

Developing Franchise in Russia

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I. Russia: essential data

Russia, with an area of 17,075,400 km², is the largest country in the world. Two thirds of the territory are occupied by plains. It shares its land borders with 14 countries including Norway, Poland, Ukraine, and Kazakhstan to the south; Mongolia, China and North Korea to the southeast. The capital of Moscow includes 10,433,200 inhabitants with a total population of 141.9 million inhabitants. The Russian Federation is populated mainly by 81.5% Russians 3.8% Tatars, 3% Ukrainians, 1.2% Bashkirs and 1% Chuvashes. The territory is very unevenly inhabited: about 80% of the population lives in the European part of the Russian Federation, on a territory that is only a quarter of the country's total area. The urbanization rate reaches 73%. The top cities represent about a quarter of the urban population.

On the political front, Russia is a federal state governed by the rule of law with a republican form of government. The Constitution enshrines the separation and independence of the executive, legislative and judicial powers. The judicial system is mainly based on the German civil law.

II. Russia's economy and the sector of distribution

In 2007, Russia's Gross Domestic Product was estimated to be US\$ 1.290 billion (including 4.6% for agriculture, 39.2% for industry and 56.3% for services). Growth stood at 6.4% in 2005, 7.1% in 2006 and 8.1% in 2007. Russia registered a 7.6% growth in September 2008. The growth forecast for 2009 should be revised downwards in light of the falling oil prices and the consequences of the global financial crisis. The official unemployment rate is 5.6% and the inflation rate was about 11.9% in December 2007. External trade has continued to grow since 1992 despite a sharp contraction in trade during the financial crisis of 98.

Franchising has really started in Russia in the 90's with notably the big fast-food companies ("McDonald's", "Pizza Hut" and so on.). For 10 years, the Russian market has seen the creation and development of a number of world-known foreign and Russian companies such as "Sbarro", "Subway", "Masterfibre", "Hirsh", "Grillmaster", "Ekonika", "Enton", "Kopeyka" and many others.

In 2005, Russia has experienced a very strong growth in the number of franchise offers, mostly from local businesses. The number of networks increased from 67 brands in 2003 and 85 in 2004 to 138 brands in 2005. Today, there are about 165 networks (including foreign brands and master franchisees) and approximately 3,000 stores.

Russia is very attractive for retail networks because it turned into a market in continuous growth in the consumption field. The growth rate of retail sales reached 15.6% in 2007. There are about 85 million working Russian consumers.

The type of activities involved in franchise reflects trends seen across the world. The retail sector, including different types of food stores, clothing, shoes, etc., holds the first place with 48% of franchise activities. The food industry takes the second place (23%), followed by networks of personal services (12%).

III. Chapter 54 "Commercial Concessions" of the Russian Civil Code

The law of franchise is not regulated as such. Only some aspects of the relationship between the parties are

governed by the provisions of Chapter 54 (“Commercial Concession”) of the Civil Code of the Russian Federation, which entered into force on 1st of March 1996. Thus, the franchise contract is in this text the equivalent of the “contract of the commercial concession”, franchisors are the “right holders” and franchisees the “users”.

Concerning the terms of execution of the franchise contract, two conditions must be met: (a) the contract must be written and (b) it must be registered at the initiative of the franchisor, by the body that has proceeded to the registration of the person or legal entity, whether or not the body is located in a foreign country. Registration is important because it is only after this step that the contract will be enforceable against third parties. Failure to comply with these conditions has the effect of making the contract void. Although the chapter does not cover pre-contractual information in detail, *section 1031* provides that the franchisor has an obligation to transfer the technical and commercial documentation to the franchisee and provide other necessary information in order for the franchisee to exercise the rights granted to him under the contract.

Requirements to obligations of the franchise agreement are similar to the French contractual mechanisms: good faith in the performance of contractual obligations, reciprocal performance of parties’ obligations, and payment of royalties. It should be noted that it belongs to the franchisor to control the quality of products marketed by the franchisee. In addition, the franchisor cannot set standards or limits on product prices of the franchise. *Section 1033* regulates the provisions concerning the restrictions on the rights of the parties and *section 1034* the right holder’s liability for any claim regarding the quality of products sold on the basis of the contract. Regarding claims against the manufacture of franchisor’s products, the latter will be jointly liable with the franchisee.

The franchisor has the right to refuse the renewal of the contract provided that during three years after the expiry of the contract he does not conclude a similar contract of commercial concession or franchise or gives his consent to the conclusion of similar contracts of sub commercial concession in the territory of the expired contract. Otherwise, the franchisor is obliged to offer the franchisee the conclusion of a new contract or compensation for losses suffered by him. If a new contract is concluded, its provisions shall not be less favourable to the franchisee as those contained in the original contract.

Each party has the right to terminate the contract at any time by notifying the other party 6 months in advance. The early termination of the contract is subject to a registration procedure. If the franchisor is not anymore the holder of rights pertaining to his name or his trade name without being replaced by similar rights, the contract will be automatically terminated. It is also the case where the franchisor and the franchisee are declared insolvent.

Aspects such as the use of the trademark, the design of the store, the pricing and advertising are not included in the provisions on the commercial concession. Furthermore, there is still no specific legislation concerning pre-contractual information, specific to franchise contracts. Regarding the Registration of trade marks, Russia, like France, is a signatory to the Madrid Convention.

Gilles Menguy

Avocat & Solicitor, GM Avocats

gmenguy@gm-avocats.com