



ICLG

The International Comparative Legal Guide to:

Franchise 2015

1st Edition

A practical cross-border insight into franchise law

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Cyprus

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1 Relevant Legislation and Rules Governing Franchise Transactions

1.1 What is the legal definition of a franchise?

There is no statutory definition of a franchise in Cyprus law, and there is no recognised association to offer a generally-accepted definition. The term is generally understood to refer to a licence given to a manufacturer, distributor or trader to enable them to manufacture or sell a named product or service in a particular area for a stated period.

1.2 What laws regulate the offer and sale of franchises?

No legislation dealing specifically with franchise agreements is currently in force, nor is the enactment of such legislation contemplated. No franchise-specific issues have been litigated, although general issues involved in franchising agreements have come before the courts. The principal issues governing franchises are regulated by the laws relating to competition, contract and intellectual property.

1.3 Are there any registration requirements relating to the franchise system?

There are no specific requirements in Cyprus in relation to the execution of franchise agreements beyond their signature by persons authorised by the parties involved. Although not a requirement, a witness to the signing would add validity to the document.

No specific consents, authorisations, approvals, licences or orders are required from any court or government body in Cyprus for the execution and delivery of a franchise agreement with regard to the franchise itself. There is no obligation to file, record or register a franchise agreement under Cyprus law to render it valid and enforceable.

1.4 Are there mandatory pre-sale disclosure obligations?

While it is usual for the parties to agree between themselves to pre-sale disclosure, there is no mandatory requirement in this regard.

1.5 Do pre-sale disclosure obligations apply to sales to sub-franchisees? Who is required to make the necessary disclosures?

Similarly, there are no mandatory pre-sale disclosure obligations

regarding sales to sub-franchisees. The parties are free to agree to any terms and conditions that are lawful.

1.6 Is the format of disclosures prescribed by law or other regulation, and how often must disclosures be updated? Is there an obligation to make continuing disclosure to existing franchisees?

There is no prescribed format of disclosures prescribed by law or other regulation.

1.7 Are there any other requirements that must be met before a franchise may be offered or sold?

The limitations prescribed in the Contract Law, Cap 149 (“the Contract Law”) apply to franchise agreements. These include incapacity to contract, illegality of contract and contracts brought about by misrepresentation, mistake or duress. All types of contract are subject to a standard of reasonableness and fairness. As with most contracts, stamp duty is payable on franchise agreements. An unstamped agreement will not be admitted as evidence before a Cyprus court or accepted by a government authority such as the Registrar of Trade Marks. The franchisor is advised to apply with the Registrar of Trade Marks to record the registered user of the trade marks and must ensure that all marketing and advertising material complies with the law.

1.8 Is membership of any national franchise association mandatory or commercially advisable?

No. There is no national franchise association.

1.9 Does membership of a national franchise association impose any additional obligations on franchisors?

This is not applicable in Cyprus.

1.10 Is there a requirement for franchise documents or disclosure documents to be translated into the local language?

No, there is no requirement for documents to be written in or translated into an official language. However, in the event of court proceedings the court may require the parties to provide an official translation of the franchise agreement and any other relevant documentation.

2 Business Organisations Through Which a Franchised Business can be Carried On

2.1 Are there any foreign investment laws that impose restrictions on non-nationals in respect of the ownership or control of a business in Cyprus?

No. Foreign direct investment in Cyprus from non-EU countries has been fully liberalised since 1 October 2004. The only exception from this principle relates to regulated sectors such as financial services, the media and public utilities.

2.2 What forms of business entity are typically used by franchisors?

The most commonly-encountered franchise structure is through a legal entity. Joint ventures are not commonly used in franchise operations. The advantage of using a legal entity is that it ensures that the franchisor has the exclusive commitment of the franchisee (the legal entity) to market the goods in the local market and achieves a more effective control and supervision of the brand market. The disadvantage is that it requires a long-term investment because the brand product returns can be slow.

2.3 Are there any registration requirements or other formalities applicable to a new business entity as a precondition to being able to trade in Cyprus?

There are the usual formalities and requirements to be met before a new business entity can begin to trade, such as registering for taxation, VAT and social insurance. Other requirements depend on the nature of the business, for example in order to protect public health and welfare, but they are no more onerous than in the rest of the EU.

3 Competition Law

3.1 Provide an overview of the competition laws that apply to the offer and sale of franchises.

All franchise agreements must comply with Cyprus competition law, which is governed by the Protection of Competition Law 2008 and 2014 (Law 13(I) of 2008 as amended by Law 41(I) of 2014) (“the Competition Law”). The Competition Law was introduced to harmonise Cyprus competition law with EU competition legislation. Its main provisions are a reproduction of Articles 81 and 82 of the Treaty establishing the European Community (which were formerly Articles 85 and 86 of the Treaty of Rome and are now Articles 101 and 102 of the Treaty on the Functioning of the European Union (“TFEU”)).

3.2 Is there a maximum permitted term for a franchise agreement?

No, there is no legal limit on the duration of a franchise agreement. Usually a franchise agreement has a term of about two to five years. From a competition law perspective the duration of a franchise agreement is one of the factors that are taken into account in order to determine whether there may be a potential adverse effect on competition, along with the nature of the product, the territorial restrictions, restraints of trade and the franchisor’s share of the market for the relevant product.

3.3 Is there a maximum permitted term for any related product supply agreement?

No, there is no legal limit on the duration of a product supply agreement. However, from a competition law perspective the term of the product supply agreement may be challenged by an interested party or examined *ex officio* by the competition authority and such term may be determined as unfair by the competition authority, taking into account the guidelines established in reported cases of the EU Commission.

3.4 Are there restrictions on the ability of the franchisor to impose minimum resale prices?

All franchise agreements must comply with competition law, and any agreements between undertakings that may affect trade and which have as their object or effect the prevention, restriction, or distortion of competition within Cyprus are prohibited and void *ab initio*. Agreements or concerted practices having as their direct or indirect object the establishment of a fixed or minimum resale price or a fixed or minimum price level to be observed by the buyer, are treated as a hard-core restriction by the competition authority.

3.5 Encroachment - are there any minimum obligations that a franchisor must observe when offering franchises in adjoining areas or streets?

From a competition law perspective the franchisor is obliged to ensure that any proposed franchise arrangements for an adjoining territory will not constitute unfair competition for the incumbent franchisee. Furthermore, under the principles of Cyprus contract law, there is an implied covenant of good faith and fair dealing that forbids a party to a contract from doing anything that will impair the other party’s right to receive the fruits of that contract.

3.6 Are in-term and post-term non-compete and non-solicitation of customers covenants enforceable?

Non-competition clauses are common in franchise agreements to protect the know-how and goodwill that is licensed to the franchisee. Covenants not to compete are classed as “restraint of trade” clauses under Cyprus law. Section 27(1) of the Contract Law (which is to a great extent a codification of the English common law on contracts) provides that any agreement by which any person is restrained from exercising a lawful profession, trade or business of any kind is to that extent void. The use of non-competition clauses during the term of the franchise agreement and for 12 months after the termination of the agreement in the same area as the franchise outlet is generally accepted by the courts as an appropriate means of protecting the franchisor’s know-how and trade secrets. A non-competition obligation may be imposed after the termination of an agreement if the following conditions are met:

- It is limited to a period of one year.
- It relates only to goods or services that compete with the goods or services that are the subject of the agreement.
- It is limited to the premises and land from which the goods or services were sold.
- It is indispensable in order to protect know-how transferred during the course of the agreement.

4 Protecting the Brand and other Intellectual Property

4.1 How are trade marks protected?

Trade marks and service marks may be protected in Cyprus by registration with the Registrar of Trade Marks, a department of the Registrar of Companies and Official Receiver, under the Trade Marks Law, Cap 268, as amended (“the Trade Marks Law”). In order to register a trade mark the specified application form (TM1) must be completed and submitted by a lawyer authorised to practise in Cyprus. Any legal or natural person, regardless of nationality or domicile, may register a trade mark in Cyprus and has the same rights of registration as a Cypriot proprietor. The registration and protection is for an initial period of seven years, and may be renewed on application for periods of 14 years at a time; there is no limitation on the number of renewals.

Licensing of unregistered marks may be achieved in practical terms, either by the signing of a separate licence agreement or through the incorporation of a licence clause in the franchise agreement.

It is advisable to register the licensed user of Cyprus-registered trade marks with the Registrar of Trade Marks, to avoid any possible issues that may arise about the rights of the licensee with regard to the licensed marks. In the event of non-registration of a licensed user, a clause preventing the franchisee from registering the franchisor’s trade marks in the franchisee’s name can be incorporated. In the instance of unregistered trade marks, the franchisor is advised to register these with the Cyprus Registrar of Trade Marks and to apply, as the registered owner of the Cyprus marks, to register the user of the Cyprus trade marks, thus making it impossible for the franchisee to register the trade marks under his name.

4.2 Are know-how, trade secrets and other business-critical confidential information (e.g. the Operations Manual) protected by local law?

The goodwill of a business in Cyprus is protected by the law of passing off. Confidential information and know-how relating to the franchisor’s business (including information on marketing procedures, staff training and pricing policies) are protected contractually through the franchise agreement itself, as the law of copyright does not offer protection unless the confidential information or know-how bears an original distinctive representation of the franchised business. Within the constraints imposed by competition law, the franchise agreement must emphasise the franchisee’s duty to maintain the confidentiality of the information and know-how licensed to it.

The relief usually sought for infringement is an injunction restraining the further use of the trade mark by the unauthorised party and an enquiry as to damages. If the infringement is substantial, the court may also order the delivery up of the spurious marks for destruction, or the defendant may be ordered to account for the profits made through the sale of the goods or services infringing the proprietor’s trade mark.

The defences to infringement are various and include the arguments that the respective marks are not confusingly similar or that the goods in respect of which the alleged infringement is taking place are not covered by the registration. In addition, the defendant may claim that the registration is invalid or liable to be expunged. Under the assertion of honest concurrent use as provided by section 14(2) of the Trade Marks Law, the court or the Registrar may permit the registration or use of trade marks that are identical or nearly resemble each other in respect of the same goods or services or description of

goods or services, by more than one proprietor where there has been honest concurrent use, that is to say, where the use of the trade marks has been in good faith. Registration is subject to such conditions and limitations as the court or the Registrar may impose.

In an action for infringement, the burden of proof lies on the proprietor of the registered trade mark to establish that the resemblance between his trade mark and that used by the defendant is deceptive.

A foreign proprietor of a trade mark registered in Cyprus can bring proceedings against a third party for infringement, having joined the licensee as a party to the action and given security for costs.

4.3 Is copyright (in the Operations Manual or in proprietary software developed by the franchisor and licensed to the franchisee under the franchise agreement) protected by local law?

Copyright is capable of protecting many aspects of the franchised business, such as proprietary software, design of products, decoration, staff uniform, insignia or other logos and layout plans, irrespective of the fact that such designs or marks may be capable of registration as trade marks or designs. Examples of confidential information and know-how that can be copyrighted include operation manuals, slogans, publicity materials and computer programs. No copyright may exist unless the work is of an original character and has been reduced to writing, recording or some other material form.

Although there is currently no system of copyright registration in Cyprus, effective protection of rights and restrictions pertaining to copyright is provided by the Right of Intellectual Property Law, Law 59 of 1976, as amended (“the Copyright Law”). It is therefore advisable that a franchise agreement should clearly stipulate the material and information that the franchisor deems to be protected by copyright, especially where such information is confidential and unpublished, and should set out concisely and comprehensively the conditions on which such material and information is licensed to the franchisee.

The Copyright Law provides remedies for copyright infringement, setting out a range of offences committed by those who infringe copyright and imposing sanctions. Penalties include fines or imprisonment for up to three years. The court may order that copies of the work in the possession of the offender which appear to be infringing copies should be destroyed or delivered to the owner of the copyright.

Both preventive and compensatory civil remedies may be sought in the event of copyright infringement. Preventive remedies include the power of search and seizure of infringing material and anticipatory injunctions, whereas compensatory remedies consist of an award of damages to the plaintiff, an order for destruction or delivery up of infringing copies and the equipment by which copies are produced, and an order for accounts.

5 Liability

5.1 What are the remedies that can be enforced against a franchisor for failure to comply with mandatory disclosure obligations? Is a franchisee entitled to rescind the franchise agreement and/or claim damages?

The franchisee may seek an interlocutory order prohibiting the franchisor from disclosing any information. The franchisee is entitled to rescind the contract and claim damages for loss resulting from the breach.

5.2 In the case of sub-franchising, how is liability for disclosure non-compliance or for misrepresentation in terms of data disclosed being incomplete, inaccurate or misleading allocated between franchisor and franchisee? If the franchisor takes an indemnity from the master franchisee in the Master Franchise Agreement, are there any limitations on such an indemnity being enforceable against the master franchisee?

In the case of sub-franchising, liability for disclosure, non-compliance or for misrepresentation in terms of data disclosed being incomplete, inaccurate or misleading, may be incurred by the franchisor or the franchisee depending on the interpretation of the terms of the franchise agreement between the franchisor and the franchisee. An indemnity clause as regards non-disclosure obligations will be enforceable against the master franchisee so long as it is interpreted as reasonable and fair and is not against the general principles of contract law, competition law and intellectual property rights laws.

5.3 Can a franchisor successfully avoid liability for pre-contractual misrepresentation by including disclaimer clauses in the franchise agreement?

No, a franchisor cannot avoid liability for pre-contractual misrepresentation by including disclaimer clauses in the franchise agreement, because the franchise agreement may be held to be void, and therefore unenforceable, if it was brought about under fraudulent misrepresentation.

5.4 Does the law permit class actions to be brought by a number of allegedly aggrieved claimants and, if so, are class action waiver clauses enforceable despite the expense and inconvenience of individual arbitrations?

Under the Civil Procedure Rules, class actions are not available. In civil actions the aggrieved parties may apply for an order of the court to be joined as co-plaintiffs or co-defendants where they have a joint cause of action or joint defence.

6 Governing Law

6.1 Is there a requirement for franchise documents to be governed by local law? If not, is there any generally accepted norm relating to choice of governing law, if it is not local law?

No, there is no requirement for franchise documents to be governed by local law and there is a general acceptance of another country's law to govern franchise agreements. A choice of a foreign law as the governing law of a franchise agreement would most likely be recognised and given effect to in any action brought before a court of competent jurisdiction in Cyprus, subject to that law being pleaded and proved, except for provisions:

- which the court considers procedural in nature;
- which are revenue or penal laws; or
- the application of which would be inconsistent with public policy as that term is interpreted under the laws of Cyprus.

6.2 Do the local courts provide a remedy, or will they enforce orders granted by other countries' courts, for interlocutory relief (injunction) against a rogue franchisee to prevent damage to the brand or misuse of business-critical confidential information?

Subject to the terms of the franchise agreement, the franchisor is entitled to sue as a plaintiff in the Cyprus courts to enforce its rights under the franchise agreement. The relief usually sought for infringement is an injunction restraining the misuse by the unauthorised party and an enquiry as to damages. Plaintiffs from outside the EU may be required to provide security for costs unless they have sufficient assets in the jurisdiction to satisfy any order that may be made against them to pay the defendant's costs.

The arrangements for enforcement of overseas judgments and awards are as follows:

- a judgment obtained in a court of an EU Member State against a franchisee will be recognised and enforced in Cyprus under Regulation 44/2001;
- there are bilateral agreements with several other countries under which judgments obtained in the courts of those countries may be enforced;
- a judgment obtained in any other foreign court may be enforced in Cyprus under common law by bringing an action on the judgment; and
- as a contracting state to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, Cyprus is bound in principle to enforce awards made in foreign states which are parties to the Convention.

7 Real Estate

7.1 Generally speaking, is there a typical length of term for a commercial property lease?

A typical term for a commercial property lease is two to five years with a right to renew prior to expiration. In the instance of a statutory tenancy, the tenant has the right to retain possession at the expiry of the tenancy agreement subject to payment of the rent due in accordance with the terms of the tenancy agreement or payment of the revised rent in compliance with a court order.

7.2 Is the concept of an option/conditional lease assignment over the lease (under which a franchisor has the right to step into the franchisee/tenant's shoes under the lease, or direct that a third party (often a replacement franchisee) may do so upon the failure of the original tenant or the termination of the franchise agreement) understood and enforceable?

The franchisor has no power to take over or assign the lease or direct a third party to do so and carry on the business of the franchisee on the failure of the original tenant (franchisee) who defaults or becomes insolvent, unless the lease agreement specifically provides this.

7.3 Are there any restrictions on non-national entities holding any interest in real estate, or being able to sub-lease property?

The Acquisition of Immovable Property (Aliens) Law, which regulates the purchase of immovable property in Cyprus by non-

Cypriots, is a relic of British rule, and the restrictions on foreign ownership of immovable property have all but disappeared. Since Cyprus joined the EU in 2004 the restrictions on EU (and EEA) citizens have been removed and EEA citizens and companies incorporated in the EEA are free to acquire property on the same terms as Cyprus citizens. Only third-country nationals and companies incorporated outside the EU are required to go through the approval procedure set out in the law, which in any event is generally a formality. In the instance of sub-leasing property there are no restrictions on overseas entities.

7.4 Give a general overview of the commercial real estate market. Specifically, can a tenant reasonably expect to secure an initial rent free period when entering into a new lease (and if so, for how long, generally), or are landlords demanding “key money” (a premium for a lease of a particular location)?

The current state of the market for commercial properties, specifically the retail, coffee shop, food takeaway, restaurant and hotel sectors, offers excellent opportunities for lessees or purchasers.

8 Online Trading

8.1 If an online order for products or request for services is received from a potential customer located outside the franchisee's exclusive territory, can the franchise agreement impose a binding requirement for the request to be re-directed to the franchisee for the territory from which the sales request originated?

A binding requirement in a franchise agreement for an online order or request for services to be re-directed to the franchisee for the territory from which the sales request originated, may be interpreted by the competition authority as re-routing customers in violation of the Block Exemption Regulation, and thus invalid on competition grounds.

8.2 Are there any limitations on a franchisor being able to require a former franchisee to assign local domain names to the franchisor on the termination or expiry of the franchise agreement?

There are no limitations for the assignment of local domain names to the franchisor on the termination or expiry of the franchise agreement. The recording of the assignment of a domain name can be filed with the appropriate local authority. A franchisee cannot refuse to assign a domain name to the franchisor where the franchise agreement explicitly stipulates that the domain name is to remain the property of the franchisor after the termination of the franchise agreement.

9 Termination

9.1 Are there any mandatory local laws that might override the termination rights that one might typically expect to see in a franchise agreement?

No. There are no mandatory local laws that might override the termination rights in a franchise agreement. Termination of a franchise agreement is governed by the provisions of the Contract Law. As noted in question 12.1, it is prudent to make clear that the agreement does not give rise to a commercial agency.

10 Labour Laws

10.1 Is there a risk that a franchisee or a franchisee's employees might be treated as the employees of the franchisor, so that the franchisor has vicarious liability for their acts and omissions? If so, can anything be done to mitigate this risk?

Cyprus law distinguishes a contract of service (employment) from a contract to provide services as an independent contractor or consultant. In determining whether a person is an employee or an independent contractor, all the circumstances of the relationship must be taken into account, including the degree of control over the individual's work activities, integration, ownership and the economic substance of the relationship, and not just the signed contract.

In order to mitigate the franchisor's risk from vicarious liability of the acts or omissions of the franchisee, it is advisable to insert an express term in the franchise agreement to the effect that the relationship between the franchisor and the franchisee is not one of employer and employee.

11 Currency Controls and Taxation

11.1 Are there any restrictions (for example exchange control restrictions) on the repatriation of royalties to an overseas franchisor?

Cyprus is a member of the Eurozone and both residents and non-residents, whether individuals or corporate bodies, may hold and manage assets and liabilities in any currency and in any country, including freely convertible and transferable balances with banks on the island. There is no distinction between nationals of Cyprus, nationals of other EU Member States, and third-country nationals.

Cyprus is an excellent location for franchisors to hold their intellectual property rights, as it offers attractive incentives and tax exemptions relating to income from intellectual property rights and proceeds from their disposal, known as an intellectual property box (“IP box”).

Four-fifths of the profit earned from the use of intangible assets (including any compensation for improper use) is disregarded for tax purposes. In addition, four-fifths of any profit resulting from the disposal of relevant intangible assets is disregarded for tax purposes (in practice, with proper structuring, profits on disposal of intangible assets can be completely sheltered from tax).

The net effect of the new scheme is that the rate of tax on income from the exploitation of intellectual property will be 2.5 per cent or less. Since there are no taxes on dividends paid to non-resident shareholders, a Cyprus company can be used to generate royalties under licensing or similar arrangements with third parties and distribute profits to its shareholders by way of dividends with minimal tax leakage.

11.2 Are there any mandatory withholding tax requirements applicable to the payment of royalties under a trade mark licence or in respect of the transfer of technology? Can any withholding tax be avoided by structuring payments due from the franchisee to the franchisor as a management services fee rather than a royalty for the use of a trade mark or technology?

There is no withholding tax on dividends, interest and royalties paid to non-residents apart from a 10 per cent withholding tax on royalties

(5 per cent in the case of films) arising from the use of intellectual property in Cyprus. This can be minimised by characterising payments appropriately in the franchise agreement.

11.3 Are there any requirements for financial transactions, including the payment of franchise fees and royalties, to be conducted in local currency?

No, there are no such requirements.

12 Commercial Agency

12.1 Is there a risk that a franchisee might be treated as the franchisor's commercial agent? If so, is there anything that can be done to help mitigate this risk?

Yes, franchise holders and distributors may sometimes be referred to as "agents" of the franchisor. Although such a person could be confused with an agent in that their obligations to their principal are similar to those of a commercial agent, a franchisee is generally regarded at common law as a purchaser for resale and, therefore, the more stringent protection afforded to commercial agents would not be applicable to a franchise relationship. In order to mitigate the risk the franchise agreement may expressly provide that the relationship between the franchisor and franchisee is not one of principal and commercial agent.

13 Good Faith and Fair Dealings

13.1 Is there any overriding requirement for a franchisor to deal with a franchisee in good faith and to act fairly according to some objective test of fairness and reasonableness?

Yes. All types of contract are subject to a standard of reasonableness and fairness.

14 Ongoing Relationship Issues

14.1 Are there any specific laws regulating the relationship between franchisor and franchisee once the franchise agreement has been entered into?

No, there no specific laws regulating the relationship between the franchisor and the franchisee once the franchise agreement has been entered into.

15 Franchise Renewal

15.1 What disclosure obligations apply in relation to a renewal of an existing franchise at the end of the franchise agreement term?

There are no statutory stipulations in this regard and this is a contractual matter.

15.2 Is there any overriding right for a franchisee to be automatically entitled to a renewal or extension of the franchise agreement at the end of the initial term irrespective of the wishes of the franchisor not to renew or extend?

No, there is no such right.

15.3 Is a franchisee that is refused a renewal or extension of its franchise agreement entitled to any compensation or damages as a result of the non-renewal or refusal to extend?

There are no statutory stipulations in this regard and this is a contractual matter.

16 Franchise Migration

16.1 Is a franchisor entitled to impose restrictions on a franchisee's freedom to sell, transfer, assign or otherwise dispose of the franchised business?

The franchisor is entitled to impose restrictions on the franchisee's freedom to sell, transfer or assign or otherwise dispose of the franchised business so long as these restrictions are reasonable and lawful under competition law and the Contract Law.

16.2 If a franchisee is in breach and the franchise agreement is terminated by the franchisor, will a "step-in" right in the franchise agreement (whereby the franchisor may take over the ownership and management of the former franchisee's franchised business) be recognised by local law, and are there any registration requirements or other formalities that must be complied with to ensure that such a right will be enforceable?

An automatic "step-in" right is not recognised and the franchisor will generally need to seek an appropriate court order to protect his interests.

16.3 If the franchise agreement contains a power of attorney in favour of the franchisor under which it may complete all the necessary formalities required to complete a franchise migration under pre-emption or "step-in" rights, will such a power of attorney be recognised by the courts in the country and be treated as valid? Are there any registration or other formalities that must be complied with to ensure that such a power of attorney will be valid and effective?

There is no specific legislation that regulates the formalities of a power of attorney or the inclusion of a power of attorney in a commercial contract, and the courts will have regard to the Contract Law and the general principles of common law regarding the execution of deeds. It is generally advisable that any power of attorney should take the form of an *addendum* constituting part of the commercial agreement. Where the identity of the attorney is not known at the outset of the agreement, and is merely described (for example, "any director of the franchisor"), the courts may deem that it is void and unenforceable on the grounds of uncertainty.



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