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Legal Incentives for the Franchising Investments – Serbian Case

Introduction – contemporary legislation of franchising on national and international level

Security of investment in the country considers a healthy commercial law environment. This is of great importance especially for investments in the form of franchising agreements in various forms. A healthy commercial environment embraces a general legislation on commercial contracts as well as an adequate company law, in the sphere of joint venture legislations. Of special importance for the security of franchising investments are intellectual property right regulations where franchisors can rely on ownership of trademarks and know-how. An additional security of franchising investments in the country is been enforced through the confidentiality agreements as well as considerable number of laws and regulations both those that are applicable to the contracts in general and those that considers the specific franchising regulation – *lex specialis*.

In the last 15 years an increased number of the countries, especially developing countries and countries with economics in transition have regulated franchising. Nowadays approximately 30 states have incorporated rules on franchising in domestic regulations.¹ Process and legislation initiatives on national level correspond with the past activity of UNIDROIT (International Institute for Unification of Private Law situated in Rome) in the area of franchising. The instruments which are used in this regulations vary from the

¹ The author spent 2 month research period at the UNIDROIT Library in Rome working on project “Enacting Franchising Disclosure Law in Serbia” in 2005. The Report on Research Project has been adopted from the Governing Council of UNIDROIT in May 2005. The opinion and attitudes in this articles are author’s and doesn’t represent the official opinions of UNIDROIT.

specific franchising law legislations – *lex specialis*, enactment the provision related on franchising in national Civil Code, franchising regulation in other different area of law (for example law that regulate intellectual property) and limited number of countries regulated franchising through governmental regulation. The most numerous are the countries which adopted specific franchising regulation. The first law on franchising was adopted in the USA in 1979, where franchising originated and US federal law on franchising was adopted in 1979 as Federal Trade Commission (FTC) Rule on Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures. It was the first law which regulates the information a franchisor is required to supply the prospective franchisee with (so called *franchising disclosure law*) in order to provide it with all the elements necessary to evaluate the franchise it is proposing to acquire. It is the federal law and FTC Rule applies in all fifty states and it is indented to provide a minimum pre-contractual protection of the franchisee. It therefore applies wherever states have not adopted more stringent requirements. This law is still in force although an amended Rule has been adopted and effective as from July 2007.

France was the first European state which enacted franchising specific disclosure law in 1989 (*Loi Doubin*). After French legislative initiative other countries took the inspiration from the U.S. and France and the process of the franchising national legislation have been started. Nowadays approximately 30 states have incorporated rules on franchising in domestic regulations. Specific franchising regulation in form of the law has also Brazil 1994, Malaysia 1998, Kazakhstan and Korea in 2002, Italy 2004, Belgium 2006, Sweden 2006. Other countries that regulate franchising enacted the provision on franchising in their Civil Code. After Albania in 1994, this method has been used by Russian Federation 1996, Georgia 1997, Belarus 1998, Lithuania 2000, Kazakhstan 2002, Moldova 2003, and Ukraine 2004. The autonomous regulation made by the most important franchising association International Franchise Association and European Franchise Association provides the pre-contractual duty of disclosure in their Code of Ethics for Franchising.

The most important legal instruments regarding franchising are UNIDROIT (International Institute for the Unification of Private Law) *Guide to International Master Franchise Arrangements* (Rome 1988, rev. 2007) contenting high-level information of all problems in different stages of conclusion and implementation of franchising agreement not limited to legal issues only, and the chronologically second instrument, but of the greatest importance for topic of the enactment disclosure law project in Serbia is UNIDROIT

Model Franchise Disclosure Law devoted to the franchisor's duties to disclose material information to franchise, which is together with its Explanatory Report clearly addressed to national legislators, as the "soft law" instrument of the new *lex mercatoria*.

Beside the positive economic climate in Serbia which is very beneficial to franchising, with the most of areas of business life regulated very clearly and sophisticated examination of the legal context on doing franchising in Serbia will be the main subject of the paper. The paper examines the different fields of law relevant for the establishment of franchised concepts and the main fields of law and regulation in Serbia which create such a legal context for franchising agreement in Serbia. Adequate regulation of those fields of law creates a healthy commercial law environment which is of the indispensable importance for franchising development and investments in franchising industry in Serbia.

Recent development of franchising in Serbia and issues to be considered

The current growth in the franchising industry in Serbia is very promising. It starts to be obvious after establishing the Serbian Association for the Development of Franchising (SURF) in 2009, which Association in 2011 has passed the procedure for provisional membership to the European Franchise Federation. Those activities have been followed by number of specialized trainings for potential franchise contractual parties and permanent growth in area of franchising has been confirmed by two International Franchising Fairs in Serbia in 2010 and 2011. All those activities have been organized under auspices of Center of Franchising which is established in 2007 as specialized institution of Serbian Chamber of Commerce for support and promotion of franchising in Serbian economy. In the meantime import of foreign franchise systems such as Fornetti, IQS, Wok to Walk, Costa Coffee, Zara, Mango, Top Shop, Odeja, ReMax, Husse, Dormeo etc. have take the place in Serbia franchising market. Simultaneously, those activities of importing foreign franchise systems has been followed with the creation of numbers of domestic franchised concepts such as MEGA, Adore, Squadra Fish&Bar, Galerija podova and many others. Creation of domestic franchising systems was an important step which shows the more mature level in Serbian development of franchising industry. The legislative activities have followed the process of reintroduction of franchising in Serbian economy and it was twofold. The first initiative was given by the Creators of Draft of the Serbian Civil Code

which have put in the Draft idea and solutions for regulation of contractual aspects of franchising. At the other side there is already present idea of regulation disclosure aspects of franchising activities in Serbia which was inspired by the past work of UNIDROIT and its Franchising Disclosure Model Law. In 2011 UNIDROIT Guide on International Master Franchise Arrangements have been translated into Serbian language and offers a comprehensive examination of the most relevant legal and contractual aspects of franchising such as negotiation, drafting, content and other contractual elements of the master franchise agreement.

Those issues were the positive sign for all the prospective investors in the franchising industry. The Franchising Agreement is quite complex legal instrument asking for the research and implementation of various and numerous aspects of law such as business and company law, law on torts and obligations, contract law, distributorship law, fiscal law, labor law, foreign investment law, competition law, intellectual and industrial property law, real estate and leasing law, law on finance and audit est. In spite Serbian law does not recognize nor provide explicit legal provisions or specific legislation on franchising there are number of laws which could be applied on the franchising arrangements. However from the legal standpoint franchising agreement creates many difficulties and misunderstandings because franchising is not one specific type of the agreement. Franchising is rather a concept which includes different types of contracts and also creates effects of legal instruments which derives from the area of company law such as trust, affiliation or holding (Petsche, Riegler 2004: 4). The most similar to the franchising is the license agreement. From the other side the franchising creates more complex legal relationships between involved parties because of the very close and connected relationships between the franchisors and franchisee. The main feature of the franchising agreement is high level of subordination which is being embodied in the franchisor's right to control of how the franchisee manages its business activities and subsequently in obligation of the franchisee to follow the instructions of the franchisors. Those features of franchising agreement create organization structure which is not typical for the obligation law relationships than rather for the proprietary structures of company law or joint venture agreements.

Franchising has been created the biggest impact in the service industry through the supplying by the franchisee the services according the franchisor's way of doing business and under its business concept which area is most appropriate for cloning of the business activities.

Contemporary legal theory and business practices increasingly use the term franchising to refer the type of so called business format franchising

(BFF) which is the last developed form of franchising (Peters 1996: 695–697). In its integrated and contemporary stage franchising has evolved to the business format franchising. BFF arrangement represents complex agreement under which the franchisee undertakes to manage a business or sells the products or offers the services in accordance with methods and procedures prescribed by the franchisor, and the franchisor undertakes to assist the franchisee through advertising, promotion and other advisory services. The main feature of business format franchising is an exclusively identification between franchisor and franchisee where the later adopts franchisor's entire business system, including its product, brand name, operating manual and marketing strategy. The franchisor has elaborated and tested a specific business procedure for the distribution of goods or supplying of services, known as *business format* contented in Operation Manual (OM) which franchisors then proceed to grant franchisees the right to use. In the *master franchising agreement* the franchisor grants to a partner in another country (sub-franchisor) the exclusive right within the specified territory to open franchise outlets itself or to recruit other partners (sub-franchisees) to grant franchises. It appears that sub-franchisor acts as an alter ego of franchisor in the foreign country. The maintenance of exclusive rights in the master franchise depends on the fulfillment of the prescribed schedule. Master franchising is the multi-contractual arrangement with the three-tiered contractual structure because of the involvements of two agreements which connected three contractual partners: franchisor, sub-franchisor (master franchisee) and sub-franchisee (unite franchisee).

The other frequently used possibility of applying franchising agreement is the *joint venture franchise* whereas franchisor and franchisee enter a joint venture in which the franchisor grants a unit, area development or master franchise to the joint venture entity.

Incentives and prospective methods of franchising regulation in Serbia

Various endeavors of the Serbian institutions to promote and develop of franchising activities in Serbia have been followed during the last years with visible attempts in new Serbian legislation policy to regulate franchising agreement *de lege ferenda*. The most ambitious is the legislative work of the Commission of Legal Experts formed from the Serbian Government in 2006 which proposed in 2007 Model for the regulation of franchising agreement as well as other modern contracts such as leasing and factoring, which are

not regulated contracts in Serbian legislation. Those rules will be integrated as “New Commercial Contracts” in prospective Serbian Law of Obligation which will be the part of the new Serbian Civil Code which is drafted by the Commission. There are number of clauses indented to regulate franchising agreement proposed by the Serbian legislator. The most relevant are relationship provisions which should regulate contractual relationships between the franchisor and franchisee. The most important obligation law aspects of franchising agreement are prescribed to regulate franchising agreement and its essential elements. Those elements includes are contracting parties, area of the economy in which franchising system is to be established, exclusive rights which should be transferred through the agreement, fee amount, terms and payment’s instruments, rights and obligations of the parties, post terms commitments of the parties, liability of the parties for non-performance or delayed performance of the commitments, dispute resolutions clauses, territorial exclusivity clauses, termination clauses and conditions for the renewal as well as other clauses stipulated by the parties to be essential elements of the franchising contract (Draft Serbian Civil Code 2007: 295–296). Other clauses stipulated by the Draft Civil Code stipulated to regulate franchising agreement in Serbia beside the contract’s content and contractual specification is the contract obligatory written form clauses and registration requirements clauses, obligation of the parties, clauses on sub-franchising contract, restrictions, responsibilities, termination and other relationship norms which are stipulated on order to protect equivalency of mutual commitments in franchising contracts as well as position of the franchisee as economically weaker party.

Beside endeavors described below there are trends visible in Serbian legal doctrine which accept contemporary concept of franchising disclosure regulation. Those attempts expressed in the serial of articles in domestic legal literature follows the trends of international franchising regulations realized under auspices of the UNIDROIT (UNIDROIT Model Disclosure Law 2002) prescribing franchisor’s obligation to inform franchisee on most relevant aspects of the prospective franchising contracts which are crucial for their future legal relationship. (Milenkovic-Kerkovic 2009: 12). This type of franchising legislation is indented to protect franchisee as an economy weaker party. More than 2/3 of all states which regulate franchising incorporate the disclosure commitment as an obligation of the franchisor (Milenkovic-Kerkovic 2010: 114–116). One of the most reliable methods to create a secure legal environment for the development of franchising business in Serbia is to enact regulation which prescribes disclosure obligation for the franchisor

offering to sell its franchising concept on Serbian market (Spasic 1996: 12; Parivodic 2003: 125–133)².

Besides, there are various methods and franchising strategy but some of those different approaches are commonly in use, which includes:

- Operations owned my company,
- Direct franchising,
- Area development agreements,
- Master franchise agreements,
- Joint ventures.

The chosen method by which the mechanism is implemented may involve franchisor in establishing some of the form mentioned above, such as branch operation, or subsidiary (Mendelsohn 2000: 18–22).

Actual legal context for franchising business in Serbia

In process of creating decision to invest in Serbian economy through franchising concept there are various factors to be evaluate and considered by prospective international franchisor. In order to be well prepared in process of negotiations with prospective franchisee and later in drafting appropriate franchising agreement foreign investor should take in to the consideration two major aspects of franchising in the targeted countries. There are various business issues which have to be taken into the consideration in the process of establishment the franchising system in target country, such as prospective partners, their business environment and professional network, available financial and labor resources, marketing conditions and circumstances, competitive and finance issues. The common approach in taking decision to invest in the country by establishing franchising system is to consider business auditing together with the investigation of the legal context of the targeted country. Franchising is strongly connected with numbers areas of law so explore of the legal issues should be deep and wide because it could contains various hidden pitfalls which are not created only by the fact of differences between civil law and common law legal tradition and culture.

² After U.S. original disclosure requirements regulation there were proliferation of this type of franchising legislation. After Canada, France was the first European country which enacted specific disclosure regulation in 1989 (*Loi Doubin*). After solutions offered in UNIDROIT Disclosure Franchising Model Law there is a visible trend followed by numbers of countries to take over disclosure method in regulation of franchising agreement. Those are Albania (2001), Australia (2006), Belgium (2006), Brazil (1994), Canada (Alberta) (1995), Canada (Ontario) (2000), Canada (Prince Edward Iceland) (2007), Indonesia (1997 ed. 2006), Italy (2004), Japan (2002), Malaysia (1998), Mexico (2006), China (2004), Romania (1998), Spain (1998), Sweden (2006), Vietnam (2006).

Those different areas of law should be regulated domestically but some of them are regulated at the international level also, such as competition law. Because of complexity of franchising agreement special care could be taken to number of laws, where the most important are the follows:

1. Code of Obligations (Serbian Code of Obligations – published in the Official Gazette SFRJ, No. 29/1978; Amendments in No. 39/1985, 45/1989, and 57/1989; final amendments in the Official Gazette SRJ, No. 31/1993),
2. Serbian Law on Business Companies Act (Official Gazette 36/2011),
3. The Law on Trademarks (Official Gazette No. 104/2009) and other laws on intellectual property,
4. Law on Protection of Competition (Official Gazette 79/2005) and other laws on fair competition and price regulation,
5. Law on Product Liability (Official Gazette 101/05),
6. Legal Entity Profit Tax Law (Official Gazette RS, No. 18/2010),
7. Law on Foreign Exchange (Official Gazette No. 20/09 of 19 March 2009 and 72/09 of 3 September 2009),
8. Company Law (Official Gazette No. 36/2011),
9. Legal Entity Profit Tax Law (Official Gazette, No. 25/01, 80/02, 43/03, 84/04, 18/2010 of 26 March 2010 and 101/11 of 30 December 2011),
10. Law on Consumer Protection (Official Gazette 73/2010),
11. Law on the Amendment of the Legal Entity Profit Tax Law, (Official Gazette, No. 26/01, 80/02, 135/04 and 61/07 and 5/09 of 22 January 2009),
12. Bankruptcy Law (Official Gazette 104/09 of 16 December 2009),
13. Product Liability Law (Official Gazette 101/05),
14. International Private Law (Official Gazette SFRJ No. 43/82 i 72/82 and Official Gazette No. 46/96),
15. Labor Law (Official Gazette, No. 24/2005 of 15 March 2005, 61/05 of 18 July 2005 and 54/09 of 17 July 2009),
16. Law on Accounting and Auditing (Official Gazette 46/06 and 111/09),
17. Law on Financial Leasing (Official Gazette 55/2003 and 61/2005) and other laws which should be applied on franchising.

Reference should be made to all multilateral and bilateral treaties and conventions, especially on double taxation treaties tax as well as on multinational convention which is directly applicable in Serbia, because of ratification such as UN Vienna Sales Convention from 1980.

The most important legal aspect for expanding franchising in targeted country is general contract law of the country which is basis for the conclu-

sion of the franchising agreement and their solutions differ from legislation to legislation. The most important are the differences between civil law legal systems and common law legal systems. Under the civil law systems the code contents implied terms which depending on the nature of contract cannot be contracted on the other way than prescribed (mandatory rules). As there is no specific legislation on franchising in Serbia the relationship between parties is ruled by the freedom of contract principle. Some of the provisions is being enacted for the protection of the economically weaker party- franchisee in case of the franchising contract, which are mandatory. The main legal source of contract law in Serbian legislation is the Code of Obligations which doesn't provide explicit provisions dealing with franchising contracts. Serbia doesn't have separate regulations of commercial contracts from that of other contracts. There is not the specific provision for concluding franchising agreements. Therefore from the strict legal point of view franchising contract should be concluded orally as well, although then there arises problems of proof. But, from 2005 the Law on Trademarks prescribes that franchising contract should be in writing and be registered in the Registrar of Agency for Intellectual Property. Commercial contracts are not subjects to any requirement of the form³ except possible exceptions prescribed by applicable law or form requirements agreed by the parties. From the other side general rules and principles of Serbian Code of Obligations may be applied to franchising contract such as good faith and fair dealing provisions (art.12 of the Code) which prescribed that in conducting the negotiations and in drafting of contract, the parties must conduct themselves in good faith and performed contract in good faith. This broad provision is capable to allow judges to use substantial discretion in applying this principle in the context of pre-contractual disclosure as well. Other general contract clauses should be implemented on the conclusion of franchising agreement such as franchisors duty to provide franchisee with appropriate and objective information, regarding the market opportunities, profitability calculations or sales possibilities. Breach of this duty to inform should fall franchisor under the provision of *culpa in contrahendo* liability for breach of duty to negotiate on fair way in pre contractual phases (art. 30 of the Code). There is another general contract law clause which could be implemented on the franchising contracts which traditionally is drafted as a standard form legal document by the franchisor. This is rule *contra preferentem* (Serbian Code of Obligations, art. 100) which prescribes liability for the party who formulates contract terms in cases of unclear contract clauses which will be interpreted against the party which

³ As prescribed in art. 26. of the Code of Obligations.

stipulated the agreement. In most number of the cases contract stipulator is franchisor.

Other obligation law provisions which could be applied on the franchising agreement *mutatis mutandis* are those which regulate those specific and legislate agreements which implies franchising in their legal nature such as sales agreement clauses (art. 451–551 of Code), lease agreement clauses (art. 567–599 of the Code), license agreement clauses (art. 686–711 of the Code). Especially important are the clauses which regulates termination of lease and license agreements in case of cancellation as well as clauses which prescribe right of licensor for direct compensation of license fee from the sub-licensee in order if licensee fails to realize this commitment personally (art. 707 of the Code).

Legal status of the parties in franchising contracts are of the significant importance which is favorable in Serbian legal context and support independent legal status of the contractual parties in franchising transactions where franchisee is not an agent of the franchisor nor their employees. Serbian Companies Act (Official Gazette 36/2011) enables establishment of franchisee as well as the franchising unit in the property of franchisor in different forms of business entities. Beside entrepreneur which carries on business as individual, franchisee could be established in various forms of partnership (commercial partnership – “ortacko drustvo – OD” and limited partnership – “komanditno drustvo – KD”), limited liability company (“drustvo sa ogranicenom odgovornošću – DOO”) or stock corporation (“akcionarsko drustvo – AD”) and branches.

The most common legal entity in Serbian economy is limited liability company (over 75% of all business entities are established in this legal form) which together with other forms of companies fulfills the conditions to create an independent legal party in franchising agreements.

Serbian Law on Protection of Competition prescribes that franchising agreements could be excluded from the restrictions provided in the law in order to protect free market and prevent abuse of the dominant position of the company.

In complex process of elaboration and taking decision to invest in Serbian economy through conclusion of franchising agreement there are number of questions which relate to various and specific areas of law and solutions which offers Serbian legislation. There are numerous areas of law such as industrial and intellectual property, competition law, taxation law, corporate laws which is connected with legal status of the parties and nature of the legal relationships, employment law, property law, foreign exchange law, import

and export controls, accounting regulations and law. Beside, the main decision have to be taken to operate in a market of Serbia, is the methods by which an franchising operation will be established.

The Relationship of the Parties in Franchise Agreement in Serbian Civil Law

As in most European countries in Serbia also there is neither specific franchising legislation nor regulation neither the specific franchising disclosure law regarding the obligations of the Franchisor to supply the disclosure document to the prospective Franchisee. So, the prospective *Franchisor in Serbia is not specifically or mandatory obliged to communicate to the franchisee franchise offering circular* nor any kind of disclosure document in any other form (FDD). This is applied to all varieties of franchise agreements – master franchise agreements, area development agreements or to the local unit franchise agreements. Of course, general contract law principles contained in the provisions of the Serbian Code of Obligations which relates to the commercial contracts is to be applied. Especially, the franchise agreement has to be based on the general principles and provisions expressed in the Code of Obligations relating inter alia on the obligation to act in accordance with good faith and fair dealing, preventing negotiations in bad faith (*culpa in contrahendo*) provisions, the autonomy of contracting parties as regards the content of the agreement, prohibition of the abuse of rights, prohibition of fraud, *contra preferentem rule* (art.100 Code of Obligation) etc.

Mutual obligations of the parties in franchise contract should be prescribe in the agreement in order to prevent post-contractual interpretations. Contractual provisions regarding the parties' duties and rights it is important all obligations to be included in the contract because there are no regulation which predict mandatory content of the contract but there is general principle of contract law that contract should be drafted and fulfilled in good faith preserving equivalency of parties position during the life of the contract. Almost all franchising contracts content the parties rights to transfer their right from contract or theirs contracts position to a third person which is called sublicensing. The *sublicensing of the trademarks is expressly allowed* by Serbian Code on Obligations (art. 704–707) and contract should provide if the transfer of right to use the license from Licensee to the Sub licensee is conditioned by the authorization of the Licensor. The License Agreement must be in writing as well as the Sublicense Agreement. (art. 687 Code of

Obligation). The Agency for the Intellectual Property keeps the Registry of Trademarks where all the License or Sublicense Agreements are recorded as the legal ground for the transfer of rights on the license at the request of the trademark holder and/or applicant or assignee.

Parties in franchise agreement are independent business entities and each of them is personally responsible for its business activities as well as for the products and services which offers through the franchising network. However, the question of the extent of a *franchisor's liability for products or services provided by a master franchisee* in Serbia is very often set by the prospective investor in franchising area. That issue is the matter of vicarious liability of the master franchisor which is predicted in some national legislation for franchising (Russian Civil Code) but not in Serbia.

Franchised business in Serbia is not issue of any specific regulation of the Serbian law because of the independent legal status of the franchisee. The new Consumer Protection Law in Serbia which enter into force in 2011. prescribes liability of some distributorship systems for sold products and only partially for the services but those provisions are not applicable to the independent legal status of Master Franchisor and Master Franchisee in front of the third parties or customers.

In order to limit its liability for acts of the franchisee Master Franchisor usually set contractual clauses as a disclaimer of liability for acts and omissions of a Master Franchisee. The main goal of those kind of clauses is to show that Master Franchise Agreement related to independent legal status of the Master Franchisee and non existence of any status or corporate legal link between Master Franchisor and Master Franchisee. Independent legal status of franchisee is substantive element of Franchise agreement and franchising legal concept.

Serbian Solutions for the Termination and Expiration of the Franchise Contracts

In Serbia there isn't any specific regulation affecting the termination of the Franchise agreement nor common court practice in this field up to now. It is advisable to predict in Master Franchise agreement that the termination of the Master Franchise Agreements creates simultaneously termination of the Unit Agreement. Otherwise that two independent legal instruments could have independent legal destiny which could create many disputes.

The reasons for termination of agreement are predicated in the contract and one of the reason is franchisor's right terminate the Agreement upon the

filing of a bankruptcy or similar petition by the master franchisee, insolvency, or commencement of actions by creditors.

Under the Serbian Code of Obligations those circumstances create good causes for the termination of the agreement as predicted in the Master Franchise Agreement and those provisions are in accordance with mandatory provisions of Serbian Bankruptcy (2009). Beside there are possibility that depends on the given the nature of the franchisor/master franchisee relationship, the franchisor have rights and ability to terminate the Agreement upon a default by the master franchisee.

And the common clause in franchise agreements relates on franchisors right to refuse to renew the Agreement at the end of the term without cause is applicable by the solutions given in Serbian Code of Obligations. Right of renewal the Franchise agreement does not exist in Serbian legislation or jurisdiction.

There is no specific regulation or legislation in Serbia which could prevent Master Franchisor to refuse to renew the Agreement when it came to its end without a cause. In spite of the fact that some national legislations predict those provisions as the instrument of the Franchisee legal status protection there isn't such a regulation in Serbia nor in the general rule on contract law (Code of Obligation) nor in the regulation of any specific commercial contracts , such as regulation on License Agreement (Code of Obligation, art. 686–711). No laws in Serbia impose Franchisee right on renewal.

Common clause in franchise agreements is the franchisor's right to restrict transfer the master franchisee's rights and obligations from the agreement to a third person. The general rules of the Code of Obligations (art. 145–147) regulate the right of transferring the contract or right to assign the rights under agreements which rules are applicable on the Franchise agreement. General provisions of the Serbian Contract Law allow the rights of the party to prevent or condition such kind of rights with prior consent or approval of the contractual party. Legal nature and features of the Franchise agreement as *intuitu persone* contractual obligations which is concluded because of personal characteristic and features of the Franchisee gives the right of imposing such a condition without any doubts. Those provisions are common in commercial praxis in Serbia and SSI rights as provided in the Section 11 are reasonable and necessary and drafted in a sophisticated way in order to protect mutual interest of the parties.

Intellectual Property Rights as the Incentive for the Franchising in Serbian legal context

Industrial and intellectual property legal institutes are the basis upon which franchise relationship is built and of the fundamental importance so the international conventions and national regulations must be taken into account. Legal protection of the franchising system's elements is crucial for an effective establishment of franchising network. Those elements are trademarks, samples and trade name of the franchisor's company need to be registered and protected. As a franchising system requires the use of common denomination it is the matter of trademark protection and its issue is connected with sublicensing of trademarks.

The License Agreement must be in writing as well as the Sublicense Agreement (art. 687 Code of Obligation). The Agency for the Intellectual Property keeps the Registry of Trademarks where all the License or Sublicense Agreements are recorded as the legal ground for the transfer of rights on the license at the request of the trademark holder and/or applicant or assignee (The Law of the Trademarks 2009).

The Sublicense agreement shall be in writing and shall contain: the date of signing, name and surname or business name, domicile or place of dwelling, and/or seat of the contractual parties, the trademark registration number and/or the number of the trademark application, the term of validity of the license and the scope of the license. Special decision on the registration of the Sublicense Agreement in the Registrar of Trademarks is to be issued under the procedure of the Law on Trademarks and specific Governmental Regulation (art. 52–56 the Law of Trademarks).

After the termination or expiration of the Master Franchise Agreement the Master Franchisee as prior licensed user of the trade mark, trade name, know-how and other intellectual property rights derived from the right to use franchise do not have any rights to use or to transfer any rights deriving from the terminated or expired contract under the Serbian law, as predicted in Section 10.4. of the Master Franchise Agreement.

Taxation law as the Incentive for Franchising Investment in Serbian Economy

In Master franchise agreements fiscal and tax issues are substantively connected with the double taxation treaties (DTT). If franchisor's origin's country has not double taxation treaty with Serbia the taxation structure in interna-

tional franchise transaction considers impose of 20% the Serbian withholding tax rate on the initial franchise fee (entry fee) as well as on the royalty (continuing franchise fee) that is to be paid by Serbian master franchisee party (resident-taxpayer) to Master Franchisor as non-resident. A withholding tax of 20% applies to rental payments transferred outside the country and gains on sale earned by non-residents. The 20% withholding tax should be reduced only under some double tax treaty which in the case of the U.S. and other countries with which Serbia at the moment is not connected with double taxation treaties (Law on the Amendment of the Legal Entity Profit Tax Law 2009, art. 40): “Any taxpayer shall account and pay withholding tax at the rate of 20% on the following: 1) Dividends and share in the profits of a legal entity; 2) Copyright fees and interest accrued to any non-resident taxpayer.” (Art. 40 Legal Entity Profit Tax Law).

If the Franchisor has its own permanent operating unit in the territory of the Republic of Serbia to which Master Franchisee pays entry fees and royalties only then the withholding tax is not to be counted and paid. Instead of withholding tax in this situation the corporate (legal entity) profit tax shall be 10% (which is the lowest in Europe) and in this case non-resident of the Republic of Serbia (non-resident taxpayer represents legal entity formed and having its head office of actual management and control outside the territory of the Republic) shall be subject of taxation for the profit realized by entry fee and royalties paid by Master Franchisee at the rate of 10% which is legal entity profit tax rate which is in Serbia proportional and uniform. (Art. 3–4 Legal Entity Profit Tax Law).

Confidentiality, Trade Secrets and Post-Term-Non-Competition Clauses in Franchise Agreement According Serbian Company Law

In Serbian franchising practice the Agreement on Confidentiality between Franchisor and Master Franchisor (Franchisee) or other person involved in the Master Franchise imposing the indemnity in the form of liquidate damages are very common. The obligations of confidentiality could be imposed not only on the part of the Master franchisee through the Master Franchise Agreement but it is possible to impose enforceable duty on confidentiality on the side of Master Franchisee employees. But, as a separate legal document the Master Franchise Agreement is not a three-party agreement so it can impose obligation only on the side of the Master Franchise. So, it is advisable to impose both an obligation on the side of the Master Franchisor to keep

confidentiality of the essential features of the franchise concept together with the obligation to impose such kind of obligation on the part of the sub-franchisee through the Unit franchise agreement between Master Franchisee and sub-franchisee derives from the Master franchisor's country. Many positive laws in Serbia relate to the prohibitions on the unauthorized disclosure of confidential information such as Company Law, 2011 (especially art 38. of Company Law relates on the protection of the trade secret), corpus of laws in the field of intellectual property, ect. prescribes this duty.

Contractual term and post term non-competition clauses are typical and common in all Franchise agreements in Serbian legal practice. In the Serbian Labor Law, 2009 the post term non-competition clauses are restricted to 2 years period after the termination the labor contract (art. 161. of the Labor Law). Accordingly, both provisions on confidentiality and on contractual and post-contractual non-competition clauses could be imposed in the Unit agreement and in the Labor contract. But, these clauses and their legal ground need to be provided in the Master Franchise Agreement also.

Applicable Law and Choice of Law Issues in Franchise Agreements

According to the art. 19 of Serbian International Private Law: "The Contracts are governed by the law chosen by the parties if not otherwise specified by this Code or by an international treaty". That provision clearly states that the choice of law provision will be recognized and enforced by the Serbian courts as well as the choice of forum clauses which appointed an arbitrator as a choice of forum whose decision or award will be final and binding and at the same time this decision will be recognized and enforceable in front of the Serbian court. Serbia is the party of the New York UN Convention on Recognition and Enforcement on International Arbitration Awards which is ratified in Serbia and as such is a substantial part of national law.

Registration and Governmental Approvals of the Franchise Agreement

The Master Franchise as well as other types of franchise agreements in Serbia are not subject to any governmental approvals of any Serbian governmental body or state agency nor subject any other formalities or neither procedure nor registration is required or necessary.

Conclusion

The above examination of legislative activities and solutions in comparative law and of the provisions of specific franchise laws adopted in recent years and comparison with legal context for franchise agreement in Serbia gives rise to several observations.

First, Serbia doesn't have specific law for franchising agreement in spite there are various areas of law which could be implemented in process of negotiation and drafting of franchising agreements. Serbian Code of Obligations as a modern legal mechanism give through its general legal principles as well as through various specific solutions of different contracts applicable on franchising enough space for development of franchising agreements and franchising business in Serbian economy. Serbian legal context is promotional for franchising. There is no any disclosure requirement for prospective franchisor intended to invest through the franchising in Serbian economy nor there any specific relationship law which contain protective clauses for franchising in Serbia and its contract specification. Serbia doesn't have any requirement for registration nor franchising agreement nor franchise as business activities. Franchisee's right of renewal of the agreement contract on same terms after the agreement is expired doesn't exist in Serbia. Termination of the contract as well as the post-term restrictions cannot gives the right to the franchisee to be awarded to corresponding financial compensation for entering out form the franchising. From the other side the most of the area of law create context which is favorable for franchising such as taxation and fiscal law, protection of the competition law. Provisions relates to intellectual property rights are regulated those content of franchising contracts in modern way which is promotional for franchising.

Institution such as Serbian Association for Franchising Development (SURF) as well as Center for Franchising Serbian Chamber of Commerce give the necessary support in practical and legal problems which could arise in franchising agreements.

Legal activities of Serbian legislator *de lege ferenda* give the reason to believe that in some period of time franchising will be regulated in some way. We consider disclosure as effective way which can protect interests of the parties and could be incentives for prospective franchising development in Serbian economy.

Abstract

Legal Incentives for the Franchising Investments – Serbian Case

The development of the franchising industry and investments in the form of business format franchising in the country is significantly connected with the healthy commercial environment. The franchising agreements are very complex legal instruments, originated in the common law legal systems. Those contracts are the subjects to the considerable number of laws and regulation such as business and company law, law on torts and obligations, contract law, distributorship law, fiscal law, labor law, foreign investment law, competition law, intellectual and industrial property law, real estate and leasing law, law on finance and audit. Together with import of foreign franchise systems during the last years, Serbian economy has witnessed the number of domestic franchised concepts which have been emerged in the last period. The main legal context on doing franchising business in Serbia is offered in the paper. Assuming the commercial law and intellectual property rights as the crucial legal incentives for the investment in the form of franchising the author examines two separate categories of law and regulation relevant for franchising. The law and regulations which are applicable to the notion of the contract as the general institute of the obligation law are the first category of law examined in the article. Other is the regulation relevant for the franchising as the sui generis contract such as disclosure law, as the form of franchise specific regulation. Beside the review of the harmonized legislation on franchise law in international level as well as different national regulation relevant to franchising the author examine the main fields of Serbian law and regulations relevant for franchising agreement and its influence for further franchising growth in Serbian economy.

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