

Franchise

In 25 jurisdictions worldwide

Contributing editor
Philip F Zeidman



2016

GETTING THE
DEAL THROUGH 

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DEAL THROUGH 

Franchise 2016

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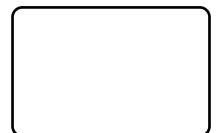


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Mexico

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Overview

1 What forms of business entities are relevant to the typical franchisor?

There are basically two kinds of business (commercial and mercantile) entities that are regularly used by foreign franchisors to do business within Mexico by either utilising them as subsidiaries or as businesses with which franchisors may enter into franchise agreements. These entities are the stock corporation and the limited liability company. In both cases, these entities may also be of variable capital that facilitates the increase or reduction of their corporate capital without having to comply with special formalities. The liability of the holders of interest in any of these two types of entities is limited to the amount of their contributions to the corporate capital.

2 What laws and agencies govern the formation of business entities?

The formation and corporate maintenance of business entities are governed by the General Law of Business Organisations. Different government agencies have jurisdiction over business entities depending on the activities performed by them. The main agencies governing business entities' activities are the Public Registry of Commerce, where all commercial companies must be recorded, the Administration Revenue Service for tax matters and, in the case of foreign entities, the National Registry of Foreign Investments.

3 Provide an overview of the requirements for forming and maintaining a business entity.

Business entities must be incorporated before a notary public and recorded with the Public Registry of Commerce of their corporate domicile. The deed of incorporation of a business entity consists of the by-laws and articles of incorporation evidencing the initial corporate capital, the names of the holders of interest in said capital, the appointment of directors and officers, and the express granting of powers of attorney to specific individuals to represent the company. The minimum number of shareholders or quota-holders to incorporate a stock corporation or a limited liability company is two. Once incorporated, any company having foreign participation in its corporate capital must be recorded with the National Registry of Foreign Investments and the record must be renewed on a yearly basis by submitting an economic, accounting and financial report.

4 What restrictions apply to foreign business entities and foreign investment?

The Mexican government's attitude towards foreign investment is, in general, an open one. Foreign investment in Mexico is regulated mainly by the Constitution and the Foreign Investment Law and its regulations, which exclusively reserve certain activities to Mexican entities without foreign investment, as well as certain activities to Mexican entities with a limit or maximum percentage of foreign investment. In general, the activities in which franchise systems participate in Mexico (such as the hospitality, restaurant, fast-food, automotive and health-care industries) are non-regulated activities; therefore, foreign investors may participate in these without any limitation or restriction.

5 Briefly describe the aspects of the tax system relevant to franchisors. How are foreign businesses and individuals taxed?

Federal, state and local taxes are imposed in Mexico. Federal taxes are collected by the Administration Revenue Service, while state and local taxes are collected by the treasuries of the state and municipal governments.

In accordance with article 1 of the Income Tax Law, individuals and entities are bound to pay income tax in Mexico on the following income:

- Mexican residents, with respect to all their income, without regard to the location of its source;
- non-residents with a permanent establishment in Mexico, but only with respect to the income attributable to such a permanent establishment; and
- non-residents, with respect to income coming from a source located within Mexico, when they do not have a permanent establishment within Mexico or when, having a permanent establishment, the income is not attributable to such an establishment.

In regard to this, article 2 of the Income Tax Law provides that if a foreign resident performs activities within Mexico through an individual or entity (which is different from an independent agent), it would be considered that the resident has a permanent establishment in Mexico with respect to the activities performed by the said individual or entity on behalf of the foreign resident if such an individual or entity exercises powers of attorney to execute agreements in the name of or on behalf of the foreign resident. Likewise, it is considered that a foreign resident has a permanent establishment in Mexico when the foreign resident performs activities in Mexico through an independent agent and this agent carries out the said acts outside its normal activities or course of business.

Foreign franchisors not having a permanent establishment for tax purposes in Mexico, but obtaining an income from a source located within the Mexican territory, are normally taxed on income, which is a tax of a federal nature, and is paid in Mexico by the foreign franchisor through retention or withholding made by the corresponding franchisee.

Likewise, the Income Tax Law establishes that the benefits of international tax conventions shall be applicable when the taxpayer evidences residency in the corresponding foreign country. Mexico's Supreme Court of Justice has determined that the application of tax conventions holds precedence over the federal tax laws (such as the Income Tax Law). This means that a foreign franchisor, as a resident for tax purposes of its country of origin, has the right to be submitted to taxation under the terms of the corresponding tax treaty or convention, if any, instead of being submitted to the provisions of the Income Tax Law. Normally, the applicable withholding tax rates included in international tax conventions to which Mexico is a party are lower than the income tax rate provided for in the Income Tax Law.

6 Are there any relevant labour and employment considerations for typical franchisors? What is the risk that a franchisee or employees of a franchisee could be deemed employees of the franchisor? What can be done to reduce this risk?

None of the applicable Mexican laws contain provisions relating to the possibility of considering the existence of labour relations between a franchisor and a franchisee or between the employees of the franchisee and the franchisor. Nevertheless, when entering into a franchise agreement with

a franchisee, the franchisor should bear in mind that under Mexican law, contracts are governed by their contents and not by how they are named. Therefore, if the franchisor incorporates or accepts the inclusion of provisions within the franchise agreement in error, that may be interpreted as constituting or creating labour relations and the Mexican labour courts would have sufficient authority to determine the labour obligations of the franchisor and find in favour of the individual franchisee or the franchisee's employees due to the nature of the agreement, regardless of its name. The courts could then penalise the franchisor for non-compliance with such labour obligations.

The most important element that could be used by a franchisee to consider the existence of labour relations would be the subordination between the franchisee and the franchisor, which means that all 'recommendations or guidance' provided by the franchisor are in fact considered 'imperative instructions' for the franchisee to comply with. It seems difficult for a franchisor to be considered an employer of its franchisee and certain additional elements would need to be present, such as:

- periodic payments to be made by the franchisor to the franchisee;
- material evidence of the 'instructions' periodically provided by the franchisor to its franchisee;
- the franchisee must be an individual and not an entity; and
- the franchisee needs to have material evidence of its subordinated relationship with the franchisor and its being part of the same company of the franchisor, such as credentials, memoranda, etc.

To reduce the risk of a franchisor being considered an employer of its franchisee under Mexican law, it is suggested that the franchisor should require its prospective franchisee to create a Mexican company to enter into the franchise agreement, which in no way limits the right of the franchisor to request the individual with whom it has been dealing to also sign a franchise agreement as personal guarantor.

Likewise, the franchise agreement must contain a provision called 'absence of labour relations and non-representation', in which both parties state that they enter into the franchise agreement in their capacity as independent contractors and establish the distinction and independence between franchisor, franchisee and the franchisee's employees, among other stipulations.

In general terms, the franchise agreement must be reviewed to confirm that none of its language could be construed to be creating labour relations with its franchisee. Additional practical recommendations may be made on a case-by-case basis.

7 How are trademarks and know-how protected?

Trademarks in Mexico are protected through their registration at the Mexican Institute of Industrial Property (IMPI). Any holder of a trademark registration must prove use of the same, otherwise a cancellation action may be exercised by any third party claiming lack of use by the holder. The Industrial Property Law (IPL) allows for proving the use of a trademark through a licensee (franchisee) provided that the corresponding licence is recorded in the IMPI.

There is no legal obligation for franchisors or franchisees to register a franchise agreement with the IMPI; however, foreign franchisors should consider making such a registration for the purposes of proving the use of their trademarks and protecting their industrial property rights against third parties for the reason explained above. In order not to reveal confidential information contained in the corresponding franchise agreement to the IMPI and in the respective manuals being a part thereof, it is permissible to submit a summary of the franchise agreement containing only the essential information.

There are two alternatives that could be used jointly or separately to protect know-how in Mexico. One is through copyrights based on the federal Copyright Law, and the other is through patents or trade (industrial) secrets based on the IPL. In addition, and to efficiently safeguard franchisors' intellectual property rights, it is always advisable to execute confidentiality agreements with the individuals who will have access to information containing know-how.

Trade secrets are known under Mexican law as 'industrial secrets' and are specifically protected under the IPL. In some cases, disclosure of industrial secrets may be considered a felony. The breach of a confidentiality obligation may result in the payment of damages and losses caused, or of a conventional penalty (liquidated damages) if agreed in the corresponding franchise or confidentiality agreement.

Unauthorised use of intellectual property rights is considered an administrative infringement under the IPL and, therefore, the IMPI is entitled to exercise specific actions against the corresponding infringer. Certain violations of the IPL may be considered felonies.

8 What are the relevant aspects of the real estate market and real estate law?

There are some restrictions on the acquisition of real estate by foreigners or foreign-owned Mexican entities. As a general rule, a foreign individual or entity may directly own real estate in Mexico but foreigners (including individuals or entities) may not acquire direct ownership of land and water located within the 'restricted zone' that consists of a 50km strip of land inland from Mexican coasts and 100km from the country's borders. Although foreigners may not acquire direct ownership in the restricted zone, they can acquire other rights (similar to ownership rights which allow them to dispose of the real estate, and which are commonly used) over real estate in the following cases:

- wholly foreign-owned Mexican entities may directly acquire property within the 'restricted zone' to perform non-residential activities (industrial, commercial or tourism activities). Such acquisitions must be recorded with the Ministry of Foreign Affairs;
- if the real estate is for residential purposes, foreign individuals or entities and Mexican companies with foreign participation in their corporate capital (up to 100 per cent) may acquire the rights of use and benefit from the real estate through a trust; and
- foreign individuals or entities may take and grant a lease in any real estate and other properties in Mexico without any limitation.

Laws and agencies that regulate the offer and sale of franchises

9 What is the legal definition of a franchise?

Article 142 of the IPL defines a franchise as follows.

A franchise exists whenever, in conjunction with a licence to use a trademark granted in writing, technical knowledge is transmitted or technical assistance is furnished in order to enable the licensee to produce or sell goods or render services in a uniform manner and with the operating, commercial and administrative methods established by the holder of the trademark, with the goal of maintaining the quality, prestige and image of the products or services distinguished by the trademark.

10 Which laws and government agencies regulate the offer and sale of franchises?

Franchises in Mexico are governed and regulated by the IPL and its regulations. The governmental agency in charge of applying the IPL is the IMPI. In addition, there are other laws that may have an application to franchises depending on the type of activity performed in Mexico, such as the Commercial Code, the Consumer Protection Federal Law, the Economic Competition Federal Law (the Antitrust Law), the General Law of Business Organisations and the Federal Civil Code.

11 Describe the relevant requirements of these laws and agencies.

The IPL requires that, prior to granting a franchise, the franchisor's information (disclosure document) must be provided to the prospective franchisee at least 30 business days before the execution of the franchise agreement.

Additionally, as a result of the amendments to the IPL effective from 26 January 2006, franchise agreements must be in writing and contain the following minimum provisions:

- the geographical zone in which the franchisee shall mainly perform the activities that are the subject matter of the agreement;
- the location, minimum size and investment characteristics of the infrastructure, relating to the premises in which the franchisee shall carry out the activities deriving from the agreement;
- if applicable, the policies of inventories, marketing and advertising, as well as the provisions relating to the merchandise supply and the engagement with suppliers;
- the policies, procedures and terms for any reimbursement, financing and other considerations in charge of the parties;
- the criteria and methods applicable to determining the franchisee's commissions and profit margins;

- the characteristics of the technical and operational training of the franchisee's personnel, as well as the method or manner in which the franchisor shall provide technical assistance to the franchisee;
- the criteria, methods and procedures of supervision, information, evaluation and grading of the performance and quality of the services under the respective responsibility of the franchisor and the franchisee;
- the terms and conditions of any sub-franchise, in the event it is agreed by the parties;
- termination causes under the franchise agreement;
- events under which the parties may review and, if this happens, mutually agree to amend the terms or conditions of the franchise agreement;
- if applicable, provisions regarding the franchisee's obligation to sell its assets to the franchisor or the franchisor's designated representative, upon the termination of the franchise agreement; and
- if applicable, provisions regarding the franchisee's obligation to sell or transfer the shares of its company to the franchisor or to make the franchisor a partner of such company.

Commercial Code and Federal Civil Code

As previously stated, franchise agreements are governed by the IPL and by the general rules of contracts contained in the Commercial Code and the Federal Civil Code. Commercial activities and contracts in Mexico, such as franchise agreements, are regulated by the general principle of contractual liberty, which applies to all provisions and aspects of a franchise agreement not specifically regulated by the IPL.

Federal Consumer Protection Law

The governmental body in charge of applying this law is the Federal Consumer Protection Agency. In general, this law protects consumers and regulates the activities of providers selling goods and rendering services to the consumers. Its provisions include protection for consumers and restrictions regarding use of information pertaining to the consumers, information provided and advertisements, promotions and offers, services, credit transactions, real estate transactions, warranties and adhesion contracts, among others.

Federal Economic Competition Law

The governmental body in charge of applying this law is the Federal Economic Competition Commission. In accordance with the provisions of this law, there are some restrictions on the general principles of contractual freedom, such as when, through agreements, arrangements or a combination of acts between economic agents, the production, processes, distribution or commercialisation of goods and services is diminished, harmed or impeded, in which case the situations are considered as monopolistic practices. Infringements to the provisions of the Federal Economic Competition Law may result in the nullity of the acts and agreements in violation of the law and the imposition of administrative fines or the payment of damages and losses to third parties.

12 What are the exemptions and exclusions from any franchise laws and regulations?

The IPL is the general applicable law, therefore all franchises operating in Mexico, either through the scheme of master franchise, sub-franchise or individual or unit franchise, are subject to its provisions. The IPL does not provide for any exemptions or exclusions as to its applicability to franchises and does not provide the regulatory authority in charge of its application (IMPI) with the discretion to determine whether a particular distribution or similar arrangement is considered a franchise or not, regardless of its name. There are no exemptions for partnership relationships, wholesale distribution agreements or specific industries (for example, gasoline dealers or automotive dealers) if the relationship meets the definition of a franchise set forth in the IPL.

13 Does any law or regulation create a requirement that must be met before a franchisor may offer franchises?

In terms of the IPL and its regulations, the only requirement that must be met before a franchisor may offer a franchise is the submission of the disclosure document mentioned in the answers to questions 15 and 17.

14 Are there any laws, regulations or government policies that restrict the manner in which a franchisor recruits franchisees or selects its or its franchisees' suppliers?

No, there are no restrictions as to the manner in which a franchisor may recruit franchisees or select its or its franchisees' suppliers.

15 What is the compliance procedure for making pre-contractual disclosure in your country? How often must the disclosures be updated?

The IPL states that disclosure must be provided to the prospective franchisee or master franchisee at least 30 days before entering into the corresponding agreement. According to the provisions of the IPL, all terms provided for in that law must be calculated on business days pursuant to the calendar published every year by the IMPI.

The IPL does not provide for any obligation to update the information contained in the disclosure document, which must be accurate at the time it is delivered to the prospective franchisee.

16 In the case of a sub-franchising structure, who must make pre-sale disclosures to sub-franchisees? If the sub-franchisor must provide disclosure, what must be disclosed concerning the franchisor and the contractual or other relationship between the franchisor and the sub-franchisor?

The IPL makes no distinction in its applicability to master franchises or individual or unit franchises. Its provisions and the disclosure obligations apply to all types of franchises to be established in Mexico.

The IPL requires 'the grantor of a franchise' to provide disclosure to a prospective franchisee. This requires any franchisor, including a master franchisee acting as franchisor, to provide disclosure to the prospective franchisee.

Assuming the master franchisee holds sufficient rights in the franchise to execute a sub-franchise agreement, then the master franchisee would also qualify as the grantor of a franchise and be required to provide disclosure to a prospective sub-franchisee. Even if the franchisor is a party to the sub-franchise agreement, the master franchisee must provide the disclosure since it is the actual grantor of a franchise. In the case of a sub-franchising structure, the disclosure document must contain the same level of information applicable to any franchise, but, in addition, it must describe the relationship between the franchisor and the master franchisee, from which the rights of master franchisee to grant sub-franchises derives.

17 What information must the disclosure document contain?

In accordance with the provisions of the regulations of the IPL, the following technical, economic and financial information must be provided through the submission of the disclosure document:

- name, corporate name or business name, domicile and nationality of the franchisor;
- description of the franchise;
- seniority of the original main franchisor and, if applicable, of the master franchisee of the business subject matter of the franchise;
- intellectual property rights involved in the franchise;
- amounts and concepts of payments that the franchisee must make to the franchisor;
- types of technical assistance and services that the franchisor must provide to the franchisee;
- definition of the geographical area in which the business exploiting the franchise operates;
- rights or restrictions to grant sub-franchises to third parties and, if applicable, the requisites the franchisee must fulfil to grant sub-franchises;
- obligations of the franchisee with respect to the confidential information provided by the franchisor; and
- in general, the obligations and rights of the franchisee arising from the execution of the franchise agreement.

18 Is there any obligation for continuing disclosure?

Once the disclosure document is delivered and the obligation contained in the applicable provisions of the IPL is fulfilled, no ongoing disclosure obligation exists. Though not addressed by the IPL, disclosure should be provided to both a renewing franchisee and to a transferee franchisee, but this does not imply the creation of a continuing disclosure obligation.

19 How do the relevant government agencies enforce the disclosure requirements?

The disclosure obligation may be enforced by the IMPI through the imposition of fines in the event of violation.

20 What actions can franchisees take to obtain relief for violations of disclosure requirements? What are the legal remedies for such violations? How are damages calculated? If the franchisee can cancel or rescind the franchise contract, is the franchisee also entitled to reimbursement or damages?

Failure of a franchisor to provide the disclosure document at least 30 business days prior to the date of execution of a franchise agreement may result in the imposition of an administrative fine by the IMPI. This will only occur, however, if the franchisor fails to provide such information after a written request for it has been made by the prospective franchisee to the franchisor.

In the event of lack of veracity of the disclosed information, the franchisee will be entitled to request the judicial authority to nullify the franchise agreement and to award payment of corresponding damages and losses.

Under Mexican law, there are only damages (as a general figure) and losses; the law does not contemplate other damages such as consequential and punitive damages. According to the provisions of the Federal Civil Code, damages are defined as the decrease or reduction of the patrimony resulting from the breach of an obligation, and losses are defined as the privation of a licit gain that would have been obtained as a consequence of the compliance of an obligation. A competent judge with jurisdiction over the matter would have to calculate the corresponding damages and losses based on the evidence offered by the affected party.

21 In the case of sub-franchising, how is liability for disclosure violations shared between franchisor and sub-franchisor? Are individual officers, directors and employees of the franchisor or the sub-franchisor exposed to liability? If so, what liability?

The only individual or entity liable for a breach of the disclosure obligation is the individual or entity that will effectively grant the franchise. There is no extended liability of the officers, directors or employees of the franchisor for violation of this legal obligation.

22 In addition to any laws or government agencies that specifically regulate offering and selling franchises, what are the general principles of law that affect the offer and sale of franchises? What other regulations or government agencies or industry codes of conduct may affect the offer and sale of franchises?

The only laws that govern the offering and selling of franchises are the IPL, the Regulations of the IPL, the Commercial Code and the Federal Civil Code. As previously stated, franchise transactions are ruled by the general principle of contractual liberty, provided that the terms and conditions contemplated by or contained in the relevant agreements are not against these laws. If the franchisee is able to prove that his or her consent to enter into a franchise agreement was granted based on an error in which the franchisee incurred owing to the violence or bad faith from the franchisor, then the franchisee may be entitled to exercise a legal action and claim for the nullity of the agreement.

23 Other than franchise-specific rules on what disclosures a franchisor should make to a potential franchisee or a franchisee should make to a sub-franchisee regarding predecessors, litigation, trademarks, fees, etc, are there any general rules on pre-sale disclosure that might apply to such transactions?

In addition to the obligation for all franchisors to provide and deliver a disclosure document to their prospective franchisees, which must comply with all requisites established by the IPL and its Regulations and be delivered at least 30 business days prior to entering into the corresponding franchise agreement, there are no other obligations that would apply to pre-sale disclosure. The disclosure document may be prepared in Spanish or in any other language familiar to the prospective franchisee. There is no obligation to register the disclosure document or to obtain authorisation from any governmental agency as to the form and content of the disclosure document.

24 What actions may franchisees take if a franchisor engages in fraudulent or deceptive practices in connection with the offer and sale of franchises? How does this protection differ from the protection provided under franchise sales disclosure laws?

Depending on the specific fraudulent conduct of the franchisor, the franchisee may request the nullity of the franchise agreement, the payment of damages and losses and, in some particular cases, criminal prosecution for fraud.

Legal restrictions on the terms of franchise contracts and the relationship between parties in a franchise relationship

25 Are there specific laws regulating the ongoing relationship between franchisor and franchisee after the franchise contract comes into effect?

The Commercial Code, the Federal Civil Code and the general principles applicable to contracts and of contractual liberty are the laws and principles applicable to the ongoing relationship between the franchisor and franchisee; therefore, such a relation will be mainly governed by the terms and conditions of the franchise agreement.

26 Do other laws affect the franchise relationship?

In addition to the laws regulating a franchise relationship mentioned in question 25, the Federal Law for Personal Data Protection Possessed by Private Persons may have a direct and significant impact on the operation, structure and risk administration of companies involved in the franchising industry that process personal data. The main purpose of this law is to protect personal data held by private persons in order to regulate the lawful, informed and controlled treatment of said data, with the objective of ensuring the right to privacy as well as the right of control over personal data for persons. The law protects personal data that is subject to treatment, use or transfer, at a national and international level.

27 Do other government or trade association policies affect the franchise relationship?

No other government or trade association policies affect the franchise relationship.

28 In what circumstances may a franchisor terminate a franchise relationship? What are the specific legal restrictions on a franchisor's ability to terminate a franchise relationship?

If there are no specific circumstances detailed in the franchise agreement for the anticipated termination or rescission of that agreement, then the provisions of the Federal Civil Code shall apply. These establish that if a party to a contract is in breach of its obligations derived from the corresponding agreement and the other party is in compliance with its own contractual obligations, the non-defaulting party shall have the right to request from the courts having jurisdiction over the matter the rescission of the contract based on the breach by the defaulting party, as well as the payment of corresponding damages and losses.

In addition, if, as a result of an event that is not attributable to any of the parties (that is, due to force majeure or acts of God), the performance of the obligations derived from the agreement is deemed to be impossible, any of the parties may request from the corresponding judicial authority a declaration of termination of the agreement without fault on any side.

Finally, if the agreement is executed for an undetermined period of time, any of the parties will have the right to terminate the agreement at any time, though prior notice must be given to the other party. Although there is no specific term for the anticipation of the delivery of the termination notice, the custom in Mexico is to deliver the said notice at least 30 calendar days before the effective date of termination.

29 In what circumstances may a franchisee terminate a franchise relationship?

In addition to the specific circumstances provided by the IPL that basically refer to the lack of veracity of the information disclosed, a franchisee may terminate a franchise agreement in the same circumstances applicable to a franchisor (see question 28).

30 May a franchisor refuse to renew the franchise agreement with a franchisee? If yes, in what circumstances may a franchisor refuse to renew?

If there are no renewal provisions or rights detailed by the franchise agreement, upon expiration of the duration of the agreement the franchisor may freely refuse to renew the agreement.

31 May a franchisor restrict a franchisee's ability to transfer its franchise or restrict transfers of ownership interests in a franchisee entity?

Pursuant to the provisions of the Federal Civil Code, a franchisee would not be authorised to assign its obligations derived from a franchise agreement without the previous consent of the franchisor. The parties may regulate the transfer of rights and obligations in the franchise agreement with the understanding that they may agree on restrictions for the franchisee to assign or transfer its rights and obligations in the franchise agreement and to subject such transfer to the prior written authorisation of the franchisor, which may be granted or denied at its sole discretion.

With respect to the transfer of ownership interests in the entity appointed as franchisee, the franchisor shall only have the right to restrict such a transfer if, as a consequence, it may modify the personal characteristics of the franchisee that were foreseen by the franchisor as the main motive for entering into the franchise agreement. Therefore, it is advisable to reflect in the franchise agreement that the franchisee must obtain the prior written authorisation of the franchisor for such a transfer.

32 Are there laws or regulations affecting the nature, amount or payment of fees?

There are no laws or regulations affecting the nature, amount or payment of fees. All the same, depending on the nature of the goods or services for which payment is being made, the tax treatment may have different implications. Normally, the international tax treaties to which Mexico is a party distinguish different concepts of payment such as royalties, technical assistance and business profits that have different withholding rates. Therefore, specific tax analysis of the concepts of payment that may derive from a franchise agreement is strongly recommended before entering into the agreement.

33 Are there restrictions on the amount of interest that can be charged on overdue payments?

The franchise agreement is a contract of commercial or mercantile nature, regulated by mercantile laws such as the Commercial Code. As a consequence, according to the provisions of the Commercial Code, there are no restrictions on the amount or percentage of interest that may be charged by a franchisor to a franchisee on overdue payments, even if the franchisee is a natural person or a civil partnership.

If the parties fail to include the applicable default interest on overdue payments in the franchise agreement, then the franchisor will be entitled to charge the legal interest of 6 per cent per annum set forth in the Commercial Code.

34 Are there laws or regulations restricting a franchisee's ability to make payments to a foreign franchisor in the franchisor's domestic currency?

Parties to a franchise agreement can agree in the corresponding contract or agreement to make payments in any currency. But if according to the corresponding contract or agreement the payment is to be made within the territory of Mexico, then, pursuant to the provisions of the Monetary Law, the party obligated to make the corresponding payment may freely elect to make such a payment either in the foreign currency agreed in the contract or agreement or in Mexican currency (pesos) according to the exchange rate published by Mexico's Central Bank in the Official Gazette on the date of payment. If it is agreed that payments are to be made abroad, then the party obliged to make such a payment cannot elect to make it in Mexican currency based on the provisions of the Monetary Law.

35 Are confidentiality covenants in franchise agreements enforceable?

Confidentiality covenants can be enforced in Mexico, especially if violation of the confidentiality obligation under the agreement is sanctioned through the payment of a conventional penalty (a figure similar to liquidated damages) and if the contractual breach constitutes a violation of the

IPL. Pursuant to the provisions of the IPL, violation of a confidentiality obligation through the non-authorised disclosure of a trade (industrial) secret may be considered a felony and can be criminally prosecuted.

36 Is there a general legal obligation on parties to deal with each other in good faith? If so, how does it affect franchise relationships?

In accordance with the provisions of the Federal Civil Code, the consent of a party to an agreement will not be valid if that party was in 'error' when granting its consent. A legal or factual error nullifies the agreement when such an error exists with respect to the mistaken party's main motive for entering into the franchise agreement. In this regard, the Federal Civil Code describes 'bad faith' as the dissimulation of an error by a party to an agreement that was known by the said party. As a consequence, and interpreting the above-mentioned provisions of law in a contrary sense, the parties to an agreement such as a franchise agreement must deal with each other in good faith.

37 Does any law treat franchisees as consumers for the purposes of consumer protection or other legislation?

In principle, under the Federal Consumer Protection Law a 'consumer' is considered to be the natural person or entity that acquires or enjoys goods, products or services as the final beneficiary of the same and a 'supplier' is considered to be the natural person or entity that regularly offers, distributes, sells, leases or grants the use of goods, products, services or a combination of these. In terms of the Mexican legislation, a franchisee is normally considered to be a supplier and not a consumer. An exception to the above is that when a transaction between a franchisee and a third-party supplier (such as the franchisor) involves a claim equal to or less than 367,119.59 pesos, a franchisee could be considered a consumer under the Federal Consumer Protection Law and, therefore, the franchisee may benefit from the protection provided by such statute. In this regard, if the franchisee is an entity, it shall only be considered as a consumer if, in addition to complying with the aforementioned condition, the franchisee is considered to be a micro-entity or a micro-industry in terms of the Law for the Development of Competitiveness of Micro, Small and Medium Entities and the Federal Law for the Promotion of the Micro-Industry and Handicraft Activity.

38 Must disclosure documents and franchise agreements be in the language of your country?

The IPL does not impose any obligations for the disclosure documents and franchise agreements to be prepared in Spanish; however, the summary of the franchise agreement that should be recorded with the IMPI (see question 7) must be in Spanish.

39 What restrictions are there on provisions in franchise contracts?

As a result of the amendments to the IPL that came into effect on 26 January 2006, franchise agreements must be executed in writing and comply with the minimum requirements indicated in question 11. Likewise, none of the parties to a franchise agreement are entitled to terminate or cancel (rescind) the agreement unless it is entered into for an undetermined period of time or except in the event of a just cause that can be foreseen in the agreement.

40 Describe the aspects of competition law in your country that are relevant to the typical franchisor. How are they enforced?

As explained above, the law applicable to competition matters is the Federal Economic Competition Law (see question 11). In accordance with the provisions of this law, there are some restrictions to the general principle of contractual freedom. If agreements, arrangements or a combination of acts between economic agents diminish, harm or impede the production, processes, distribution or commercialisation of goods and services, pursuant to such law, this would be deemed to be monopolistic practice.

Infringements of the provisions of the Competition Law may result in the nullity of the violating acts and agreements, the imposition of administrative fines and the payment of damages and losses to third parties. For example, the obligation imposed on a franchisee by a franchisor to sell its products at determined prices could be considered a monopolistic practice and, therefore, it is advisable to include in franchise agreements that the franchisor will provide the franchisee with a list of suggested retail

prices that will not constitute an obligation on the franchisee, but merely a recommendation.

41 Describe the court system. What types of dispute resolution procedures are available relevant to franchising?

If a dispute arises under a franchise agreement that is considered as a commercial or mercantile agreement, and if the parties to it decide to submit themselves to the applicable laws and competent courts, an ordinary commercial or mercantile procedure may be initiated. The final resolution issued by the corresponding local judge in the first instance may be appealed before the local court of appeals. The final resolution issued by the court of appeals in the second instance may be challenged before a federal court through a constitutional procedure, also known as *amparo*, but only if during the process specific constitutional rights were violated or if the final resolution is issued against the principles of Mexico's Constitution. The resolution issued by the court in the *amparo* procedure would be final and definitive.

An alternative dispute resolution mechanism is arbitration, which may be subject to Mexican or foreign law. Awards that are issued under the law of a country that is party to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards will be recognised and enforced in Mexico as long as such awards are not contrary to Mexico's public order laws. Foreign judgments and arbitration awards that do not contravene public order laws are enforced in Mexico through a recognition and enforcement procedure before a judge, by means of a homologation process, given that Mexico is a party to the United Nations Convention.

The dispute resolution alternatives (jurisdictional and arbitration) are in addition to and independent from any administrative infringement action that may be initiated by a franchisor against any person violating the provisions of the IPL, in which case the IMPI is authorised to impose

provisional or precautionary measures that include the seizure of merchandise and the closure of premises.

42 Describe the principal advantages and disadvantages of arbitration for foreign franchisors considering doing business in your jurisdiction.

In general, arbitration may have more advantages than disadvantages, especially when the foreign franchisor does not have a local subsidiary and operations in Mexico. Arbitration has proved to be time-efficient and if Mexican law is governing the franchise agreement and the resolution of the dispute, it should be possible to enforce an arbitral award. Arbitration in the franchise industry also carries the advantage of allowing the resolution of a problem to be carried out by one or more arbitrators with the necessary expertise and knowledge in franchising, which is a subject not necessarily known or explored by the courts. The most important possible disadvantage is that in certain cases the related costs and fees could be much higher than those applicable in a jurisdictional procedure, depending on the agency administering the arbitration, its rules and the profile of the arbitrators.

43 In what respects, if at all, are foreign franchisors treated differently from domestic franchisors?

From a legal and practical view, domestic and foreign franchisors have equal treatment in Mexico and are equally protected and restricted in terms of Mexican legislation, but lack of knowledge of the domestic laws, administrative restrictions and commercial and operational customs, as well as the lack of legal advice from a competent Mexican law firm, are important elements that could hamper foreign franchisors' entry into the Mexican market.

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