

# FRANCHISING IN BULGARIA

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This article offers a unique and practical overview of the laws and regulations which apply to franchising agreements in Bulgaria. The authors consider issues of contract, commercial, competition, intellectual property, tax and investment law. They further discuss the development of the franchising sector in Bulgaria as supported by the activities of the Bulgarian Franchise Association.

## GENERAL OVERVIEW

Currently, there are no franchise laws or specific regulations pertaining to this area in Bulgaria. A legal definition can be found in the supplementary provisions of the Corporate Income Tax Act and, within the meaning given by this act, “franchising” is the totality of industrial or intellectual property rights relating to trade marks, trade names, logotypes, utility models, designs, copyrights, know-how or patents, granted in return for a royalty, to be used for the sale of goods and/or the provision of services. The Income Taxes on Natural Persons Act provides that “franchising agreement” shall have the respective meaning as defined in the Corporate Income Tax Act.

A “healthy commercial law environment” is of paramount importance for franchising. Indeed, without this legal framework, franchising would not be able to function. A healthy commercial law

environment includes legislation on commercial contracts, adequate company law, including rules for joint ventures, and further, regulations regarding intellectual property rights in which companies can rely on the ownership rights of trademarks and know-how as well as on confidentiality agreements.

## LEGAL FRAMEWORK

The Bulgarian legal framework is very accommodating to foreign franchises. In general, no specific registration or governmental approval is required in order to establish a franchise enterprise. Franchisors must comply with the provisions of the Bulgarian Commercial Act. Bulgarian Law imposes no restrictions on repatriation of earnings, capital, royalties or interest. Intellectual property rights are both recognized and protected in Bulgaria.

Franchise arrangements are subject to a considerable number of laws and regulations in addition to the Bulgarian Commercial Act and intellectual property laws.

## Financial Investments

The Investment Promotion Act, last amended in 2008, was designed to encourage foreign investment. This Act provides for the equal treatment of foreign and domestic investors and allows for improved

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administrative services. It further includes an incentive system for investments and encourages the implementation of investment projects over a period of at least five years. It is this law that explicitly recognizes intellectual property and securities as foreign investments.

U.S. franchisors are further protected by the U.S.-Bulgaria Bilateral Investment Treaty of 1994, last amended in 2007. The treaty includes rights for U.S. investors such as national treatment and most favoured nation status, the right to make financial transfers freely and without delay, further, the Investment Treaty contains international law standards for expropriation and compensation and access to binding international arbitration.

### Intellectual property

Intellectual property rights are the basis upon which the franchise relationship is built. They are therefore of fundamental importance.

The Bulgarian legislation provides adequate and effective protection for intellectual property and for the acquisition and disposition of property rights. All laws related to intellectual property are harmonized with EU legislation, the Agreement on Trade-Related Aspects of Intellectual Property Rights and other international acts. Bulgaria is a member of the World Intellectual Property Organization and a signatory of the Paris Convention for the Protection of Intellectual Property. All intellectual property rights of any of the 171 contracting States to the Paris Convention, including the United States and most European countries, are equally recognized, protected and applicable both domestically and abroad.

### Copyright

The Copyright and Related Rights Act protects literary, artistic, and scientific works. The Act provides a full listing of protected works, including computer programs (which are protected as literary works). The use of protected work without the author's permission is generally prohibited. Since 2000 the Copyright and Related Rights Act has been revised in order to comply with EU- and

international legislation. The term for the protection of copyrighted work was extended from 50 to 70 years after the author's death. This prolonged protection has retroactive effect. Copyrights for films and other audio-visual works are protected during the life-time and for 70 years after death of the respective director, screenplay-writer, cameraman, or the composer. Other amendments to the Copyright and Related Rights Act enable copyright owners to file civil actions to suspend the activities of pirates; further, the amendments provide for confiscation of equipment and pirated materials; they enhance border control of pirated material and introduce a new neighbouring right for film producers and harmonize Bulgarian legislation with the EU Association Agreement.

The Copyright Office of the Ministry of Culture is responsible for copyright matters in Bulgaria. The National Film Center is responsible for enforcing intellectual property rights with respect to films and videos. Bulgarian legislation provides for criminal, civil and administrative remedies against copyright violation.

### Patents

The Patents and Utility Models Registration Act has been harmonized with EU Law as regards the application procedure for European patents and utility models. Bulgaria joined the Convention on the Granting of European Patents ("*European Patent Convention*") in 2002.

The independent Patent Office is the competent authority with respect to patent matters. Bulgarian patent law determines the application and examination procedures. Applications have to be directly submitted to the Patent Office and recorded in the state register. Compulsory licensing may be ordered under certain conditions: (1) the patent has not been used within four years of filing the patent application or three years from the date of issuance of the patent or (2) the patent holder is unable to offer a justification for not adequately supplying the national market.

Bulgaria grants the exclusive right to the use of inventions and utility models for 20 years starting

from the date of filing of the patent application. The term for the validity of a utility model registration is limited to four years starting from the date of filing of the application. It may be extended by two consecutive three-year periods, but the total term of validity may not exceed 10 years.

Inventions eligible for patent protection must be new and applicable to industrial applications and further involve some degree of innovation. The Patents and Utility Models Registration Act lists items which are not considered to be inventions. Utility models are also specifically defined in such Act.

Disputes arising from the creation, protection or use of inventions and utility models can be settled under administrative, court or arbitration procedures.

### **Trademarks**

The Marks and Geographical Designations Act was amended between 2005 and 2009 in order to comply with EU standards. This Act regulates the establishment, use, suspension, renewal and protection of trademarks as well as collective and certificate marks, and geographic designations.

The registration of a trademark is refused, or an existing registered trademark is cancelled, if the trademark constitutes a reproduction, an imitation or if there is a likelihood of confusion with an already registered or well-known trademark, as stipulated by the Paris Convention and the Marks and Geographical Designations Act. Applications for the registration of trademarks must be submitted to the Patent Office in compliance with established procedures.

The right of priority, regarding trademarks which do not differ substantially, is only granted to applications which are filed in compliance with the law. The right of priority can also be granted on the basis of a request made by a signatory to the Paris Convention or a member of the World Trade Organization. To exercise the right of priority, the applicant must file a respective request within six months commencing on the date of the original filing for registration of the trademark.

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The exclusive right for the use of a trademark starts with the date of submission of the application and is granted for ten years. Any requests for extension of the protection of the trademark must be filed during the last year of its validity, but not less than six months prior to its expiration. Protection is terminated if a trademark is not used for a period of five years.

Bulgarian legislation provides for criminal, civil and administrative remedies against all types of trademark violations. In Bulgaria, trademarks and service mark rights and rights for geographic designations are only protected upon their registration with the Bulgarian Patent Office or another international register which specially mentions Bulgaria. Protection does not evolve from “use in commerce” of a trademark.

### **Firm name**

Furthermore, the Commercial Act and the Commercial Registry Act grants the exclusive right for a firm's name to be used only by the entrepreneur who has registered it. In case of infringement, the interested party is free to seek an injunction and damages. The Commercial Act also obliges procurators, agents, assistants and representatives to protect trade secrets and the company's good standing.

### **Competition**

Competition Law may apply to the provisions of a franchise agreement which relate to the price that a franchisee should charge for offered products or services and to those provisions concerning exclusive rights which are granted to the franchisees under a franchise relationship and which could be

deemed as market sharing or as joint action between members of a network. However, it is difficult to ensure that the franchisee is given the best possible protection in order to be able to develop its territory, e.g. through exclusive territorial rights, and at the same time to ensure that the respective provisions of the franchise agreement do not infringe competition law. This should be taken into consideration when drafting franchise agreements. The Law on Protection of Competition allows business methods to be kept as commercial and production secrets.

### Taxation

Tax regulation is of considerable importance, not only because taxation issues are often decisive with respect to the corporate form which the parties will adopt but also with regard to the franchisor as regards its presence in the host country and the franchisee in relation to its establishment. Issues including the payment or withholding of taxes need to be regulated in franchise agreements.

### FRANCHISING DEVELOPMENT

Encouraged by the supportive commercial environment and the large market potential, franchising has recently experienced significant growth. Over the last five years the number of international franchise systems in Bulgaria has more than doubled. The first franchises and licenses in the country date back to the 1970s; the first contracts were signed with Hertz, Novotel and Sheraton.

Today franchising is present in many different sectors, including beverages, cosmetics, education, fast food, gas retail, hotels and real estate brokerage. Among the most popular international franchisors in the Bulgarian market are *Arexim, Bally, Benetton, Berlitz, Best Western, Century 21, Dunkin' Donuts, ERA, GNC, Golden Tulip, Hertz and Avis, Hill International, Hilton, KFC, McClean, McDonald's, Monsieur Bricolage, NEOSET, OMV, Pizza Hut, Radisson, Remax, Shell, Sheraton, Snelling Staffing, Superstore USA, Office 1, PMC Management and Wilson Learning*. Bulgarian-founded franchise systems have also emerged on the market, such as *Policontact*, a Bulgarian franchisor which conducts business in the employment services industry, or

*Happy*, another Bulgarian franchisor which owns the largest restaurant chain in the country and operates more than 20 domestic and several international outlets.

Despite the swift development of licensing and franchising in recent years, Bulgaria's franchise market is still largely untapped.

To date, no Bulgarian financial institutions have specialized in financing the development of franchising. However, banks, EU programs and special funds which support small and medium-sized business also provide credit financing for franchise projects. In this respect, the Bulgarian Franchise Association offers guidance on financing opportunities.

Franchise business is likely to be highly profitable in Bulgaria, due to the reasonable price of real estate, favourable wage rates for educated and skilled workers and strong market demand. The combination of a retail sector which is still developing, an underdeveloped service sector, strong local demand for products and services of consistently high quality and the large number of West European tourists who are familiar with the logos, brand names and trademarks of Western franchise companies, make the Bulgarian market attractive for franchise expansion.

### BULGARIAN FRANCHISE ASSOCIATION (BULFA)

BULFA is a non-governmental organization established in 1994. It is a member of the International Franchise Association in Washington, D.C. BULFA consists of professional consultants who are specialized in sales, advertising, development, privatization and the arrangement of seminars, support and management for the franchising industry. It assists interested parties with information concerning franchise opportunities and regulations and arranges venues for meetings with the Bulgarian franchising industry. BULFA organises seminars which deal with topical subjects, in particular regarding the internationalization of Bulgarian companies through franchising.

BULFA's work encompasses, in particular, the following topics:

- providing information regarding franchise possibilities in the Bulgarian market;
- assistance to foreign franchise companies by establishing contacts with potential master franchisors in Bulgaria;
- promotion of members' interests in franchising in Bulgaria;
- consulting with franchisees, assisting them in setting up franchises and acquiring rights to use trademarks and service marks of franchisors; and,
- assistance regarding obtaining financing and support in financing negotiations for franchise projects.

BULFA maintains a databank for research on regulations and practices in the local franchise sector, franchise concepts, financing opportunities, guidance for preparation of franchise agreements, and marketing plans.

Since 1994, BULFA has supported well-known U.S. and European franchise companies in their entry to the Bulgarian market through the sale of master franchises. It also has helped entrepreneurs to find suitable franchisees and to register franchisee companies with the governmental authorities.

The Association's priorities are to establish a venture capital fund for financing franchise projects and to provide online services for members and foreign franchisors in order to contribute to the development of the Bulgarian franchise market.

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## FRANCHISING AGREEMENT

As already stated above, Bulgaria still lacks experience regarding the franchise industry and has no specific regulations with respect to this area of business. Consequently, franchising associations as well as the codes of ethics adopted by these associations are of great importance for the development of the franchise sector. The Bulgarian Franchising Code of Ethics (“BFCE”) was adopted by BULFA and entered into force on June 7, 1994.

The BFCE was established in cooperation with the EU Commission in Brussels and according to the European Franchising Code of Ethics, which was first published in 1972. The Code of Ethics applies only to the members of BULFA.

Under Bulgarian law, franchising agreements are subject to the general rule of freedom of contract. In general, franchising agreements are bipartite and of a long term character (5 to 10 years).

The franchise agreement has to comply with the Bulgarian law, European community law and the BULFA's Code of Ethics.

The agreement should reflect the interests of the members of the franchised network in protecting the franchisor's industrial and intellectual property rights and in maintaining the common identity and reputation of the franchised network. All agreements and all contractual arrangements in connection with the franchise relationship should be written in or translated by a sworn translator into the official language of the country the individual franchisee is established in, and signed agreements should be given immediately to the individual franchisee.

The franchise agreement should set forth without ambiguity the respective obligations and responsibilities of the parties and all other material terms of the relationship.

The essential minimum terms of the agreement should be the following:

- (i) the rights granted to the franchisor;
- (ii) the rights granted to the individual franchisee;
- (iii) the goods and/or services to be provided to the individual franchisee;
- (iv) the obligations of the franchisor;
- (v) the obligations of the individual franchisee;
- (vi) the terms of payment by the individual franchisee;
- (vii) the duration of the agreement which should be long enough to allow individual franchisees to amortize their initial investments specific to the franchise;
- (viii) the basis for any renewal of the agreement;
- (ix) the terms upon which the individual franchisee may sell or transfer the franchised business and the franchisor's possible pre-emption rights in this respect;
- (x) provisions relevant to the use by the individual franchisee of the franchisor's distinctive signs, trade name, trademark, service mark, store sign, logo or other distinguishing identification;
- (xi) the franchisor's right to adapt the franchise system to new or changed methods;
- (xii) provisions for termination of the agreement;
- (xiii) provisions for surrendering promptly upon termination of the franchise agreement any tangible and intangible property belonging to the franchisor or other owner thereof.

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The BFCE defines franchising as a marketing system for goods and/or services and/or technology, which is based upon a close and ongoing collaboration between legally and financially separate and independent entrepreneurs, the franchisor on the one hand and its franchisees on the other hand, whereby the franchisor entitles franchisees to use its concept and at the same time imposes the obligation to conduct business in accordance with this concept.

The franchisee is entitled and obliged, in exchange for a direct or indirect financial consideration, to use the franchisor's firm name, and/or trade mark and/or service mark, know-how, business and technical methods, procedural systems, and other industrial and/or intellectual property rights, supported by the provision of commercial and technical assistance, within the framework and for the term of the franchise agreement, which is concluded between the two parties for this purpose.

The BFCE also considers that franchise agreements must comply with National Law, European Community Law, the Code of Ethics and any national regulations related thereto. Furthermore, the BFCE specifies the minimum terms of a franchise agreement (rights granted, goods and/or services to be provided, obligations, fees, terms of payment, duration and renewal of the agreement, provisions regarding the sale or transfer of the franchise business, use of firm name, trademarks, service marks, store signs, logos or other distinguishing identification).

A franchise agreement must reflect the interests of the members of the franchising network by protecting the franchisor's industrial and intellectual property rights and the common identity and the reputation of the franchising network. All agreements and all contractual arrangements in connection with the franchise relationship must be written in - or translated by a certified translator into - the official language of the country where the individual franchisee is established.

## FORMS OF FRANCHISING

All forms of franchising (distribution of products or service franchising) can be used in Bulgaria. No specific requirements or restrictions exist regarding foreign franchisors in Bulgaria. The prevailing forms of franchising are direct (unit) franchising, master franchising, regional development, joint ventures, and the establishment of affiliates. Due to the relatively small size of the Bulgarian market, foreign franchisors usually establish master franchises for an entire region, i.e. the Balkans or Eastern/South Eastern Europe.

## CONCLUSION

Although franchising is a relatively new concept for the Bulgarian business community, the Bulgarian legal system accommodates franchise agreements. No specific registration or government approval is required in order to establish a franchise enterprise and the market potential in Bulgaria currently presents excellent prospects for the establishment of new franchise systems.

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