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

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I. Piercing the "Contractual Veil"?

Franchising systems are hybrid structures between "market and hierarchy". 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. In addition to these formal problems, the external liability of franchise systems, which in German law until now has hardly been analyzed, is not easy to deal with in legal terms since they facilitate 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. On the other hand, they take on the form of harmful individual contracts between a number of sales outlets (franchises) and one central sales headquarters (franchisor). This breaking-down of the organization into a number of individual

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1 For helpful criticism I would like to thank Anamari Abidi Abidi, Andrés Schmiedt and Sean Smith.
2 The title of Oliver P. Williamson's book, Markets and Hierarchies, New York 1979, has become the term for comparable studies dealing with the area between market and organization.
3 Cf. on this subject the national reports by T. Dallin, H. Mauclaire, S. Smeets and B. Schaller, the economic analysis of franchise contracts by A.W. Deck and on general report by Ch. Jorgens in this volume.
4 An excpet analysis of franchising research on piercing is to be found in M. Marvin, Franchising: Grundlagen der 2.219; und wettbewerbliche Rechtsordnung der verschiedenen Ordnungsebenen, in: Abhandlungen vom Wissenschaftlichen Verlag 1987, 75 eqq.
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contracts result 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.6 Polemically speaking, we find in franchising contracts the same organized lack of responsibility as in many other formal organizations.7

This becomes clearer if we look at the "external relations" of franchise systems. Consumer interests are primarily affected. 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 consignment logistics. Is there a need here for "putting the contractual veil", a legal instrument making the central office directly liable?8

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


peers, 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? 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 plant and on which franchisees' representatives have a seat and a vote?

Furthermore, creditors 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 central public are also affected. If the franchisee package provides for a course of action which might endanger public goods, such as the environment. Here, the internal division of labor is such that we might well question whether the individual liability of a franchisee is an adequate way of trying to prevent environmental damage.

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 franchise is a GmbH — private limited company) or if he cannot fulfill 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 (produce policy committee or advertising committee), 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 new cope with the organization's 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 franchise system into consideration is open to the following points of criticism:

1. Existence 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 Oberverwaltungsgericht, Freie Streitwacht, 1980, 941, dealt with a similar case.

9 Cf. on the subject of the extent of liability by means of liability for damage to the environment G. Bridgmann, Delikates, Radebe—Radebe, 1964, 432 et seq.: A. Konig, "Die BdStV, Rechtsschutz fur Konsumenten 1985, 200 et seq.

(2) **Division of labor:** Customer services are organized partly centrally and partly centrally by the head office. If that is not the case, a need to take account of any third party effects ("Drittmarktung")\(^{11}\) 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 various liability in \$ 834 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 forms:** 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?

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\(^{11}\) J. Gogelhöfer provides a systematic analysis of the effects of contractual obligations on third parties, in *Schultheiss*, 8th year, pp. 468 to 494.

\(^{12}\) § 834 BGB. "Whenever neither master nor apprentice is bound to compensate any damage which the employee may suffer from use of the tools of the master or from the execution of the work. If, in the course of agreed, and it means he has appropriate equipment of tools and is responsible for their use or deliberation, he has available equipment of tools or has violated the duties of the work, then in the proviso of the employer, or if the damage would have been prevented by an application of this standard, then the duty does not exist.*

\(^{13}\) The same responsibility applies to those who contract with the principal to take care of the handling of the facts described in paragraph 1, clause (2)."
(5) Deference. If we take the deference rationalist of liability law seriously, 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 franchisee at all, as the center of self-regulation in the franchising system, or only indirectly; in any event, they have no direct effect on the firm’s benefit calculations.

(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 (“Kommanditisten”? Do not these similarity justify—and if so on what conditions—a piercing of the “perception 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 gray area of “contra” 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 consist of aspects of the interpenetration of contract and organization. Not for nothing do contemporary economists and organization theorists concentrate on this area. These intermediate organizations have become so important in the USA and Western Europe and above all in Japan, that the “third arena of resources allocation” (in addition to market and organization) is already being spoken of. 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 structures 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 makes it particularly suitable to use as an illustration of the legal problems concerned with this kind of hybrid structure.


16 Oh, the happy days are here! see III.

The problems involved in providing a legal definition of the economic phenomenon of franchising — as a nexus of contracts ("Vertragsverhältnisse")\(^{18}\), as a partnership or as mere tortious "transactions" — reflect real trends in the evolution of the interpenetration of market and organization\(^{16}\). 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 ("Verband") 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. As 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\(^{19}\). 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 franchise) 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 ("BGH-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\(^{20}\)), distribution systems could be clas-
afforded as fiduciary relations since it emphasizes safeguarding interests22. In this way their contractual nature was made clear — paradoxically by reason of their hierarchical organization. Organizational structures were compensated for with the legal concept of "integration" (Eingliederung) of the distribution agents into the distribution organization23. 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 other24.

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 niggardly distracting 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 centralised. This tightly organised internal coordination as well as its external appearance as a single competitive, 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 agents27. On the other hand, there appears to be a phenomenon of "partnership franchising" ("Gemeinschafts-Franchising") which 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 in the American franchising systems of the third generation, the "partners for profit", especially franchised hotel chains and also franchising in the transport and fashion industries28. So, in this context, the difference between safeguarding the in-
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interests 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. There is a tendency, especially in France, to view franchise systems as associations. Not only is the "groupement d'interet economique" held to be the most suitable legal form; but there have also already been legislative proposals that franchise systems should be granted an independent legal personality.

In Germany it is Martinetz, 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. Martinetz suggests the application of the law of partnerships to some franchising arrangements. According to Martinetz, franchising becomes organizations governed by partnership law when a certain level of cooperation has been exceeded. It distinguishes four constellations: subordination, coordination, coalition and confederation. The terms are self-explanatory. He suggests that contracts 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.

Indeed, Marzick even goes so far as to make strictly organized forms of franchising...
sion subject to the German law concerning group enterprises33. He distinguishes between highly centralized forms of "subordination franchising" which become subject to the law of subordinate group enterprises ("Unternehmenskonzern") and those of "cooperation franchising" which are subject to the law of coordinate group enterprises ("Gesellschaftskonzern").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 analogus application of the general principle of liability under the law of associations in § 31 BGB35 seems possible for coalition franchising, which is interpreted as a civil law partnership, and even more so for coalition franchising as a large civil law partnership.36 As far as the extremely hierarchical forms of subordination franchising are concerned, external liability based on the principles of a "qualified" group of companies "a la Aquanor & Telefunken"37 is unavoidable, to say nothing of piercing the corporate veil as a means of direct liability of corporate groups under German corporate law.38

However, striking this construction may appear as first sight, we close inspection we would want to ask whether this construction of 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 Martin's says "organization", he suppresses context; when he says "contract", he suppresses organization.


34 M. Weizsäcker, op. cit., 657 et seq.

35 § 31 BGB is the fundamental rule governing liability of an association for the actions of its members. "The association is responsible for the damage which the board, a member of the board, or another authorized and regularly appointed representative in the exercise of his power, has caused at a third party as a result of action required under the law".

36 Cf. P. Ulrich, in Muster-Kommende Handbuch zur UGb, art. 190 et seq. for a discussion of the liability of civil law partnerships according to § 31 BGB. In analogous applicability to existing systems (including limited liability) it is examined by W.-H. Roth, Quaestiones in UGB-Kapitel 2, Gabler Verlag 1982, 435.

37 There are few decisions by the German Federal High Court concerning external liability of highly centralized groups of companies. Referred to is BGR 55, 330 — Aegina, BGH Telefunken v. Weichert GmbH 1985, 440 — Teyss. For a brief discussion, see H.-D. Amsden, op. cit. (part 33), 337.

38 As established in the leading cases of, e.g. D.H.N. Ltd. v. Towner Maritime 1976, 1 WLR 852, CA., and Franchise Tyre Distributors Ltd. v. Towner Maritime 1967, 136 L.T derived L.N. 213 et seq.

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When Martinetz 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. The common object of sales-promotion, the system's objective of organizing distribution, as it is so clearly defined by Martinetz 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.

This construction is particularly strange in the case of "co-ordination franchising", i.e. where franchised hotel chains or transport franchising with central logistics are concerned. According to Martinetz, 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.

When Martinetz 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.

However, the individual interests of the parties, by contrast, are no longer legally relevant but are merely "economic" motives.

It seems as if neither a purely contractual classification nor a capstoning of contracts into organization can do justice to the hybrid nature of franchising. One should therefore try to mix the types. For example, a simple combination could be to break down into areas of contractual and company law. But this would not help us in any further with franchising contracts, where the fields of action are so intertwined 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.

40 On the case law M. Martinetz, op. cit. (note 4), 586, 214 et seq. (criticism of jurisprudence oriented towards individual contracts), on the other hand 347, 251 (comment on § 347 BGB in restructuring franchising and in coordination franchising is only momentary, see 356 et seq. and 358 et seq.)
41 M. Martinetz, op. cit. (note 3), 280 et seq.
42 M. Martinetz, op. cit. (note 3), 378 et seq., especially 384.
43 § 705 BGB, "through the partnership contract, the partners unilaterally bind themselves to procure, in the manner defined in the contract, the achieving of a common purpose, in particular to make the agreed contributions".
44 M. Martinetz, op. cit. (note 3), 251 et seq., 391 et seq., 412, 420 et seq.
45 See P. Ullrich, in Mischlager Konsortialtarif BGB, Intro, in § 750, no. 70 et seq.; W. Haddick, in 2 T. Sonntag, H. Sterber, Konsortialtarif BGB, Intro in § 750, no. 17 et seq.; more general M. Wolf, in Sonntag, Sterber, Konsortialtarif BGB, § 705, no. 77 et seq.
46 BGHZ 49, 127, 129 et seq.; BGHZ 46, 362.
47 M. Wolf, in Sonntag, Sterber, Konsortialtarif BGB, § 705 no. 22.
noticeable hesitation in academic opinion. These contracts, as usually classified as being sui generis or at least being similar to those governed by company law, apart from the increased duties of loyalty, common to long-term contracts. As far as distribution systems are concerned, in German legal doctrine every associational element is rejected. While each party uses a sales interval, 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, the contractual elements are pressed down. As soon as an exchange element is assumed, then there is a tendency to deny any common objective. At this point, the following question goes to mind. Is it impossible, as a matter of legal construction, to conceive of action being oriented simultaneously towards both collective and individual objectives?

IV. Network

Are we facing here the paradoxes of unitas multiplex which appear in distribution systems just as they do in group enterprises? 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 trusts do not result from the usual legal problems of definition, but from the real contradictions in organized distribution itself? Could it be that eco-

46. M. Lewisch, op. cit., S. 295
47. H. Braulke, Gesellschafts- und betriebliche Gesellschaften, Wirtschaft, 1914, p. 276
48. H. Braulke, op. cit., S. 295
49. H. Braulke, op. cit., S. 295
50. H. Braulke, op. cit., S. 295
51. Ibid., S. 295
52. G. Treuherz, op. cit., S. 295

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nomic actors have invented organizational arrangements which, in the form of formal coincidences oppositioireum, cannot be grasped with conventional legal termi-
ology? In what follows I would like to adopt the thesis that franchising, as one particularly extreme type of closely coordinated distribution system, repre-

mises 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 competition53. In group sociol-
gy the term found its way into "personal networks", loose forms of cooperation which show neither the intensity nor the bureaucratic disadvantages of formal organization54. Political science, "policy-networks" is the name given to a de-
centralized order of political actors, and which is used particularly in the analysis of neo-corporatist phenomena55.

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 assembly56. The idea of a "net contract" was used in con-
tact law to describe banks' payment transactions57. And in company and labour law the concept of a network was used to deal with the external liability and in-
ternal constitution of decentralized-organized group enterprises58. Reecently the

54 N.M. Tushman, Networks in Organizations, in: P.C. North/ W.H. Starbuck (eds.), Handbook of organi-
56 K. Stern/ P. Schroeppe, Interorganizational Policy-making, London 1977; K. Teubner, Exchange Net-
59 W. Mischy, Dezentrale Strukturen der bargeldlosen Zahlungsverkehr, Archiv für die handelsrechte Praxis 189 (1985), 211 et seq.
60 G. Teubner, op. cit. (note 15), 168 et seq.; 174, G. Teubner, Union Mergers, Zeitschrift für Un-
term has also caused a sensation in economics. While the sharp dichotomy of
markets and hierarchy had long prevented a suitable analysis, economists can
now no longer exist the illusion of Japanese suppliers' networks and other,
 similar institutional arrangements. The new solution is as follows: "strategic
networks" have a decisive 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"50
If one wants to go beyond a mere metaphorical use of the image of a "net" and
its "know", then one usually makes the following theoretical statement. By net-
work one generally means a decentrally organized entity of cooperation among
autonomous actors. Networks are seen as loose forms of cooperation which do
not possess the same intensity as formalized organizations. Economists like using
suggestive formulae like "something between markets and hierarchies"51, "managed
economic systems"52, "complex arrays of relationships among
firms"53. Oliver Williamson's theory of hybrid arrangements can be taken as rep-
resentative. Williamson pictures a sliding scale of "Economic Institutions of
Capitalism", from spot-market transactions via long-term contracts to integrated
forms, 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 calculation of transac-
tion costs by the resource owners concerned.64
Even if these ideas aim in the right direction they still have not grasped the cru-
cial point. Networks should not be seen as institutions "between" contest and
organization, but as institutions "beyond" contest and organization. Network ar-
rangements are only possible if the distinction upon which they are built is
fiercely 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-

50 K. MacIntosh/D. Farrow, Redrawing the Boundaries of the Firm, 27 The Journal of Industrial Eco-
nomics 277 (1979). I. Kaufmann, op. cit. (note 51), 17. J. Kogut, The Strategic Networks, Strate-
51 V. Schmidt, op. cit. (note 50), 9.
52 H.B. Young, Networks: Between Market and Hierarchies, 7 Strategic Management Journal 37
(1996).
53 K. MacIntosh/D. Farrow, op. cit. (note 51), 206.
54 J. Kogut/0. Moon, Institutional Relations in Industrial Systems: A Network Approach,
Compared with the Transactional Approach, International Journal of Management and Organiza-
tion (1980).
55 O.E. Williamson, The Economic Institutions of Capitalism: Firms, Markets, Institutions, Cam-
56 K. Sima/If. Hami, op. cit. (note 17), 206 et seq., offer a diagnosis of market and organization failures
in this area and suggest certain cases of "entrepreneurship".

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ous relationship between variety and redundancy. 60 Contractual relations are ex-
tremely flexible, adaptable and innovative; however they show little long-
term orientation, coherence, endurance or accumulated experience. The inven-
tion 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 large 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. 61 Networks, then,
result from a re-entry of the institutionalized distinction between market and hi-

erarchy into the area which the market/hierarchy distinction itself distinguishes.

In the words of the Japanese teachers Izum & 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.

In this way two types of network can be distinguished depending on which side 
of the distinction the reentry is made — market or organization. "Organisation

networks" arise when organizations repeat in themselves the internal differen-
tiation of the economy into a formally organized area and a spontaneous area. De-
centralized group enterprises in the famous "multidimensional form" are the most
significant innovation in this area. In comparison with this, "market networks"
are in areas organized on a market basis. Contractual relations repeat within
their limits the distinction between market and hierarchy by including organiza-
tional elements in the contracts. Networks such as these can rarely organize them-

selves spontaneously. A hub firm, a focus firm or an "imperativa guida" regularly
plays the key role in the construction and running of coordination. This special-
ization 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 differ-
ent levels of the market: industry-trade, or industry-supplier); network centres
on the basis of an equal division of power are just as widespread. 62

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. These relationships have most of the charac-
teristics of a hierarchical relationship relatively untrained tasks, long-term

60 N. Luhmann, The Colos of Law System, in: A. Fiebuch/G. Teuber (eds.), State, Law, Eco-

nomy as Anthropologic System, Munich 1979.


62 K. Hartleb, op. cit. (note 39). The idea of a non-hierarchical centralisation seems to cause

problems for lawyers in the functioning field who want to extract functioning conceptually to hierarchical

subordination. Cf. W. Stauder, op. cit. (note 7) and Ch. Ziegler, op. cit. (notes 3 and 7). Experience

from other network relations should give cause for thought.
point of view, relatively unspecified contra. Three relationships have all the characteristics of ‘investment’, 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 among many of their dimensions.30

In this way contractual networks make use of the interaction between mechanisms which increase variety and those which increase redundancy. 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 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 (“Unternehmensvertrag”), collective ownership (“Gesellschaft”, “Actengesellschaft”) to fully fledged corporations, we regularly notice that collective elements become more important in the same measure as individual elements become less important.31 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, as one and the same time, be greatly

31 C.f. e.g. the commentaries by W. Hachinger, in: Strebel, Stelwens, Kommentar zum BGB, 16th ed., § 705, nos. 7 to seq., 17 to seq.
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increased. The "many-headed hydra" is an exact metaphor for this constellation.

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. From a juridical point of view, the simultaneous coexistence of individual objectives and of common objectives in one and the same instational 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")). From both an economic and a juridical point of view, the behaviour of the actors is simultaneously oriented, 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 forms 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 intranet

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7) See M. Mantorp, op. cit., passim, 412 et seq.
8) H. Woldemar, Die Unvollkommenheit der Privatracht, Tübinger 1988, 10, describes the group of transactions ("Kommern") as a "many-headed monster". Market systems can evolve similarly unforeseeable variations.


chising systems are "observed" as a paradoxical unit multiplex, i.e. as an organizational unit and simultaneously as a plurality of actors. 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 "practices," 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 "initiate" the double orientation of network behavior. It is only the simultaneous influencing of cost-benefit calculations of "net" and "knots" that gives liability law certain chances to control the behavior of the network. A type of liability "beyond" the individualistic joint obligation ("Gesamtschuld") and the collectiveistic collective obligation ("Gesamthand- schuld") should be established. A type of liability which would allow the decentralization of liability within the big network.

As an initial result of this discussion on network structures we can note that franchising systems cannot be one-sidedly qualified as contract or as organization without neglecting important structural features. Merely to say that a certain identity of coordination market the transition from contractual to company law franchising is of little assistance. Nor is it 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 behavior orientation, and of individual and common objectives seems promising. And it suggests a model of "network liability." This 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. Martinez, op. cit. (note 4), 121, who is very informative on this subject.
78 This liability model is chosen in the constitution of the collective obligation ("Gesamthand- schuld") and simultaneous liability of the partners. Hereafter, problems are solved on the one hand by "overlapping," and on the other by the relation of both obligations to each other. Cf. C. Zeller, Al- geweit der Teilhabe-Gesellschaften angewandt, Vol. 1, 1 (Hin zum Fremdvertragsgeschäft), Berlin 1977, 322 sqq. More precise remarks on this are to be found after (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 § 831 BGB79. With these comments on the structural features of "networks" in mind, we can readdress the problems regarding the 'oscillation' in the franchisers' position which are caused by the application of § 831 BGB. It seems that the emphasis on the franchisers' 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" ("Verrichtungsgenossen") of the franchisor. For, in keeping with the hybrid nature of the franchising net, any increased autonomy of the franchisers 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 instructions80, should therefore be extended to include franchisee 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 ("Geschäftsverbreitung"). Unlike the case of employees, who are completely integrated in the hierarchy of a firm, it makes sense, when franchisers are concerned, to talk of their independent liability81. Where, as above, the franchise 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 franchiser and franchisor. But how can we solve the problems that extend beyond the scope of § 831 BGB and which concern the inclusion of the franchisee, 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 burden the franchiser directly with increased duties, i.e., the typical duties of the producer, without there being any need for complicated "piecing together" conventions under the law of contracts or associations82. In this case it is irrelevant whether or not the franchiser relationship is publicly dis-

79 See note 12.
80 BGS Nein Juristische Wochenachse 1980,661; C. Schröder, op. cit. (note 59) 68.
81 C. Brüggemeier, 1986, op. cit. (note 91), 167, correctly distinguishes between employees who are integrated in the hierarchy on one hand and "professionals" on the other. According to him, only the former are independent vis-à-vis liability. Running parallel to this is the principleื่ืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืืื่

82 E. Károki, op. cit. (note 7), 306; Chr. Jäger, op. cit. (note 7).
It is purely and simply the producer's "duty of care" ("Verkehrsphilie") which is decisive.\textsuperscript{53}

Even in those forms of franchising in which the franchisor rather than the franchisee produces the product (bunbargst-ul), the franchisor is directly liable according to the principles of product liability, inasmuch as the production process is subject to its 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.\textsuperscript{44}

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 it into a distinguishing feature on the product presents himself as its producer'.\textsuperscript{54}

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 it is integrated into the production and distribution process.\textsuperscript{55}

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 "nets" and "knots" 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, independency 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 as

\textsuperscript{53} Ch. Jungen, op. cit. (note 7), 210.

\textsuperscript{43} E. Kiesen, op. cit. (note 7), cf. also A. Lindau, "Produktionsliability in und aus fremden Kursen" -- Zürcher Handelsblatt (1986), 553.

\textsuperscript{44} H. Thomas, in O. Palkšte, Kommentar zum ZGB, (München 1990) ProdHaft 4, no. 3, Ch. Jungen, op. cit. (note 7), 216.

adequate measure of consumer protection, e. g. by means of a compulsory insurance scheme for franchises of a sufficient guarantee in the franchise-system. Today, it is a condition of the new group exemption regulation that obligations under guarantee serve to be fulfilled everywhere in the system—a remarkable innovation which represents a kind of "network liability". Since product liability is limited to industrially produced goods, it does not cover the whole field of service franchising. Neither does it address secondary duties which do not refer to products. Apart from the exception under §§ 14 III, 1 III UWG ("Geachtet gegen den unbrauchbaren Wettbewerb") or the Law Against Unfair Competition which establishes a limited extent, the liability of the agent in cases of unfair competition, remains only as liability to sort franchise-systems which, since it is to the formation of individual liability of the system's members, does not deal adequately with their highly-organised nature.

This might be remedied with the further development of the cost law concerning "duties of care" ("Verkehrssicherung") . The basic idea is that setting up a dangerous set of stipulations ("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
until now been accepted. The distribution organization of goods and particularly of services would then be a set of transactions in this sense and the franchise, through heightened duties of care and with no possibilities of excusation, would be directly liable under the law of torts for its defective functioning. 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 establishment of a contractual network such as, 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 ("Verkehrsverpflichtungen") with those under the law of associations ("Organisationsverpflichtungen"). There is also the problem of the unavowed servitutal claims of "consorts": How can these "distribution duties" in the sense of tortious duties of care be distinguished from quasi-contractual, protectivistic duties of good faith ("Schutzpflichten")? 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 delimitation is not yet in sight.

An in-depth examination of this is not possible here, but I would like to point to the rest of my considerations on the following distinction: encouraged by the differentiation between production costs and transaction costs, I would like to distinguish 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., those 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, coop-

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. "Foti 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 enterprise: the group-specific liability, piercing the corporate veil and the principles established in the "Autostran" case. For liability in franchising this would mean that the "technical" risks of the distribution system (transport, storage, information) would be internalized by the various 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 franchisee 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 to 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 law97, 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 Reichsgesetz and some earlier 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 at the level of control. Sc, where does the structural analysis of franchise-system as "networks" had us now?

97 For example W. Heidkamp, in: Steegel-Siebmann, Kommentar zum BGB, Appendix to § 278, no. 25.
Of prime importance for a liability based on the law of associations is the legal principle of § 31 BGB. 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 franchisee. Various doctrinal constructions lead to this result. If one agrees with Martinsek and classifies franchising with its tightly-organized structure as a coordinate group enterprise ("Gliechordnungsgenossen") 98, 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 99, and his construction of "confederate franchising" as one large partnership 100, 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 101. Not to mention the application of § 31 BGB to sub-partnerships ("Unternehmensbeteiligungen") and to partnerships without joint capital ("Gesamthandsvermögen") which it much more problematic 102. Of course the tight internal organization of franchising systems suggest that joint capital and corporate structure 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 this famous "organizational duties" of German case law can be extended to cover contractually organized distribution systems 103. If so, then we can justify the different treatment of the franchisor firm, depending on whether it is organized under company law or whether it is a sole trader 104. On the other hand, the question must be examined of whether the constant extension of the liability of associates under § 31 BGB to cover unincorporated associations, business partnerships, civil law partnerships, and even special assess which have become separate entities, such asehinations at bankruptcies' estates, can stop short of organ-
nized nature of contracts ("Vereinbarungshandlungen").

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 find the interpenetration of market and organisation. The application of group law depends on how we interpret the term "controlling influence" in § 17 German Aktiengesetz. Does this also cover a contractual dependency? If one agrees with Martinick and admits — at least for the extremely centralized forms of franchising — the existence of the group enterprise characteristic, then the application of liability according to the law of group enterprises becomes inevitable. For constellations of "qualified" franchise
groups still would mean a general liability of the franchisee for all the franchisees' debts under the principle of the "Auskränz" case, and in less extreme examples, a selective liability under the principles of direct liability of the group enterprise.

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

106 W. W. Rost, op. cit. (note 31) also with the question is regarded as motivated distinctly. In general for the

system of § 31 BGB as non corporeal forms D. Rauer, in Münchener Kommentar zum BGB, § 31, no. 31, etc., p. 12.

107 § 17 Aktiengesetz. (a) Controlling enterprises as legally independent enterprises (b) which number enterprises (b) controlling enterprise) can exercise, directly or indirectly, a controlling influence.

(b) In the case of a majority-owned enterprise, it is assumed that it is dependent on the enterprise which forms the majority.

108 Case law and academic opinion demand a company's law integration: L. Oettl, Zeitschrift für Wirtschaftsrecht 1951, 461, 463; H. Walter, in: Großkonsortialer Aktiengesellschaft, § 35, no. 3; R. Schulte, V. Erm

auch, Organisationsrecht, (1986) ap. 41. J. Jörn, Bürsenschrift und Aktiengesellschaft, § 17, no. 2; J. Jarve,

Konzernrecht, (1973) no. 4. An example: Bürsenschrift, § 17, no. 2. J. Jarve, Bürsenschrift und Aktiengesellschaft, § 17, no. 2.

109 M. Martinick, op. cit. (note 41) 114 also op. cit. J. Jörn, Die Notwendigkeit der Konsortialgeschäfte als Beispiel der Aktienformen, Die Betriebe 1980, 42, 44, who observes the existence of an actual group enterprise for the parallel cases of suppliers' practices which are organized according to the "just in time" con-


111 See O. Traut, op. cit. (note 32) 241, et seq.

112 Cf. D. Jensen, in: Münchener Kommentar zum BGB, § 31, no. 3 et seq.
significant features of the "network" mentioned above: decentralization, autonomy of the subsidiary unit, double attribution of action? Of course, § 31 BGB solves the problems which a purely juristic 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 contracts, 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 mistake" involved in applying the law of liability for associations in such circumstances. Franchising is not simply organizations clothed in contractual form which can be stealth 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, "agents" as autonomous units of action.

Similar statements can be made about the liability law of group enterprises. If the instruments of the "Austrian" 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 "contracts".113

113 I use this conceptual instrument to Lake Smith. For the organic development and the contemporary problems of "contract" see S. Schauer, Syntaxis, Contracts in the Modern Law 67 et seq.
Its defects cannot be overlooked. In German law there are only three dogmatic approaches, which take into account, if only in 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 these are important matters, 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 dimension.115 (2) Mixted arrangements, or, to use another term, "conventional 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 ("Vertragsgenbfindungen") there can be found a quite different, but still weakly-formed consideration of the organizational nature of contractual systems. The basic problem with the nexus of contract is that in the artificial splitting 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 organizational 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 could be taken in these areas — long-term contracts, mixed arrangements and nexus of contracts — should be systematically extended to form a law of contractual organization or "contragere". 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 thus 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. Gumbacher, op. cit. (para 113), 377 et seq. with further sources.


In some ways, liability law is a test case for these attempts. The liability of net-
works, 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 Mühlert with his proposal for a "net contact" in the
field of basis transfers\(^{116}\). This is an area which can be developed further.
The model can be related to German law by a development in the area of con-
tracts to the benefit of a third party ("Vertrag mit Schutzwirkung für Dritte").
This initiative has been expanded in order to take into account the external ef-
eff ects of bilateral contracts for third parties. Under certain circumstances, the part-
ers 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 organi-
zational 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 an decentralized and involves a division of labour, that
only part of the system (the customer's bank or franchisee) has contractual rela-
tions with the customer. This justifies the assumption of responsibility for third
party effects to the contracting members of the coordination system (relations
between banks, and between franchisor and franchisee).
The governing principle of responsibility must be this: Where the internal divi-
dion 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 con-
tractual relations with third parties, should come within the ambit of the height-
ened duties of care.

Particularly relevant are those above-mentioned considerations in which a fran-
chising system causes injury or damage to consumers because of defective ser-
VICES, and compensation cannot be obtained at all or only insufficiently from
the franchisee who performed the contractual obligation. The franchisee, as the or-
ganizational core, is contractually liable if the "defect" lies "in the system",
perhaps because of a defective instruction from the franchisor or because of a de-
fective handbook which is used for the whole system. Other franchisees are con-
tractually liable as well if a decision made by the franchisee committee had intro-


\(^{118}\) J. Getzsch, "Das Recht der Mittelstelle im Vertriebsvertrag", Zeitschrift für das gesamte Handels- und Wirtschaftsrecht 151 (1987), 93 et seq., 106 et seq., F. Schmitz, "Das Vertriebsvertrag", Zeitschrift für das gesamte Handels-
recht und Wirtschaftsrecht 151 (1987), 118 et seq.

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duced the defect into the system. The attribution of liability to the franchisee 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 highly-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 organizations and its liability law effect on third parties.