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ANALYSIS OF PROPOSED FRANCHISE LAW OF KAZAKSTAN

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A

Analysis of Proposed Franchise Law of Kazakhstan.

A. Introduction.

The legislature of Kazakhstan is currently considering adopting legislation specific to franchising.¹ The following is an analysis of the franchise legislation proposed by the legislature of Kazakhstan. The provisions of the legislation, taken as a whole, appear more restrictive than will be conducive to the establishment of franchise systems by franchisors accustomed to a free-enterprise economy and, particularly, those who are accustomed to a common law legal system. A number of the provisions undertake to regulate the relationship between the parties only in the absence of an agreement by the parties with respect to a particular matter. We suggest this approach should be taken with respect to virtually all provisions, rather than undertaking to override the agreement of the parties, freely arrived at, by legislative prescription. This will likewise diminish the view of contract law, as we understand will be the case in Kazakhstan, that what is not permitted by a specific law is prohibited. We believe there should be a presumption, provided by the law, that the parties can agree among themselves, and the statute should cover only those matters considered either so important by the legislature that the parties' power to contract should be overridden or to fill in gaps where the parties have not agreed.

We offer our critique without knowledge of the other laws of Kazakhstan already in place in, or proposed for, its commercial and civil codes. We suggest that a law on franchising should only fill gaps related to the franchise relationship not otherwise covered by trade regulation, product liability, consumer protection, intellectual property, and securities laws.

In commenting, we have had some difficulty with the translation and have assumed some interpretations (indicated in the text) which may be at odds with the language from which the franchise law has been translated. We hope we have made appropriate allowance for what may have been lost in translation as well as the fact that it is necessary to view this legislation in a civil law context.

B. Proposed Franchise Law of Kazakhstan.

1. Article 946. Definition of a Franchise Licensing Agreement.

Article 946 indirectly defines franchising by identifying the basic elements of a "franchise license agreement." These appear to be use of a trademark and know-how belonging to the franchisor in exchange for a payment by the franchisee. While the language is quite different from state and federal law in the United States, the effect is the same. We suggest, however, that without appropriate exceptions, the definition will be too broad, applying the law to virtually all wholesale arrangements in the country.

^{1/} Such legislation appears, in large part, to be derived from the Russian law regulating franchising, which became effective in March, 1996.

We suggest the following in order to limit the regulation: (1) the use of the marks should relate to substantially all of the business of the franchisee; (2) payments for goods for resale at a bona fide wholesale price should be excluded from the type of "remuneration" which is covered by the definition; (3) payments of de minimis amounts should be excluded; and (4) when the payment is made for a number of things, e.g., for equipment provided by the franchisor or for advertising, the statute should provide some standard for determining whether the payment is for the marks and know-how or the other goods and services supplied under the franchise agreement.

In addition, Article 946 specifically identifies "protected commercial information" as one of the exclusive rights to be granted to a Licensee. It is unclear what is meant by "protected" and whether the grant and use of "protected commercial information" is required in order to constitute a franchise. Note that in the U.S., although franchisors provide franchisees with commercial information which could be classified as "protected", e.g., "trade secrets," this does not appear in the definition of a franchise relationship under state law or federal regulations. Franchisors ordinarily provide information which is not afforded any protection or is "protected" only to the extent that the disclosure of such information may be prohibited pursuant to a confidentiality clause in the franchise agreement. Therefore, including "protected commercial information" as a definitional element of a franchise license agreement may unnecessarily create uncertainties.

Know-how should be of substantial importance to the business of the franchisee or the contract should not be a franchise license agreement.

Based on the foregoing analysis, it is suggested that the definition of a franchise licensing agreement be revised to more accurately reflect those elements which distinguish a franchise agreement from other similar agreements.

2. Article 947. The Franchise License Agreement Form.

This Article provides that "[a] franchise license agreement is executed in writing." The purpose of this provision is unclear.

This Article could be interpreted as providing that either (i)(A) only a written franchise license agreement is subject to the franchise license law; and (B) an oral franchise license agreement, although valid and legally binding on the parties thereto, is exempt from regulation by the franchise license law; or (ii)(A) only a written franchise license agreement is valid and legally binding on the parties thereto; and (B) an oral franchise license agreement is null and void. We suggest that Article 947 be revised to resolve this ambiguity covering both written and oral agreements.

3. Article 948. A Licensor's Duty.

In order to maintain the uniformity of a franchise system, the franchisor normally agrees to assume certain obligations. Typically, the obligations of the franchisor include the transfer of information that makes the franchise a valuable business commodity, providing marketing expertise, and training assistance. We understand Article 948 to impose two broad duties on the Licensor: (i) to provide technical and commercial instructions in written form and other information necessary to enable the Licensee to exercise the rights granted to the Licensee under the franchise license agreement; and (2) to consult with and advise the Licensee on the issues.

The obligation to provide manuals and other information is commonly assumed by Franchisor. However, the obligation to "brief" the Licensee on the issues connected with the execution of Licensee's rights under the franchise license agreement is unclear and susceptible of various interpretations. Consequently, this obligation should be revised to more clearly define this obligation. This may be a problem of translation. In English, perhaps the words "training" and "consultation" would be more appropriate than the word "brief." Note that Article 948 is interpreted as requiring the Licensor to assume at least the obligations listed. If this interpretation is incorrect, this Article should be revised to clearly set forth the drafters' intent.

4. Article 949. A Licensee's Duties.

We understand Article 949 to impose the following duties on a Licensee: (i) use of a Licensor's trade name in the manner prescribed in the franchise license agreement; (ii) to provide Licensor access to Licensee's business; (iii) to provide Licensor with documentation requested by Licensor; (iv) to follow Licensor's instructions with respect to the business; (v) to keep Licensor's know-how, production secrets, and other commercial information confidential; and (vi) to inform customers that Licensee is operating its business as a franchise and is independent from the owner of the trademark. All of these duties are obligations commonly imposed on franchisees by franchisors. It is not, however, clear whether the intent of this Article is to limit the Licensee to these specific duties or whether the list of duties is merely descriptive. As with Article 948, this Article is interpreted as requiring the Licensee to assume at least the obligations listed. If this interpretation is incorrect, Article 949 should be revised to clearly set forth the drafters' intent.

Franchise agreements ordinarily impose a number of additional duties and obligations upon franchisees. Among these duties are the use of standardized trade dress, attendance at mandatory training programs, the purchase of certain goods only from approved suppliers, adherence to a franchisor's operating manual which sets forth the standards for the operation of the franchise business, and an obligation not to compete during the term of the agreement and for some stipulated period after, an obligation which is addressed in the discussion of Article 950. If Article 949 intends to be exhaustive of Licensee's obligations, it should be expanded.

Although the duties listed in Article 949 are unobjectionable, there are numerous other duties, some of which are referred to above, which are far more critical to the successful

operation of the franchise, which are not listed in Article 949. An express provision which permits the parties "to impose such additional duties on the Licensee as the parties may agree" would be preferable to expanding the current list. Therefore, we suggest that Article 949 be revised to permit the parties to impose additional duties on the Licensee.

5. Article 950. Restrictions.

Section (1) of Article 950 sets forth certain restrictions which may be imposed upon the actions of Licensor and Licensee, respectively, all of which appear to relate to competition (excluding the last phrase of Section (1)4), and are restrictions which otherwise may be considered illegal restraints of trade. We have interpreted Section (1) as providing that, pursuant to a franchise license agreement, a Licensor may (i) agree not to issue other similar franchise licenses to be used within a Licensee's territory or agree to abstain from direct independent operation of a similar activity within the territory assigned to Licensee.

With respect to the Licensee, Section (1) has been interpreted to permit Licensee to: (i) agree not to compete with the Licensor within the territory covered by the franchise license agreement with respect to the business activity conducted by the Licensee pursuant to the franchise license agreement; (ii) waive its right to obtain other franchise licenses from an existing or future competitor of Licensor; and/or (ii) agree to permit Licensor to prescribe the location of the premises, as well as the interior and exterior design thereof. Assuming this interpretation is correct, all of the foregoing restrictions are common to franchising arrangements. However, the restriction regarding the Licensee's agreeing not to compete with the Licensor "within the territory" should be revised to permit the Licensee to agree not to compete with Licensor on a worldwide basis during the term of the franchise license agreement, and to agree not to compete with the Licensor within the territory and a reasonable area outside thereof for a reasonable period of time after the termination, for whatever reason, of the franchise license agreement.

It is recommended that the competition laws of Kazakhstan be reviewed to determine whether any of these laws conflict with the provisions of Article 950. In the event of a conflict, Article 950 should be amended to provide that the conduct permitted by this Article will be exempt from the competition laws, if agreed to by the parties.

Section (2) identifies several impermissible restrictions. Section (2)1 prohibits the Licensor from prescribing the actual price at which goods or services are to be sold by the Licensee² or setting minimum and maximum prices. Such prohibitions against price-fixing are basic to anti-trust/competition laws in the United States and the EU. Section (2)2 prohibits the Licensor from limiting the Licensee's business to only a prescribed customer group or group of

^{2/} It is assumed that the references to "Licensor" and Licensee" in Section (2)1 of Article 950 are either translation or typographical errors. Consequently, "Licensor" should be substituted for "Licensee" and vice versa.

buyers within the Licensee's territory. In the U.S., this prohibition, if we understand it correctly, is rare in franchise arrangements.³

6. Article 951. A Licensor's Liabilities for Requirements Placed On a Licensee.⁴

The translation of Article 951 states that the Licensor "bears subsidiary responsibility" for the requirements placed on a Licensee with respect to the quality of goods or services sold by a Licensee under the franchise license agreement. We interpret this to mean that, as in product liability laws in many countries, the Licensor may be liable for injuries resulting to the Licensee's customers. However, it remains unclear for what cause of action Licensor is to bear "subsidiary responsibility." Moreover, we are uncertain whether this liability is strict or subject to a negligence standard. In addition, Article 951 does not identify the party which bears "primary responsibility." We assume this is the Licensee, but remain uncertain as to the liability standard.

Our overriding concern about Article 951 is the imposition of any liability, whether primary or otherwise, on the Licensor, which presumably arises out of the actions of the Licensee. Holding the Licensor liable for the actions of the Licensee is contrary to one of the basic principles of franchising, i.e., the franchisor and the franchisee are independent business entities. Of course, if the Licensor negligently instructs the Licensee or negligently prescribes equipment or materials which injure customers, Licensor should be liable.

This Article carries the meaning, as we interpret it, that, at least with respect to customers, the Licensee is the Licensor's agent. Under a traditional franchise agreement, the parties normally agree that the franchise agreement does not create a fiduciary relationship and that the agreement is not intended to constitute or appoint either party as agent, legal representative, subsidiary, joint venturer, partner, employee or servant of the other for any purpose whatsoever. In addition, the franchisor routinely disclaims any liability for the acts of the franchisee in the operation of the franchise. As between the parties, their agreement is usually upheld.

Strict liability of the Licensor in connection with goods and/or services provided by a Licensee under the Licensor's marks is not a feature of U.S. law and, while proposed many years ago, remains unenacted in the European Union.

^{3/} Based on the analysis of Article 948, Article 950 presents an exhaustive list of permissible/impermissible restrictions. If this is not the drafters' intent, we suggest the Article be revised accordingly.

^{4/} We assume that the use of "Licensor" and "Licensee" in this Article, including the heading, is either a typographical or translation error. Consequently, "Licensee" should be substituted for "Licensor" and vice versa.

7. Article 952. A Franchise Sub-License.

We interpret Section 1 of Article 952 to permit the parties to agree that the Licensee has the right to sublicense some or all of the rights granted to Licensee under the franchise license agreement.⁵ However, the translation suggests some uncertainties. As an example, Section 1 appears to state that the franchise license agreement may provide that a Sublicensee's right to use such rights is subject to conditions agreed to with the Licensor, or "stated by the Agreement." It is not clear with whom the Licensor is to agree regarding said conditions, whether it is the Licensee or the Sublicensee, nor is it clear in which "Agreement" these conditions may be contained. By making a distinction between conditions agreed to with the Licensor and conditions set forth in "an Agreement", it appears as if the Licensor may agree to conditions which are neither set forth in the franchise license agreement nor in any other writing. We suggest that this Article be revised to provide that unless otherwise provided in the franchise license agreement, the use of any and all rights granted to a Sublicensee will be subject to the conditions set forth in the franchise license agreement.

We interpret Section 2 as permitting the Licensor to set forth in the franchise license agreement a fixed time period during which a Licensee must establish a specific number of Sublicensees and providing that for this purpose, a Licensee need not assign a territory to a Sublicensee.⁶ Although it is in a Licensor's best financial interest to set a time by which a Licensee must issue a certain number of Sublicenses, i.e., execute a certain number of franchise sublicense agreements, a more important concern of a Licensor is the Licensor's ability to prescribe the date by which the subfranchised businesses will be operational. Therefore, Section 2 should be revised to include permitting the Licensor to provide in the franchise license agreement (i) the date or dates following the execution of the franchise license agreement by which the Licensee must execute a set number of franchise sublicense agreements and/or, (ii) the date by which the subfranchised businesses must be developed and operating.

Section 3 appears to provide that the terms of the "basic agreement" are, in effect, incorporated into the franchise sublicense agreement, unless otherwise indicated by the franchise sublicense agreement and/or the basic agreement.⁷ This suggests, unless prohibited by the

^{5/} In general, subfranchising presents a potentially useful technique for bringing foreign franchises into Kazakhstan by offering foreign franchisors the option of shifting the principal responsibility for franchise development to a master franchisee.

^{6/} It is assumed that the reference to "Licensor" in Section 2 is a translation or typographical error. Consequently, "Licensor" should be replaced with "Licensee."

^{7/} For purposes of this analysis, it is assumed that the "basic agreement" referred to is the franchise license agreement.

franchise license agreement, the Licensee and Sublicensee can agree in the franchise sublicense agreement that some or all of the terms of the franchise license agreement will not apply to the franchise sublicense agreement. This result would be unacceptable to a Licensor because the Licensor could effectively lose total control over the actions of the Sublicensee.⁸ Therefore, we suggest the presumption be reversed and that this Section be revised to provide that, unless otherwise stated in the franchise license agreement, the franchise sublicense agreement is subject to the terms and conditions of the franchise license agreement; and, in the event of a conflict, the terms and conditions of the franchise license agreement control.

8. Article 953. Dependency of a Franchise Sublicense on the Basic Agreement Between a Licensor and Licensee.

We understand this Article to deal with the term of the franchise sublicense agreement. Section 1 provides that the term of the franchise sublicense agreement cannot exceed the term of the "basic" (franchise license) agreement. This is a standard provision of franchise agreements. Section 2 provides that upon termination of the franchise license agreement, all franchise sublicense agreements terminate. We interpret this to mean expiration because termination appears to be covered in Article 957.

9. Article 954. Particularities of Relations Between a Licensor, a Licensee and a SubLicensee.

We interpret Section 1 as providing that, unless the franchise license agreement provides otherwise, in the event of an early termination of the franchise license agreement, Licensee's rights and obligations under a franchise sublicense agreement are assigned to the Licensor on the terms of the franchise sublicense agreement. In other words, we interpret this Section as providing that if the franchise license agreement does not prohibit the assignment of Licensee's rights and obligations under the franchise sublicense agreement to Licensor, or does not provide that the assignment of said rights and obligations shall occur as set forth in the franchise license agreement, the rights and obligations are to be assigned to the Licensor in accordance with the franchise sublicense agreement. Note that, as this Section has been interpreted, a Licensor's failure to address this issue in the franchise license agreement can result in Licensee's rights and obligations being assigned to Licensor pursuant to an agreement to which Licensor is not a signatory. Note also that Section 1 does not provide for the situation where both the franchise license agreement and the franchise sublicense agreement are silent with respect to the assignment of Licensee's rights and obligations under the franchise sublicense agreement. Arguably, said assignment would not be permitted if not provided for in either agreement. Consequently, we suggest that Section 1 be revised to provide that (i) in the event of an early

⁸ Normally, the franchisee agrees in the franchise agreement that when entering into subfranchise agreements with subfranchisees, the franchisee will use the form of agreement agreed upon between the franchisor and the franchisee, subject to the right of the franchisor and the franchisee to mutually agree upon changes thereto.

termination of the franchise license agreement, Licensee's rights and obligations under any and all franchise sublicense agreements will be assigned to the Licensor, in accordance with the franchise license agreement, unless the franchise license agreement otherwise provides, and (ii) in the event that the franchise license agreement does not provide for such assignment, the franchise sublicense agreement will automatically terminate.

Under Section 2, a Licensee "bears subsidiary responsibility" for the "harm done" to the Licensor as a result of Sublicensee's actions, "if any other different conditions be stipulated by a franchise license agreement." This Section raises several concerns. First, as with Article 951, we do not understand the term "subsidiary responsibility." Does this mean that the Licensee is to bear subsidiary responsibility only if the Sublicensee fails to pay all damages? In addition, as translated, the phrase "if any other different conditions be stipulated by a franchise license agreement" is susceptible of two interpretations: (i) unless the franchise license agreement provides otherwise; or (ii) notwithstanding anything provided in the franchise license agreement to the contrary. This Section also fails to identify which party bears "primary responsibility" to Licensor. Consequently, this Section needs to be revised to resolve these issues.

Note that Article 954 does not address the "responsibility" of the Licensee and/or the Licensor for the requirements placed on a Sublicensee with respect to the quality of goods sold, or services provided by the Sublicensee.⁹

10. Article 955. Maintaining of a Valid Agreement with a Changed Trade Name.

We interpret this Article to provide that in the event that a Licensor changes its trade name, the Licensee is permitted to cancel the franchise license agreement and obtain compensation. Alternatively, if a Licensee chooses not to cancel the franchise license agreement, he is entitled to a reduction in payments due to Licensor¹⁰ related to such name change.¹¹ There are several problems with this Article. First, there is no indication that the Licensee must suffer actual damages before being permitted to cancel the franchise license agreement. Second, there is no limitation on the time by which the Licensee must cancel the franchise license agreement. As written, it appears the Licensee could cancel the franchise license agreement at any time after Licensor changes the trade name. Third, there is no

⁹ See Article 951, *supra* at p. 5 (a Licensor bears subsidiary responsibility for the requirements placed on a Licensee with respect to the quality of goods sold or services provided by a Licensor under a franchise license agreement.)

¹⁰ It is assumed that the term "balanced reduction" means that the Licensee may seek to offset the amount due from Licensee to Licensor under the franchise license agreement in an amount equal to the "damage" suffered by Licensee as a result of the subject change made by Licensor.

¹¹ This Article appears to be based on the assumption that a change in trade name will have a negative impact on the Licensee's business which is not necessarily the case.

indication as to how damages are to be measured. For example, in the event that a Licensee cancels a franchise license agreement immediately after the trade name change, what damages would the Licensee be permitted to recover? In the event that the Licensee chooses not to cancel the franchise license agreement, by what amount would the Licensee be permitted to reduce the amount due Licensor? While, practically speaking, the situation addressed in Article 955 rarely occurs and does not raise serious concerns, if this Article is preserved it should be revised to resolve the issues presented.

11. Article 956. Maintaining of a Valid Agreement with One or Several Exclusive Rights Changed.

This Article appears to permit the Licensor, without affecting the validity of the franchise license agreement, to unilaterally change the manner in which the Licensee is permitted to use one or more of the rights granted to the Licensee under the agreement. However, in the event of a change, the Licensee has the same options as under Article 955; Licensee can (i) cancel the franchise license agreement and seek damages; or (ii) continue operating under the franchise license agreement and reduce the amount paid to Licensor thereunder by the amount of damages suffered as a result of such change. The concerns raised by Article 955 are also applicable to this Article.

In addition, it can be argued that Article 956 limits the Licensor's ability to change crucial documents such as manuals or other information provided to Licensee under the franchise license agreement. Such a situation would be unacceptable to Licensors as interfering with their right to adapt the franchise system to commercial and competitive changes. Consequently, we believe Article 956 should acknowledge that the parties may agree that the know-how may be revised by the Licensor without liability to the Licensee.

12. Article 957. Consequences of Cessation of an Exclusive Right of Use.

We interpret this Article as providing that in the event that the Licensee's right to use a right granted to it under the franchise license agreement terminates, for whatever reason, prior to the termination of the franchise license agreement, the franchise license agreement remains valid with respect to provisions unrelated to the terminated right. For example, in the event that a Licensee were required to pay royalties based on the use of a now-terminated right, it is assumed that this royalty obligation would no longer be valid. In addition, upon termination of the right to use an exclusive right, the Licensee is entitled to call for a reduction in the amount payable by Licensee to Licensor under the franchise license agreement, unless otherwise set forth in "an agreement."¹² Note the distinction between Articles 955 and 956, and 957. Under Articles 955 and 956, the Licensee has the absolute right to either cancel the franchise license agreement and seek damages, or to seek a reduction in remuneration payable to the Licensor;

¹² It is assumed for purposes of this analysis that this reference to "an agreement" is a translation error and that the proper reference is to the franchise license agreement.

whereas, under Article 957, Licensee is not permitted to cancel the franchise license agreement and the Licensee's right to seek a reduction in the amount payable to the Licensor is not absolute. Licensee may be denied this right by agreement in the franchise license agreement.

13. Article 958. Termination of a Franchise License Agreement.

Section 1 of this Article provides that franchise license agreements containing a fixed termination date may be cancelled as set forth in the Kazakhstan Civil Code (the "Code"). This raises a concern regarding the interaction of the Code and the terms contained in the franchise license agreement regarding termination. Only a review of the Code, which is beyond the scope of this analysis, will resolve this concern. In the event the Code conflicts or is inconsistent with Article 958, Article 958 should be revised to provide that, with respect to a franchise license agreement containing a fixed termination date, unless otherwise provided for therein, said agreement shall be cancelled in accordance with the Code. This also raises the question of whether cancellation is a sole remedy.

Section 2 permits either party "to abandon ... the permanent franchise license agreement" upon providing the other party six months notice prior to such termination, unless a longer notice period is specified in the franchise license agreement.¹³ Our problem with this Section may be related to translation. It is assumed that the word "permanent" suggests a franchise license agreement with no fixed termination date.¹⁴ If it is the intent of the drafters that Sections 1 and 2 apply to fixed term and perpetual term franchise license agreements, respectively, this distinction should be more clearly indicated.

Section 2 also raises concerns regarding the interaction of Section 2 and the franchise license agreement. For instance, Section 2 could be interpreted as permitting termination by either party, with or without cause, regardless of what is contained in the franchise license agreement to the contrary, because, by its terms, this Section only appears to require notice. Consequently, we believe the relationship between Section 2 and the franchise license agreement should be clarified.

14. Article 959. Succession Under A Franchise License Agreement.

Section 1 appears to make the rights and obligations under the franchise license agreement freely assignable. Note that both the Licensor and Licensee are permitted to assign

¹³ It is advisable to require that the required notice be in writing.

¹⁴ This assumption is supported by a reading of a comparable provision in the Russian Civil Code wherein the word "perpetual", which more clearly suggests no fixed termination date, appears to have been used instead of the word "permanent". Also, if Section 2 were not assumed to apply only to a franchise license agreement with no fixed termination date, it would be render Section 1 superfluous.

any or all of their respective rights and obligations to a third party without the approval of the Licensee or Licensor, respectively. The ability of Licensees to assign freely any or all of their rights and obligations under the franchise license agreement is of particular concern to a Licensor because the Licensor has no ability to control the individual or entity with whom it will be closely identified after assignment. The Licensor may be forced to accept a Licensee who may not meet the Licensor's standards and/or might be a competitor of Licensor. Therefore, we suggest that this Section be revised to provide that either party may assign its rights and obligations under the franchise license agreement in accordance with the applicable terms thereof, and in the absence of any such terms, the rights and obligations should be freely assignable.

Section 2 provides that upon the death of the Licensor, his rights and obligations under a franchise license agreement are transferred to his legal successor on the condition that such successor is registered or will register his business within the six-month period immediately following the death of Licensee.¹⁵ Failure to so register will result in the automatic termination of the franchise license agreement. In the event that the legal successor is not properly registered on the date of Licensee's death, the rights and obligations of the Licensee are to be assumed and executed by an authorized trustee, appointed by a notary in accordance with the established procedure, until the earlier of: (i) the registration of the Licensee's legal successor; or (ii) the expiration of the six months immediately succeeding the death of the Licensee.

As under Section 1 regarding assignments, upon the death of the Licensee, the Licensor has no ability to control the Licensee's successor. Consequently, we believe this Section should also be revised to provide that upon the death of the Licensee, the rights and obligations of the Licensee will be transferred to his legal successor. However, if the franchise license agreement so provides, such transfer will occur only upon satisfaction of conditions and standards set forth in the franchise license agreement. Failure of the legal successor to meet the conditions and standards would be followed by a period in which the rights and obligations might be assigned (sold) to third parties.

C. Conclusion.

Assuming all is prohibited unless permitted, there are substantial gaps in the proposed legislation. For example, it fails to address the acceptable method(s) by which a Licensor may be compensated under the franchise license agreement, a critical omission. In addition, there are numerous other issues which are traditionally addressed in franchise agreements which the proposed legislation fails to address, e.g., a Licensee's obligations upon the termination or expiration of the franchise agreement, post-term competition, collection or use of funds for advertising, successful completion of training, maintenance of adequate insurance coverage, and methods of recordkeeping and accounting. We are also concerned about the context of these

^{15/} This implies that the Licensor is not permitted to terminate the franchise license agreement upon the death of the Licensee.

Sections in the Code, in particular with respect to the parties who may seek redress for harm from failure to adhere to these provisions, whether harm must be shown, how monetary remedies (if any) are to be measured, and whether any actions to be brought are limited by time. It should be fully understood that franchise agreements are contracts covering substantial periods of time, during which they remain executory on both sides.

A poorly drafted statute can provide more confusion than guidance, thereby discouraging franchisors from franchising. Consequently, the legislature of Kazakhstan should carefully review the draft legislation and weigh the advantages and disadvantages of including franchise law in their Civil Code. In the event that the legislature chooses to enact franchise legislation, a serious attempt should be made to address the issues raised in this analysis prior to the adoption of such legislation.

CHAPTER 48. A FRANCHISE LICENSE**Article 946. Definition of a Franchise License Agreement**

1. Under a franchise license agreement one party (a package Licensor) undertakes to furnish another party (a package Licensee) for the remuneration with a package of exclusive rights (a license package), including, in particular, the right to use a Licensor's trademark and protected commercial information, as well as other objects of exclusive rights (a trademark, a service mark, a patent, etc.), provided by the agreement, in a Licensee's operation.
2. A franchise license agreement stipulates for the use of a license package, a Licensee's business reputation and commercial experience to a certain extent (in particular, with determination of the minimum and/or maximum extent of use), with or without the indication of the territory of use as applied to the certain area of activity (distribution of goods, received from a legal owner or a user of a product, execution of works, implementation of other trade operations, rendering of services).

Article 947. The Franchise License Agreement Form.

A franchise license agreement is executed in writing.

Article 948. A Licensor's Duties

A Licensor commits itself:

to provide a Licensee with the technical and commercial documentation, as well as other information, required by the Licensee in order to exercise the rights, extended to it under the Agreement, as well as brief a Licensee on the issues, connected with the execution of these rights.

An Agreement may stipulate for other Licensor's duties.

Article 949. A Licensee's Duties

A Licensee commits itself:

1. to use in frames of activities, stipulated by the Agreement, a Licensor's business name in the manner, stated in the agreement;
2. to provide a Licensor with the right to enter its production area, to provide a Licensor with the requested documentation and assist in obtaining information, necessary to exercise control over correct use of the granted exclusive rights;
3. to follow all instructions and directions of a Licensor, referring to the nature, ways and terms of exclusive rights, granted to it;
4. not to disclose a Licensor's know-how, production secrets and other confidential commercial information, obtained from it;

- 5 to inform buyers (customers) in the most OK manner, that they use a business name, a trademark, a service mark and/or other means of individualization on the basis of a Franchise License Agreement.

Article 950. Restrictions

- 1) A franchise license agreement may stipulate for restrictions, namely:
 1. a Licensor commits itself not to issue other similar franchise licenses to be used within a Licensee's territory or to abstain from direct independent operation within its territory;
 2. a Licensee commits not to compete with the Licensor within the territory, covered by a franchise license, with respect to business activity, accomplished by a Licensee with the use of obtained exclusive rights;
 3. a Licensee waives to obtain other franchise licenses from a Licensor's existing or potential competitors;
 4. a Licensee commits itself to agree with a Licensor on location of premises, used in order to exercise exclusive rights, granted on the basis of the Agreement, as well as their interior and exterior design.
- 2) Restrictions of a franchise license, permitting:
 1. a Licensee to fix a price for goods, sold by a Licensor, or charges for executed works (provided services), or to set lower or upper price limits;
 2. a Licensee to sell goods, execute works or provide services to an exclusive customer group or exclusive buyers, located (residing) within the territory, defined by the Agreement,

are considered invalid.

Article 951. A Licensee's Liabilities For Requirements, Placed On a Licensor

A Licensee bears subsidiary responsibility for requirements, placed on a Licensor with respect to the quality of goods (works, services), sold (executed, provided) by a Licensor under a franchise license agreement.

Article 952. A Franchise Sub-License

1. A franchise license agreement may stipulate for a Licensee's right to allow other individuals or citizens, registered as legal entities, to use all or some of the exclusive rights subject to the conditions, agreed with a Licensor or stated by the Agreement.
2. Under the conditions of a franchise agreement a Licensor may be bound to issue within a definite time frame a certain amount of sub-licenses with or without indication of the territory.

- 3 Franchise sub-license agreements are subject to the terms of a basic agreement between a Licensor and a Licensee, if no other terms are stipulated by the above mentioned agreements.

Article 953. Dependency of a Franchise Sub-license on the basic agreement between a Licensor and a Licensee.

1. A franchise sub-license agreement can not be made for a period of time, surpassing the valid term of the basic agreement between a Licensor and a Licensee.
2. Cessation of a franchise license agreement terminates all other franchise sub-license agreements.
3. Should the basic agreement between a Licensor and a Licensee be rendered invalid on grounds, stipulated by legislative acts, all other franchise sub-license agreements will be rendered invalid.

Article 954. Particularities of Relations Between a Licensor, a Licensee and a Sub-Licensee

1. Should any other different conditions be stipulated by a franchise license agreement in case of its pre-schedule cessation, a Licensee's rights and obligations are assigned to a Licensor in accordance with a franchise sub-license agreement.
2. A Licensee bears subsidiary responsibility for the harm, done to a Licensor by Sub-Licensees' actions, if any other different conditions be stipulated by a franchise license agreement.

Article 955. Maintaining of a Valid Agreement With a Changed Trade Name

Should a Licensor change its trade name, a franchise license agreement remains valid with respect to a Licensor's new trade name, if a Licensee will not claim for a cancellation of an agreement and compensation for damages. If an agreement remains valid, a Licensee is entitled to call for a balanced reduction of remuneration, due to a Licensor.

Article 956. Maintaining of a Valid Agreement With One Or Several Exclusive Rights Changed

Should a Licensor change one or several exclusive rights of use, a franchise license agreement remains valid with respect to a Licensor's new exclusive rights, if a Licensee will not claim for a cancellation of an agreement and compensation for damages. If an agreement remains valid, a Licensee is entitled to call for a balanced reduction of remuneration, due to a Licensor.

Article 957. Consequences of Cessation Of An Exclusive Right of Use

Should a term of validity of any exclusive right, included into a package of rights, assigned under the agreement, expire during the term of validity of a franchise license agreement, or be terminated on other grounds, the agreement remains valid except for provisions, related to a terminated right, and a Licensee, if nothing else is stipulated by an agreement, is entitled to call for a balanced reduction of remuneration, due to a Licensor.

Article 958. Termination Of A Franchise License Agreement

1. A franchise license agreement, concluded with the indication of its term of validity, may be cancelled in accordance with the provisions of this Code.
2. A party under this agreement has the right to abandon to the permanent franchise license agreement upon the condition of notifying another party six months prior, if the agreement does not stipulate for a longer term of a notice.

Article 959. Succession Under A Franchise License Agreement

1. Assignment to another person of any exclusive right, included into a license package, is not a reason for changing or terminating an agreement. The new legal owner enters into the agreement in the part of rights and duties, related to the assigned exclusive right.
2. In the event of the death of a Licensor-person his rights and obligations under a franchise license agreement are transferred to a legal successor, provided that the latter registered or will register his business during six months beginning from the day of coming into a legacy. Otherwise the agreement will be terminated.
Until the successor obtains rights and obligations or registers his business, control over a license package is executed by an authorised trustee, appointed by a notary in accordance with the established order.