



mexico
WORLD focus

www.ipworldonline.com



informa
law

 **trademark**WORLD

 **Patent**WORLD

 **copyright**WORLD



New rules for franchising in Mexico

Ana Castañeda and Jorge León of C&L Attorneys

Franchising is typically a business situation where a franchisee pays a franchisor for the use of the latter's name, reputation and get-up, the exploitation of which will normally remain under the franchisor's control and supervision. Apart from paying a fee for the use of the common business format and the associated intellectual property rights, the franchisee undertakes to maintain and preserve the character of the franchise.¹

It is important to take into account that the legal figures that compounds the Franchise as trademarks, know-how, copyrights, software, patents as well as all the confidential information must be the object of an integral protection based on a healthy and stable legal frame which must provide security and confidence to both the franchisor and franchisee in order to ensure the success of a franchising system.

In Mexico, the Franchise has been legally recognised and regulated by the Mexican legislation since 1991 and, taking into consideration its development as well as the economic and technological benefits that this figure offers worldwide, our Industrial Property Law (IPL) has been object of recent reforms published in the Official Diary of the Federation on 25 January 2006 which extend the protection and security of the contracting parts in a Franchise agreement as well as the related legal figures.

Hereupon a brief analysis of the recent abovementioned reforms:

Article 2. – This Law intends:

VII. To establish conditions of legal security between the parts in the operation of franchises, as well as to guarantee a non-discriminatory treatment for all the franchisees of the same franchisor.

Commentary: Serving as a brief introduction, this article establishes legal security issues between the parties as a priority for the development of the franchises system in Mexico.

Article 142. (Second paragraph)

Anyone who grants a franchise must provide the applicant, at least within 30 days previous to the celebration of the respective agreement, the relative information of the state that keeps his company, in the terms that the regulation of this Law establishes.

The lack of veracity in the above-mentioned information will grant the franchisee the right to claim the franchisor the nullity of the agreement besides granting the possibility to claim payment of the damages caused to him by the breach. The franchisee will be able to exert this right within a year since the celebration of

the agreement. Once the withstanding term is concluded, the franchisee will only have the right to claim the nullity of the agreement.

Commentary: This recently added paragraph is the first recognized legal security for the franchisee in case of receiving deception of the state that keeps the franchisee company. It is important to consider that both, the nullity of the franchise agreement and the demand of damages are legal procedures carried out in the civil courts. These procedures may last between one and three years. This can also be understood as a warning to the franchisors' companies to be complied at the time of providing the offering circular, which contains important information that will define the future of the relationship between the parts.

Article 142 Bis. – The Franchise agreement must consist in writing and will have to contain at least the following requirements:

[Note: We consider the following to be the most relevant]

- “(i) The territory in which the franchisee will perform the activities object of the agreement;
- (ii) The criteria and methods to determine profit and fees of the franchisee;
- (iii) To establish the terms and conditions of sub-franchising, in case that the parties therefore are suitable to;
- (iv) The causes for termination of the franchise agreement;
- (v) The obligation of the franchisee will not exist to alienate his assets to the franchisor or to who this one designates at the end of the agreement, except for pact in opposite; and ...”

Commentary: It is important to mention that the Franchise Agreement must be recorded before the Mexican Institute of Industrial Property (IMPI) in order to be duly recognised by third parties. IMPI proceeds with this inscription in good faith without a meticulous analysis of the content and veracity of the franchise agreement, which ensures a confidential character reserved only for the parts involved which must verify and execute the corresponding legal actions in case of falsification, breach or any other vice or error contained in the agreement. The essence of this new article is the protection and fulfilment of the elements of existence and validity of the franchise agreement, which in case of controversy shall be made worth before the civil courts of the nation and not before IMPI, who only fulfills the due note in its controls of the franchise agreement.

Contract law is of direct relevance to the creation and content of a franchising agreement and particular care must be taken to avoid an agreement becoming void as being in restraint of trade.²

Article 142 Bis 1. – The franchisor will be able to interfere in the organisation and operation of the franchisee, to exclusively guarantee the observance of the standards of administration and image of the franchise according to that established in the agreement.

It will not be considered that the franchisor has interference in cases of mergers, split, transformation, modification of statutes, transmission or burden of social parts or actions of the franchisee that have been anticipated in the respective agreement like determinant of the will of the franchisor for the celebration of the contract with the franchisee.

Commentary: Once business starts running, it is a duty to verify its development and management. In this new article, the image of the involved marks is indirectly being protected in order to preserve the fidelity of the customers.

Article 142 Bis 2. – The franchisee shall keep during the term of the agreement and after termination, the confidentiality of the information that has this character or of which he had knowledge and that are the property of the franchisor, as well as of all the operations and activities celebrated due to the agreement.

Commentary: To safeguard the confidential information is not an easy task, since it is in constant risk of being disclosed and therefore of being used in an advantageous way originating unfair competition and piracy. The disclosure of industrial or commercial secrets in Mexico is not only regulated by the IPL, but also by the penal laws at federal and local levels which consider this action as a crime and therefore punished with a fine and imprisonment.

Article 142 Bis 3. – The franchisor and the franchisee will not be entitled to terminated unilaterally the agreement, unless the agreement has been entered for an indefinite term, or upon the occurrence of a termination event as provided in the agreement. So that the franchisor or the franchisee can terminate the agreement, or that this happens by mutual agreement or rescission, the causes and procedures must have been included in the agreement. In the case of violations to those arranged in the preceding paragraph, the anticipated completion done either by the franchisor or the franchisee will result in penalties that were included in the agreement, or will enable the affected party to claim damages from the other party.

Commentary: As mentioned before, the legislators' spirit consist in the protection of the agreement as the main part of the franchise, being allowed the correspondent legal actions in case of any violation to the agreement.

Article 213. – The following shall constitute administrative infringements:

XXV. Not providing the franchisee with the information

referred at article 142 of this Law, as long as the term for it has lapsed and had been requested:

XXVI. To use the combination of distinctive signs, operative elements and the image, that allows to identify products or services equal or similar in confusion to other legal figures protected by this Law and that by its use cause or induce public to confusion, error or deceit, to make believe or suppose the existence of a relation between the holder of the protected rights and the non-authorized user. The use of such operative elements and images in the indicated forms constitute unfair competition in the terms of section I of this same article.

Commentary: The addition of these two new sections in this article recognises the legal interest that both the franchisor or the franchisee would have to initiate an infringement action before IMPI. It also foresees a key point for the development of the franchising system in Mexico, which consists in offering protection to the existing franchises with respect to its image, which can be copied on bad faith by treacherous third parties by using for themselves the combination of the distinguishing elements of a franchise with impunity, causing therefore the customer's error and confusion. Nowadays this illegal activity already is considered and sanctioned as an infringement.

In view of the above, the IPL latest reforms in regard with franchising provides legal certainty to the parties not only in a mere administrative scope, but also judicial as it enables any type of legal action in case of injuring the rights of the parties as contractors.

Additionally, it is important to mention the work developed by the Mexican Association of Franchises (AMF) which since 1990,



and due to the growth and the important participation of this system in the economic development of the country, became the governing entity of the Franchising system in our country.

According to information provided by the AMF, franchises in Mexico started in 1985, with only four franchises including: McDonalds, KFC, Howard Johnson and Bing Ice-creams. Nowadays they are not alone; in 2004 there were 730 franchises operating in Mexico.³

During 2005 the economic perspective for the franchises grew by at least 17%, with 100 new brands starting business in the national market.

Mexico is ranked by the World Franchise Council (WFC) as a top 10 country in the number of franchises, just below the United Kingdom, Australia, Brazil, Japan, Germany, Canada, the United States of America and China. In only four years there were 1900 networks of franchises operating in Mexico, surpassing the 1500 networks of the USA.

For 2006, foreign franchises in Mexico will not exceed 35% of the existing supply. By mid-2006 the first Mexican Franchise will operate in the Chinese market; the so-called Mexican food franchise "El Fogoncito" will set a precedent for Mexican franchises which, until now, only had a presence in the USA, Canada and other countries of Central America. ■

Notes

1 Holyoak and Torremans, *Intellectual Property Law* (second edition) (London, Butterworth & Co), p. 535.

2 *Ibid.* at p. 536.

3 www.franquiciasdemexico.org/noticias.htm

About the authors

Ana Castañeda is a partner of C&L Attorneys in Mexico City. She specialises in Trademarks, Licensing and Franchising. Ms Castañeda is fluent in Spanish, English and French.

Jorge León is a partner of C&L ATTORNEYS in Mexico City. He specializes in Copyrights and IP Litigation. Mr León is fluent in Spanish and English.

