes, master franchisors should ensure that their rights are clearly embodied in express agreements that bind not only the parties, but also their successors.

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Endnotes

(1) The court also considered a number of other questions which were related to the trademark issue.

Comment or question for author

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