European Commission

LATIN AMERICA
IP SME HELPDESK

FACTSHEET



# Franchising in Brazil


## 1. Franchises as a business model

A franchise is an agreement between two parties, in which one party (the franchisor) grants another one (the franchisee) the right to use its trade mark or trade name (and other IPRs), as well as certain business processes to produce and market a good or a service according to certain specifications.

Many EU SMEs choose to open franchises as their sole business line or to combine it with other business lines. The Brazilian market has also acknowledged these trends and the number of franchises has significantly increased in the last years.

| | 2018 | 2019 | 2020 |
|---|---|---|---|
| Turnover (€ billions) | 27,94 | 29,85 | 6,64 |
| Units | 153,704 | 160,958 | - |
| Networks | 2887 | 2918 | - |
| Employment | 1,299,145 | 1,358,139 | 1,361,795 |

Source: Brazilian Franchise Association

The franchising scenario in Brazil shows stable growth in this country and it represents an attractive business model through which to enter the Brazilian market, depending on the activity of the company. Indeed, many European companies have chosen franchising as a way of expanding their business or entering the Brazilian market. For example, Instituto L´Oréal Professionnel or L'Occitane au Brésil, which, as of 2018, has approximately 100 points of sale all around Brazil.

Other European franchises that have been established in Brazil are FINI (candies and marshmallows), D-Unhas (personal care), Swarovski (jewellery), 5àsec (laundry), Pandora (jewellery), Ice Watch (jewellery), Mango (Clothing), Dia (supermarkets), Costa Café (coffee), Pressto (laundry) or Não Mais Pelo (waxing).


For an European SME, franchising in Brazil is halfway between licensing its IPRs (mainly trade marks) and creating subsidiaries, since it provides more control than licensing over how the product reaches the final consumer. Additionally, it is a considerably less expensive strategy than creating subsidiaries in the foreign country.

As part of a long-term business plan, franchising could be used as a first step before expanding business activities to Brazil. The company would be able to test how Brazilian consumers react to the offered product or service, receiving direct feedback from them, without involving wholesalers, licensors or distributors.

On one hand, the main advantages for franchisors are:

- the possibility of expanding their business fast without investing a large amount of resources;
- easier access to finance;
- control the way the product or service is offered to the end consumer;
- create a strong trade mark reputation and corporate image.

On the other hand, the franchisee will benefit from:

- using an already tested business model;
- a reduced learning curve;
- trade mark reputation;
- assistance and advice regarding how to run the business;
- marketing and advertising efforts made by the franchisor.

However, not all business can adopt this model. Franchising is less interesting for low margin businesses or for those that depend heavily on the specific skills of a few workers (who need particular training, for example, in artistic or technical work).

According to the most recent data from the Brazilian Association of Franchising (ABF), the market segments that have been showing the best growth rates within the first trimester of 2020 are: automotive services (7.4%), communications, informatics and electronics (6.9%) and cleaning and conservation services (5.6%). The market for service franchises also experienced a solid growth (6.6%).

**Success case:**

Founded in 2009, the Spanish company ‘Llao Llao’ opened its frozen yoghurt franchises all around Europe. From 2010 onwards, the company pursued its expansion further to South East Asia and Latin America. Currently, the company owns franchises in Chile, Colombia, Ecuador, El Salvador and Mexico and is planning to open more in Guatemala, Honduras and Panama.

## 2. Documents related to franchising

### A. FRANCHISE DISCLOSURE DOCUMENT

Designing a comprehensive franchise disclosure agreement in accordance with Brazilian legislation is essential to enter the Brazilian market correctly and safely. Before signing the contract, the franchisor has 10 days to hand over to the future franchisee the ‘franchise disclosure’ document, considered as a formal offer. According to Brazilian law, it is compulsory to provide potential franchisees with the following information:

- **Franchisor information**: the company’s background and its form of incorporation, its balance sheet and financial statements for the past 2 years; pending litigations, as well as the identity of the shareholders.
- **Franchise information**: detailed description of the franchise, general description of the business and activities to be performed by the franchisee, the ideal franchisee profile, description of the level of involvement of the franchisee in the operation and administration of the business, complete list of all franchisees of the network –as well as leaves during the last 12 months– and contact information of the members (name, address and telephone number).
- **Financial Information**: the initial investment required to purchase, deploy and start up the franchise, value of the initial membership fee or franchise fee and guarantee thereof and estimated value of the facilities, equipment and initial inventory and payment terms; clear information about periodic fees and other amounts to be paid by the franchisee to the franchisor, such as royalties, rentals or advertising fees.
- **IPRs status**: its situation before the National Institute of Industrial Property (INPI) (registration, ownership and other relevant information).
- **Other contractual obligations**: such as exclusivity, or rights of preference, other obligations imposed on the franchisee and termination conditions in case of expiration or breach.
- **A template of the contract** and, if applicable, the pre-standard franchise agreement chosen by the franchisor (full text, including its annexes and expiration date).

The franchisee disclosure document needs to be submitted to the franchisee candidate in Portuguese and the contract needs to be translated by a certified (sworn) translator. The franchisor must bear the translation costs.

**TIPS and WATCH OUTS**

Since the franchise offering letter includes sensitive information (e.g. financial statements or disclosure of part of the know-how), it is strongly advisable to include a confidentiality clause with regards to the information disclosed and documentation provided.

It is necessary to inform franchisee candidates on which services franchisors will provide in terms of training, access and use of the know-how, technologies and software, products and their replacement, materials, resources and replacement parts whenever these are applicable. This requirement became more rigid and protective of franchisees with the new Franchise Law of December 2019.

## B. FRANCHISE AGREEMENT

Legally speaking, franchising consists in a contract between two parties (franchisor and franchisee), where the former grants the latter the use of its Intellectual Property Rights and provides the franchisee with assistance and training on business management, marketing and other operational issues in exchange for initial and recurring fees or a percentage of the revenue generated by the franchisee.

Usually, the scope of a franchising contract comprises the following aspects:

- Intellectual Property Rights (non-exclusive licences);
- know-how, mainly regarding processes and good practices;
- management advice or assistance: e.g. by providing training to employees or other helpful resources related to day-to-day business administration;
- marketing and branding: establishing how the franchisee should use the distinctive signs, the layout of the establishment, advertising policy, promotions, etc.;
- fees and royalties;
- other clauses, such as confidentiality, exclusivity, breach of contract, liability, etc.

Depending on the characteristics of the business and of the parties, there are different types of fees (or royalties) that could be introduced in the contract:

- **initial fee or franchise fee:** a fixed amount of money that is usually paid at the time the agreement is signed and it typically involves the payment of the full business plan, the training of the franchisee and employees, as well as the professional assistance related to the establishment and launch of the business;
- **royalty fee:** amount of money that is periodically paid to the franchisor, usually calculated as a percentage of gross or net sales;
- **other fees:** depending on the characteristics of the franchise, the franchisee may also have to pay for certain services provided by the franchisor, such as:
  - supply of products
  - promotional and advertising services
  - other services.

As mentioned above, there is a need for comprehensive and clear information about the fees for the services and products supplied to the franchisee. Seeking local counsel from a specialised lawyer is highly recommended.



According to Brazilian law, 'the franchise agreement should always be written and signed in the presence of two witnesses and shall be valid regardless of whether it is registered with a notary or a public agency'. Thus, the formal validity of the franchising contract is subject to the requirement of the signature of two witnesses (on every page).

If the franchise agreement is signed outside Brazil, the agreement must be notarised and legalised before the local Brazilian consulate.

Registration of the franchise agreement is required for EU SMEs -being a franchisor based abroad-, since it is necessary to perform international transfers of the fees and royalties.

### C. MASTER FRANCHISING AGREEMENTS

A master franchise agreement (MFA) is a contract through which the franchisor grants the master franchisee the right to sell unitary franchises within a territory during a specified period of time in exchange for a previously fixed sum of money. It usually depends on the number of unitary franchises opened and the degree of development of the business reached by the master franchisee. In practice, the master franchisee acts as a sub-franchisor, while the unitary franchises act as sub-franchisees. The establishment of MFAs shifts part of the risk from the franchisor to the master franchisee and simplifies the franchisor's legal obligations (a single agreement instead of one for each franchisee).

This alternative may be interesting for European SMEs that have already been distributing their products or services within the Brazilian market and have a trusted partner in the country or a licensee that is interested in expanding the business, especially if the company is not interested in directly operating the franchise business or in opening a subsidiary. A master franchise agreement should provide clauses that regulate the relationship between master franchisor and master franchisee and the contract that the unit franchise should sign with the master franchisee. It is possible to transform one regular franchisee into a master franchisee as trust builds between the parties.

However, it must be emphasised that, because the licensor company is, in a way, delegating part of their IP rights management to a third party, MFA is only indicated for companies that have a genuine trusted partner or licensee in the country. In addition, if the terms in the contracts are not very well-written and boundaries are not very well drawn, MFA may represent severe risks for the licensor's IP rights. For instance, contracts must state very clearly that investments in marketing and advertisement are in no way cause for licensees to consider themselves as co-owners of the IP rights. Furthermore, it is strongly advisable to include liability clauses in the contract for cases of mismanagement of the licensor's IP rights.

MFA risks are very manageable by contracts, but there are still risks. Therefore, when drafting an MFA, it is highly recommended that a legal expert be contacted.

#### TIPS and WATCH OUTS

If you are planning to sign a master franchise agreement, pay particular attention when defining the master franchisee's liabilities. You should also include special provisions regarding the early termination of the contract, providing a smooth subrogation for the master franchisee. This type of clauses will allow you to further benefit from the franchise network created by the resigning master franchisee.

In addition, early termination and performance clauses help bring transparency to the relationship between franchisor and franchisee. Alternative dispute resolution systems before an international institution are recommended and they are faster than traditional methods. Hence, the contract should include arbitration clauses, especially if your company does not have its headquarters in Brazil.

When drafting an MFA, it is highly advisable to contact a legal expert. The Latin America IP SME Helpdesk offers free, confidential, fast first-line legal advice for European SMEs. If you are not sure about the approach you should choose for your SME, do not hesitate to contact us. Our experts will be pleased to assist you. You can find more information at http://www. latinamerica-ipr-helpdesk.eu/

The MFA is not to be confused with multi-unit franchises. MFA is a system in which a trusted partner manages franchising rights in the country –in other words, the foreign company delegates the management to this trusted partner by giving them the right to sell unitary franchises to third parties. Multi-unit franchisees, however, purchase the right to own multiple units in the country. While in the MFA system the trusted partner sells franchises, in the multi-unit franchises system one franchisee owns multiple units of franchises.

Compared to multi-unit franchises, MFAs offer the chance to expand the business in the country without overwhelming the single licensee. Despite being a good and trusted licensee, one might not be interested in managing or owning multiple franchises. For instance, managing multiple franchises may be overwhelming or beyond the managing ability of the licensee. It can also be too expensive to perform.

Moreover, multi-unit franchises represent a higher risk for licensees, since they will have to make a significant investment in multiple businesses. Because MFA diversifies the units to multiple owners, it is less risky for both the licensor and the licensee.

In short, MFA is a very useful alternative to multi-unit franchises for licensors that wish to increase the number of franchises in the country but do not want to increase the costs for managing franchising rights in the country or overwhelm the owners. The advantages of stepping aside from managing licensing rights in the countries come at the cost of delegating powers to someone that can be trusted and that is very well tied up by clear and strict contracts.

## D. OPERATING MANUALS

The operation manual is the playbook that contains the whole know-how involved in the franchised business. It is one of the key documents of the franchise system and is normally incorporated into the franchise or master franchise agreements.

Every company defines its operational processes in order to optimise resources and improve the final quality of the products and services offered to their customers. This is especially important in franchising agreements where these operational processes should be replicated by each of the franchisees.

The operating manual describes standards, rules, and specifications on how to perform a task or how to present a given product or service, such as:

- franchise system;
- operational methods such as methods for production-time, performance standards, technical specifications, installation and equipment handling or stock management;
- operational instructions: regarding staff training, pricing policy, marketing or advertising, for example;
- outlet specificities, such as location, size or layout;
- standard documentation, such as complaint forms, contracts, ordering forms…

## 3. Further Brazilian specificities related to franchising

### A. REGISTRATION WITH THE INPI

Regarding foreign franchisers, the franchise agreement shall be registered with INPI (Instituto Nacional da Propriedade Industrial). The purpose of such registration is to enable its enforcement against third parties, to allow the franchisee to benefit from certain tax deductions and to allow the franchisee to make payments to foreign countries (in line with the clearance regulation of the Brazilian Federal Bank). The following documents should be presented before the INPI to register the agreement:

- original version (or certified copy) of the agreement;
- certified (sworn) translation to Portuguese;
- power of attorney;
- statement signed by the franchisee acknowledging the receipt of the franchise disclosure document 10 days prior to the execution of the agreement.

**TIPS and WATCH OUTS**

The INPI performs a formal examination of the content and examines the validity of the IPRs licensed within the agreement. Hence, it is of the utmost importance to check that the IPRs concerned are in force and valid.

### B. APPLICABLE TAXES FOR FOREIGNER FRANCHISORS

The Brazilian tax system is usually considered as one of the most complex and difficult to navigate in the world. Thus, it is strongly advisable to seek professional help. Taxes may change from state to state and it also depends on the type of service or product provided.

Generally speaking, payments made to foreign franchisors are subject to a 15 % withholding tax, except if the foreigner franchisor is established at an offshore country, which would set the withholding tax at 25%. Additionally, franchisors are usually subject to a tax of 10 % as a Contribution for Intervention on the Economic Domain (CIDE), depending on the details of the product or service provided. However, it is possible to agree for the withholding tax to be paid by the franchisee.

Other general taxes are payable by foreign franchisors, such as the Tax for Services (ISS) ranging from 2 % to 5 %, a 1.65 % tax for PIS (Social Security Fees) and 7.6 % for COFINS (Contribution to Social Security Financing), calculated over the total amount of royalties paid.

## 4. Glossary

**Franchise:** arrangement in which one party (the franchisor) grants another party (the franchisee) the right to use its trade mark or trade name as well as certain business systems and processes to produce and market a good or service according to certain specifications (source: Business dictionary).

**Royalty:** a payment to an owner for the use of property, especially patents, copyrighted works, franchises or natural resources. A royalty payment is made to the legal owner of a property, patent, copyrighted work or franchise by those who wish to make use of it, for example, to generate revenue. In most cases, royalties are designed to compensate the owner for the use of the asset and are legally binding (source: investopedia).

**Confidentiality agreement:** a legal agreement between two or more parties that is used to state that a confidential relationship exists between them. A confidentiality agreement is used in strategic meetings in which various parties become privy to sensitive corporate information that should not be made available to the general public or to other competitors (source: investopedia).

**Franchise disclosure document**: document that contains the essential information regarding the know-how and performance of the business model being offered for franchising. It is essential for the validity of the franchising agreement.

**Operating manual:** document that contains the know-how developed by the franchisor and from which the franchisee learns how to run the business.

## 5. Related links and additional information

International Franchise Association (general information and resources): www.franchise.org/

Brazilian Franchising Association (Associação Brasileira de Franchising (ABF)): www.portaldofranchising.com.br/

Brazilian Patent Office (INPI): www.inpi.gov.br

Sebrae: http://www.sebrae.com.br/sites/PortalSebrae/artigos/a-importancia-dos-manuais-para-as-redes-de-franquias,-356df925817b3410VgnVCM2000003c74010aRCRD

A very complete guide on Master Franchising: https://www.unidroit.org/instruments/franchising/guide/second-edi-tion-2007

In English: https://www.thebfa.org/franchise-my-business/

In Spanish (how to become a franchisor, step by step): http://www.franquiciadirecta.com/informacion/paraelfranquiciador/pasosaseguirparapoderconvertirtunegocioenfranquicia/206/1144/

WIPO “Role of intellectual property in enhancing competitiveness and growth of small and medium-sized enterprises in the franchising sector”: http://www.wipo.int/meetings/es/doc_details.jsp?doc_id=85962

On applicable taxes: (Regional Council of Countability from Rio de Janeiro – CRCRJl): http://webserver.crcrj.org.br/APOSTILAS/A1041P0435.pdf

# LATIN AMERICA IP SME HELPDESK

## Franchising in Brazil

Download Guide

The **Latin America IP SME Helpdesk** offers **multilingual services** (English, French, German, Spanish and Portuguese[1]), with free information and first-line legal advice on IP related subjects, as well as training, webinars and publications, especially designed for EU SMEs.

**HELPLINE** First-line advisory service on IP protection and enforcement for EU SMEs working or planning to operate in Latin America.

**TRAINING** Targeted trainings and webinars on IPR protection and enforcement for EU SMEs (including sector- specific approaches).

**IP CONTENT** State-of-the-art publications (factsheets, learning modules, videos, IP glossary, info graphics, case studies and newsletters) on the protection and enforcement of IPR in Latin America – specifically addressing IP matters from the SME business needs point of view.

**AWARENESS RAISING EVENTS** Participation in events attended by EU SMEs to increase the awareness of IP and of the visibility of the services provided by the Helpdesk.

**IP ANALYSIS** Analysis of IP challenges faced by EU SMEs in the target markets.

**IP DIAGNOSTIC TOOLKIT** Toolkit for self-evaluation of the IP-status of the user in terms of IP knowledge and management.

**IP COST TOOL** Online tool that allows the user to pre evaluate the costs related to IP management in every Latin American country covered by the Helpdesk.

[1]The language offer will depend on the specific service and experts' availability.

If you have any queries on how to protect your Intellectual Property in Latinamerica contact our Helpdesk service:

helpline@latinamerica-ipr-helpdesk.eu
+34 96 590 9684
Working Hours: Monday - Friday 9:00 -16:30 (CEST)

If you want more information on additional free services offered by the Helpdesk contact the coordination team:

info@latinamerica-ipr-helpdesk.eu
University of Alicante, Campus San Vicente del Raspeig, Edificio Torre de Control, 03690 Alicante, Spain
+34 96 590 9684

Follow us on Social Media and stay tuned on new releases of factsheets and other IP content:

**@latinamericaipr**

**https://intellectual-property-helpdesk.ec.europa.eu/**



Luxembourg: Publications Office of the European Union, 2021

Print ISBN 978-92-9460-848-2 doi:10.2826/246732 EA-06-21-074-EN-C
PDF ISBN 978-92-9460-843-7 doi:10.2826/344184 EA-06-21-071-EN-N

Publications Office of the European Union

*Last update October 2021*