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International Commercial Transactions, Franchising, and Distribution

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I. Agreements Exclusively Performed in Brazil are Subject to the Jurisdiction of the Brazilian Courts

When a dispute resolution clause in a contract provides for the submission of controversies to a foreign court, the jurisdiction of Brazilian courts to hear the controversy cannot be excluded if the agreement is to be performed exclusively in Brazil. That was the ruling on August 19, 2008, of the third panel of the Brazilian Superior Court of Justice (*Superior Tribunal de Justiça*, (STJ),[1] which denied a special appeal filed by the British company RS Components Limited (RS UK) against the Brazilian company RS do Brasil Comércio Importação Exportação Consultoria e Representações Ltda. (RS Brazil). The British company argued that the Brazilian courts lacked jurisdiction because of a dispute resolution clause in the 1996 distribution agreement between RS UK (as principal) and RS Brazil (as distributor) to distribute the British company's products throughout Brazil. The distribution agreement contained a choice of venue clause providing for the exclusive jurisdiction of the English courts to settle any disputes between the parties.

RS Brazil sued RS UK in the city of São Paulo (where RS Brazil is headquartered), seeking indemnity for expenses incurred in setting up the distribution channels in Brazil. The São Paulo court ruled in favor of RS Brazil. RS UK had argued the venue clause in the distribution agreement was freely negotiated between the parties. RS UK also argued that Summarized Precedent (*Súmula*) 335 of the Brazilian Federal Supreme Court (*Supremo Tribunal Federal*, STF) applied to the case. According to Summary Precedent 335, the choice of venue clause is valid for proceedings arising from the contract. RS

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1. S.T.J.J., No. 0207126-3, Relator: Min. Nancy Andrighi, 19.8.2008, (forthcoming), having RS Components Limited as Plaintiff in Error (*Recorrente*) and RS do Brasil Comércio Importação Exportação Consultoria e Representações Ltda. as Respondent (*Recorrido*), and as Reporting Justice (*Relatora*) Nancy Andrighi, of the Brazilian Superior Court of Justice. The Third Panel of STJ decided unanimously to deny the appeal according to the vote of the Reporting Justice that was followed by Justices Massami Uyeda, Sidnei Beneti, and Ari Pargendler.

Brazil argued the agreement was an adhesion contract imposed upon it by RS UK without any negotiation. RS Brazil also argued that Article 9 of the Law of Introduction to the Civil Code (*Lei de Introdução ao Código Civil*, (LICC))[2] provides that contractual obligations must be governed by the law of the country where they are incurred (*lex loci domicilii*).

The São Paulo Court of Appeals (*Tribunal de Justiça de São Paulo*) decided that the choice of venue clause is valid even in adhesion contracts, provided there is no abuse or damage to the defense. In this case, the court found that there was abuse and damage to RS Brazil. In its appeal to the STJ, RS UK again argued that the clauses in the distribution agreement were freely negotiated and that Summary Precedent 335 should apply. RS UK also argued that the judgment of the São Paulo Court of Appeals offended certain rules of the Brazilian Civil Procedure Code,[3] that the contract was signed by each of the parties in their respective country of domicile, and that the payments were made abroad (outside Brazil). But the STJ denied the appeal and held that the fact that payments were made abroad was irrelevant because the obligations assumed by RS Brazil had been effectively performed in Brazil. Furthermore, the STJ found no evidence that payments were made outside Brazil. With respect to the STF Precedent, the STJ held that the choice of venue is valid to the extent that there is no abuse or damage for the adhering party–but found that in this case there was. The STJ finally held that Article 9 of the LICC should apply because the contract was performed in Brazil.

Despite the STJ's decision in the Special Appeal,[4] it is important to stress that Brazilian law contemplates another solution to oust the jurisdiction of the Brazilian courts in this type of situation, allowing the parties to choose a different dispute resolution mechanism. This solution is arbitration, which now can be considered a reliable method of dispute resolution and as an alternative to court litigation. Under Article 2 of the Arbitration Law,[5] the parties may validly insert a contract clause establishing that arbitration proceedings will be governed by foreign law and also indicating the place where the arbitration will be carried out. This choice is limited only by the public policy of the forum.

2. The basic principles of private international law are set out in Lei No. 4.657, de 4 de Setembro de 1942, D.O.U. de 9.9.1942 (Brazil). The rules relating to choice of venue (*forum*) in Brazilian private international law are found in the LICC and in the Civil Procedure Code (CPC) in C.P.C., Lei No. 5.689, de 11 de Janeiro de 1973. Article 12 of the LICC provides that "the Brazilian judicial authorities have subject-matter jurisdiction, when the defendant is domiciled in Brazil or when the obligation has to be performed here." Article 88 of the CPC establishes that "the Brazilian courts have subject-matter jurisdiction when: (i) the defendant, whatever his nationality, is domiciled in Brazil; (ii) the obligation has to be performed in Brazil; and (iii) the action arises from an event or action that took place in Brazil." Therefore, in all three cases, the jurisdiction of the Brazilian courts is not exclusive, with the parties being free to choose their venue, subject to the conditions as to public policy, morality and national sovereignty.

3. C.P.C., Lei No. 5.689, art. 88(i) and (ii).

4. S.T.J.J., 0207126-3.

5. Lei No. 9.307, 23 de Setembro de 1996, D.O.U. de 24.09.1996 (Brazil Arbitration Law).

II. Changes to Russian Franchise and Intellectual Property Laws[6]

The new Part IV of the Russian Civil Code[7] came into effect on January 1, 2008. This is an important change for franchisors because that law contains the section on contracts and other obligations,[8] as well as Chapter 54 on "Commercial Concessions" for franchises (*Kommercheskaya Kontsessiya*).[9] The new law now also contains almost all the intellectual property laws and provisions on licensing intellectual property, including trademarks.[10] The previous intellectual property laws were repealed[11] and moved to Chapter 54 of the Civil Code relating to franchising.

Moving the intellectual property laws into the Civil Code was controversial, and the implications of doing so are still being determined. One advantage of having these laws as part of the Civil Code rather than as separate statutes is that the provisions of the Civil Code are considered more important than individual statutes. Another advantage is the integration of property and contract concepts with those in the Civil Code.

The general view is that the scope of trademark rights has not changed substantially.[12] In Russia, trademark rights are acquired by registration and not by use, and this has not changed. The provisions on trademarks are now under Articles 1477 to 1514 of the Civil Code. Articles 1489 to 1491 contain the provisions on the licensing of trademarks.

There was much criticism over the existing provisions of the Civil Code on Commercial Concessions. The Russian Franchise Association had a working group that produced a draft set of amendments to these provisions and commentaries on the deficiencies.[13] When Part II of the Civil Code was adopted in 1996, an excuse could be made for how its provisions were drafted because of a concern then that elections would result in a less market-oriented Duma.[14] The Russian Franchise Association lobbied for years to amend most restrictive of the law's provisions. Although the law was amended to clarify that franchise agreements are to be registered, they did not remove the provisions on termination and liability of the franchisor as suggested by the Russian Franchise Association.

A previous draft of Part IV had required the licensor to supervise the quality of the goods produced by the licensee. Now Article 1489(2) requires that the licensor only ensure the compliance of the licensee's goods to the quality standards prescribed. But the licensor and the licensee are held jointly liable for the quality of the goods with respect to third parties' claims.

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6. Russia and Ukraine 2008, 43 INT'L LAW. 1173.

7. In Russian, Grazhdanskii Kodeks. An English translation of the first three parts is available at http://www.russian-civil-code.com. A Russian version of all four parts is available at http://www.gk-rf.ru/.

8. Grazhdanskii Kodeks [GK] [Civil Code] pt. I, § III (Law of Obligations).

9. *Id.* at pt. II, § IV, ch. 54.

10. Federal'nyi zakon [FZ] [Federal Laws] 2006, No. 230.

11. Federal'nyi zakon [FZ] [Federal Laws] 2006, No. 231. The Introduction of Part IV of the Civil Code of the Russian Federation was approved by the State Duma on November 24, 2006 and published in the Russian Gazette on December 22, 2006.

12. Pavel Sadovsky, *Part IV of the Civil Code: A Mixed Blessing*, AEB BUS. Q. No. 4 (2007), *available at*: www.magisters.com/publication.php?592/articles/.

13. *See* Franchising in Russia, www.rarf.ru/content/document_r_7DFC947F-9A10-4E58-8579-7D4B4BD40483.html (in Russian).

14. *See* Corinna M. Wissels, *The Russian Civil Code: Will It Boost or Bust Franchising in Russia?*, 22 REV. CENT. & E. EUR. L. 495 (1996).

Under Article 1034 of the Civil Code, the franchisor is liable for claims against the franchisee with respect to quality defects in the franchisee's goods and services. Franchisors consider this one of the more objectionable provisions of Russian franchise laws because it places a higher onus on franchisors.

One major change introduced by the new Part IV is the concept of a "commercial name."[15] Commercial (and certain non-commercial) organizations are allowed to use one such name. The concept is much the same as a "business style name" or "doing business as." The commercial name can be used to identify the company but need not be the same as the formal name on the incorporation documents of the company. Article 1539(5) provides that the owner of a commercial name can grant a right to use such name under certain circumstances, including under Article 1027, commercial concession (franchise) agreements.

This led to changes to Article 1027 in Chapter 54, which contains a definition of a "commercial concession." The first paragraph now reads:

> Under an agreement of commercial concession one party (the right holder) undertakes to provide the other party (the user) for remuneration for a specified or unspecified period the right to use in the user's business a complex of exclusive rights belonging to the right holder, including the right to use trademarks and service marks, as well as rights to other exclusive rights as provided by the agreement, in particular the right to use a trade name and trade secrets (know-how).[16]

The second paragraph remains unchanged and contains a reference to restrictions on the scope of use, territorial or otherwise. Another paragraph was added to state that the provisions of Part IV, Section VII of the Civil Code on license agreements apply to commercial concession agreements, provided that they do not contradict the provisions of the Chapter on Commercial Concession Agreements and the substance of the commercial concession agreement. What this means remains to be determined. Clearly a marketing plan or assistance is not a necessary part of the definition of a franchise in Russia.

Commercial concession agreements must be registered in Russia, and the amendments to Article 1028 now make it clear that the registration is to be made with the federal authority responsible for intellectual property rather than with the tax authorities.

While these provisions may make franchisors reluctant to use the Chapter on Commercial Concessions, the breadth of the definition of the concept of "commercial concession" in Article 1027 and the exemptions provided to commercial concessions in the new law *On the Protection of Competition*,[17] and the new Part IV of the Civil Code on intellectual property, make it difficult to avoid these provisions.

15. Grazhdanskii Kodeks [GK] [Civil Code], *supra* note 8, arts. 1538-41.
16. *Id.* art. 1027 (translation by Paul Jones).
17. Federal'nyi zakon [FZ] [Federal Laws] 2006, No. 135.