

Franchising in Russia is the 17th article in Wiley Rein's International Franchise Development Series. The International Franchise Development Series offers a broad overview of franchise regulation and the legal issues confronting franchisors seeking to expand into certain countries from the combined legal perspective of U.S. and local counsel.

Franchising in Russia

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Over the last decade, franchising has become a very attractive commercial and contractual model in Russia. Many domestic and foreign companies use the franchise model to expand into various regions and territories in Russia. More specifically, according to the Annual 2014 Report of the Russian Federal Service for Intellectual Property (Rospatent), there were 3,693 franchise deals registered in 2013 and 4,817 franchise deals registered in 2014.

Russia first passed its legislation devoted to franchising in 1996 (Chapter 54 of the Russian Civil Code). That legislation has been amended a few times to implement new legal concepts and statutory provisions designed to align Russian franchise law with global franchise law and practice. The franchise relationship in Russia also may be impacted by local laws and regulations, such as contract law and law of obligations, corporate and commercial law, real estate and property law, consumer protection and advertising law, taxation and currency control law, as well as other legislation.

Contract Law and Franchising

Since Russian contract law is primarily based on the principle of "freedom of contract," the parties are generally free to agree on the terms and conditions of their underlying agreement. This principle, however, is limited by certain mandatory provisions of Russian contract law and default rules on franchising. Issues that are not specifically addressed in the contract must be resolved by applying the relevant mandatory provisions of Russian contract law and/or the effective default rules on franchising, as explicitly set out in Chapter 54 and as described below.

Good Faith and Fair Dealing

The concepts of "good faith" and "fair dealing" are basic principles of Russian civil law. These principles are

usually supported and enforced by the Russian courts in all disputes involving civil law contracts. Franchise agreements are not an exception in this regard.

Intellectual Property

According to Article 1027 of the Russian Civil Code, under a contract of "commercial concession" (*i.e.*, franchise agreement), the franchisor agrees to grant the franchisee, for consideration, the right to use a set of intellectual property rights, including trademarks and other intellectual property rights, such as trade names and know-how, in the business of the franchisee. Accordingly, the key subject matter of the franchise agreement is a registered trademark. The grant to the franchisee will also include other intellectual property rights (*e.g.*, copyrights, patents, know-how), as the franchise is usually regarded as a "complex" intellectual property license in Russia. The licensed intellectual property must be protected in Russia. For trademarks and patents, the legal protection is based on registration.

Presale Disclosure and Registration

Presale disclosure is not required under Russian law. The parties, however, may elect to provide certain disclosures to each other in order to comply with the above-referenced general civil law principle of "good faith." Since the format and content of presale disclosure is not prescribed by Russian law, the parties are free to determine what presale disclosures will be provided.

An unregistered franchise transaction will be deemed invalid pursuant to Article 1028(2) of the Russian Civil Code. Consequently, it is imperative that the franchise be registered with Rospatent following the execution of a franchise agreement. Notably, there is no specified period within which the required documents must be filed with Rospatent; however, ongoing royalty payments may

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not be remitted abroad until Rospatent registration has been secured, unless otherwise specifically provided in the contract. While there is no general requirement that the franchise agreement be in Russian, the documents filed with Rospatent must be in Russian, or accompanied by a Russian translation.

Competition and Antitrust Issues

In Russia, antitrust activities, abuse of dominance and unfair competition are prohibited under the national competition law; however, “vertical” contracts, such as franchises, typically do not violate the antitrust restrictions.

According to Article 1033 of the Russian Civil Code, franchise agreements may contain various restrictions and covenants, especially on the franchisee. Specifically, the franchisor may impose an in-term non-competition restriction on the franchisee (which may be extended to the licensed territory and contracted intellectual property rights) that prohibits the franchisee from entering into a similar franchise arrangement with a competitor. The franchisee also may be obliged to sell goods at the prices fixed by the franchisor and refrain from selling similar goods offered by competitors. Other covenants as expressly permitted by law can be imposed on the franchisee under contract.

Theoretically, these restrictions may be held invalid by the Russian antimonopoly agency (Federal Antimonopoly Service) if they substantially contradict the national antimonopoly legislation, subject to the relevant market condition and economic status of the contracting parties. Nevertheless, this has not occurred to date. Notably, it is unclear if post-termination non-competition restrictions will be enforceable.

Term and Termination

A franchise agreement may have either a definite term (e.g., five years) or an indefinite term (e.g., in effect during the period of protection of the franchised trademark and/or other intellectual property rights). If the term of the franchise agreement is not defined in the contract, by default under Russian law, the franchise will be deemed granted and effective for five years.

According to Article 1037 of the Russian Civil Code, any party may terminate a franchise agreement with an indefinite term at any time. In that case, six months’ prior written notice is required, unless the contract indicates a different notice period. On the other hand, if a contract

provides for payment of a “break-up” fee, it generally is terminable following 30 days’ notice. In addition, if either party becomes insolvent (bankrupt), the franchise agreement will be terminated.

Enforcing Franchisees’ Obligations

Unlike the U.S., Russian civil procedure does not recognize the concept of “notice pleading.” For example, in the U.S., in order to assert a claim for trademark infringement against a terminated franchisee who continues to use the franchisor’s trademarks, the franchisor need only assert in the complaint its ownership of the trademarks in question. In Russia, however, the franchisor must submit the original trademark registration certificates (or notarized copies of the same). As a result, litigating a matter in the Russian courts will require prior filing of certain necessary documents, which will be different in the U.S. At the same time, enforcing franchisees’ obligations in Russia will be usually much faster from a timing perspective and, therefore, may be more cost efficient. ■

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