Business Law

Chapter V – Commercial Contracts

Chapter V – Commercial Contracts

1. Introduction

- Commercial contracts form the basis of every commercial transaction in business, whatever the jurisdiction, yet they are often negotiated in haste and drafted with little attention to fundamental principles or compelling style, which would otherwise serve to protect the parties and ensure the integrity of the transaction.
- They form the bedrock of a business' trading activities, and need to be flexible enough to enable a business to achieve its objectives and yet remain secure and effective.

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- Among the plethora of commercial contracts currently available, and in use in Portugal, specific frameworks for the following categories are analysed:

(i) Consortium,

(ii) Unincorporated partnership,

(iii) Agency agreement,

(iv) Franchising agreement,

(v) Intermediation agreement,

(vi) Commercial concession agreement,

(vii) Leasing,

(viii) Factoring.

1.2. Consortium ("Contrato de Consórcio")

- Consortium contracts are aimed at formalising joint ventures. Two or more parties undertake to carry out, jointly, a certain activity or else to act in concert, in order to achieve a common purpose (article 1 of the Decree-Law 231/81 of 28 July).

1.2.1. Legal Framework

- Consortia are regulated by Decree-Law 231/81 of 28 July.

1.2.2. Main Characteristics

- Consortia may either be formed for the purpose of preparing (carrying out all the preliminary material and legal acts) and/or implementing a given project or undertaking, supplying goods to third parties, promoting research, prospecting and exploiting natural resources (article 2).
- An external consortium is formed for the purpose of producing goods to be shared among the members.

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- **Types of Consortia:**
- Consortia will either be (article 5):

(i) internal, where either the activities are rendered or the goods are supplied directly by one of the members of the Consortium and only this member will then establish relations with any third parties, or each of the members of the Consortium renders the activity to or supplies the goods to third parties without any mention of the existence of the Consortium, or

(ii) external, where the activities are rendered or the goods are supplied by each of the members of the Consortium to third parties with mention of the existence of the Consortium.

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- The consortium agreement will set out the objective of the consortium, obligations of the parties, contributions and division of common expenses.
- Consortium members’ duties are the following (article 8):

(a) Abstain from competing with the consortium itself, unless such action is expressly permitted in the agreement;

(b) Provide the other consortium members with all relevant information; and

(c) Allow examination of goods supplied, or activities specifically carried out.

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- Consortium members are also required to nominate from among themselves a “head of consortium” (who will lead the consortium), and may optionally instate a “supervisory board” comprised of all consortium members (article 12).
- There is no joint liability in the relationships between consortium members and third parties .

1.2.3. Form of Agreement

- The formation of a consortium requires a written agreement. Where it encompasses a transfer of property for the venture, then the formation of the consortium will have to be laid out by means of a public deed (articles 2 and 3).

1.2.4. Termination of the Consortium

- The consortium is terminated where (article 11):

(i) unanimously agreed by its members;

(ii) its objective is accomplished or such accomplishment has become impossible;

(iii) the time limit, unless extended by the members, set out for the agreement's validity expires;

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(iv) all but a single member remains in the consortium;

(v) any other cause and/or condition for termination established in the consortium agreement is fulfilled; or

(vi) should none of the above apply, and if the time limit of the consortium has not been extended, it will expire within 10 years of its signature.

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➢ Right of Withdrawal

- Members unable to fulfil their obligations under the Consortium have the right to withdraw [article 9 (1) (a)].

➢ Expulsion

- Members of the Consortium may be expelled in cases of insolvency or breach of duties and obligations under the consortium agreement [article 9 (1) (b)]..

1.3. Unincorporated Partnerships ("Contrato de Associação em Participação")

- Unincorporated partnership agreements ("Contrato de Associação em Participação" or "Contrato de Conta em Participação") are an alternative to the classic route of incorporation of companies or consortia.

1.3.1. Legal Framework

- Unincorporated partnership agreements are also regulated by Decree-Law 231/81 of 28 July.
- Pursuant to such instruments, one or more individuals or entities (hidden partners) share the profits or profits and losses incurred by another (operational partners), in carrying out a given commercial activity (article 21).

1.3.2. Main Characteristics of Unincorporated Partnership Agreements

- The main characteristics of Unincorporated Partnership Agreements provide that the hidden partner shares the profits or profits and losses (sharing the losses is optional) incurred by the operational partner in the activity covered by the agreement, in return for a contribution, which may consist of capital, goods or rights (article 25).

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- Such a contribution can be replaced by reciprocal unincorporated partnership agreements, concluded simultaneously. If the hidden partner shares in the losses, its contribution may be waived.

- The agreement must specify the hidden partner's share in the operational partner's profits or profits and losses, with regard to the activity covered by the agreement. However, the hidden partner's share in such losses cannot be higher than its proportionate contribution.

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- The operational partner has the following duties (article 26):

(a) Manage the partnership with due diligence;

(b) Preserve the structure of the partnership, namely its intended object and duration unless otherwise authorised by the hidden partner;

(c) Not to engage in the same business activities as the hidden partner, unless expressly authorised by the same;

(d) Provide the hidden partner with all relevant information.

1.3.3. Form of Agreement

- This type of agreement is not subject to any specific legal form, unless otherwise required by law, with regard to the nature of the assets contributed by the hidden partner to the partnership. However, provisions concerning the exclusion of the hidden partner’s liability for losses must be laid out in writing (article 23).

1.3.4. Termination of the Partnership

- The unincorporated partnership is terminated wherever any relevant cause or conditions, as set forth in the respective agreement, are fulfilled, as well as on the following grounds (article 27):

(i) If the partnership's objective is fully accomplished or such accomplishment becomes impossible;

(ii) Upon the death of any of the partners, if expressly requested by his successors or by the surviving partner;

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(iii) If one of the partners, being a company, is liquidated;

(iv) If one of the partners attains the position of both operational and hidden partner;

(v) Termination by any of the partners on grounds of just cause; and

(vi) If any of the partners becomes bankrupt or insolvent.

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- One party can terminate the agreement on the grounds of just cause, namely when the other party has not complied with its obligations under the agreement [article 30 (1) (2)].
- In cases where the period of validity for the Unincorporated Partnership Agreement has not been established, any of the parties can terminate it within 10 years of the date of its signature [article 30 (3) (4)].

1.4. Agency Agreement ("Contrato de Agência")

1.4.1. Legal Framework

- The agency agreement, or commercial representation agreement, as it is also called, is regulated by Decree-Law 178/86 of 3 July, as amended by Decree-Law 118/93 of 13 April, which implemented Council Directive 86/653/EEC of 18 December 1986.

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1.4.2. Main Characteristics

- According to the definition set out in the abovementioned provisions, an agency agreement is a contract whereby an individual (the agent) undertakes to negotiate, on behalf of another (the principal), certain contracts within a given territory or among a specific group of clients, independently, and for a certain remuneration (usually a commission) [article 1].
- The agreement may contain provisions which limit the agent's activities to a certain area.

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- The agent may only enter into contracts on behalf of the principal if so duly empowered. However, in such cases, the agent is entitled to take all necessary steps to ensure the principal's rights are respected.
- The agent is not entitled to collect debts except if so empowered by the principal, in writing. In such cases there will be legal presumption that authority to collect debts has been granted.
- Compliance with the principal's instructions may not jeopardise the agent's independence.

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1.4.3. Form of Agreement

- Agency agreements are not required to be drawn up under a specific legal form.
- However, the following clauses are valid only if they are laid down in writing:

(i) Powers to conclude contracts on behalf and in the name of the principal;

(ii) Powers to collect debts on behalf and in the name of the principal (such empowerment is presumed if the agent is already empowered to conclude contracts on behalf and in the name of the principal);

(iii) Establishment of the agent's exclusivity (within a given territory or among a specific group of clients);

(iv) "Del credere" arrangements;

(v) Restraint of trade clause;

(vi) Termination of the agreement by mutual consent;

(vii) Termination of the agreement by one of the parties.

- In accordance with the provisions of Decree-Law 178/86, each one of the parties to the agreement is entitled to request a signed written document, clearly stating the clauses of the agency agreement. Such entitlement may not be waived (article 1).

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1.4.4. "Del credere" Arrangement

- Under the "del credere" arrangement, the agent undertakes to guarantee the obligations of a third person, provided that the contract was negotiated or concluded by the same [article 10 (1)].
- Such an arrangement is only valid if laid down in writing and provided it either specifies the contract whose execution is thereby guaranteed or indicates the person(s) to whom the guarantee relates. This agreement entitles the agent to receive a special commission [article 10 (2)].

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1.4.5. Restraint of Trade Clause

- Under a restraint of trade clause, the agent undertakes to refrain from such business activities that may compete with those pursued by the principal for a certain period of time, following termination of the agency agreement.
- Such a clause must be laid down in writing and is valid for a maximum two-year period and only for activities involving the agent’s group of clients or territory. The acceptance of this clause entitles the agent to receive compensation.

1.4.6. Professional Secrecy

- The agent cannot divulge or make personal use of secrets confided by the principal or of which it has acquired knowledge as a result of exercising its activity, even after termination of the contract, except in accordance with the strict measures allowed for within specific professional and deontological rules (article 8).

1.4.7. Use of Sub-Agents

- Recourse to sub-agents is allowed unless otherwise agreed by the parties. The sub-agency agreement is also regulated by Decree-Law 178/86 of 3 July, as amended by Decree-Law 118/93 of 13 April, with the appropriate adaptations (article 5).

1.4.8. Right to Information

- The principal is obliged to inform the agent, without delay, whether it accepts the contracts negotiated by the latter as well as those concluded without specific powers to do so (article 21).

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- The principal should supply the agent with periodical listings of the contracts concluded and commissions due, as well as all such information as the agent may need to confirm any entitlement to commissions (article 7).
- The principal should also immediately inform the agent if it is unable to fulfil its obligation of entering into the agreed or expected number of contracts (article 14).

1.4.9. Exclusivity

- Wherever established, in writing, that the agency is to be exclusive, the principal may not use other agents to carry out activities competing with those of the agent within the given area or group of clients allocated to that agent (article 9).
- The agency contract is always deemed to establish an exclusive right in favour of the principal by which the agent is forbidden to render the same activity to others (article 4).

1.4.10. Expenses and Commission

- Unless agreed otherwise, the agent does not have the right to be reimbursed for expenses incurred during his normal activity (article 20).
- The agent may be entitled to a fixed monetary retribution in addition to the commission arising from the agency agreement. The right to the commission arises in one of the following circumstances (article 18):

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1) the principal has complied with the agreement or should have complied with it;

2) the third party has complied with its obligations under the agreement.

- The parties may choose to set a different moment for when the right to the commission arises, however, this moment may not in any case come after the principal has complied with its obligations under the agreement and the third party has also fulfilled, or should have fulfilled, its obligations under the agreement.

1.4.11. Termination of the Agency Agreement

- The agency agreement terminates automatically in the following circumstances (article 26):

(i) Upon expiry of the fixed period agreed by the parties;

(ii) Through verification of a resolving condition, if such a condition was agreed by the parties;

(iii) Upon death of the agent or, in the case of a company, if it is liquidated;

(iv) By mutual written consent.

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- Only agency agreements concluded for an undetermined period of time can be terminated by either party, by serving a termination notice, in writing, to the other party (article 27).
- Unless a fixed term has been expressly stipulated, by the parties, the agreement is deemed to have been entered into for an undetermined period of time.

1.4.11.1. Period of Notice

- The period of notice is equal to one month, two months and three months for the first, second, and third and subsequent years of the agreement, respectively [article 28 (1)].
- Failure by either party to comply with the period of notice entitles the other party to compensation [article 29 (1)].

1.4.11.2. Rescission of the Agreement

- The agency agreement can be rescinded immediately by either party in two cases (article 29):

(a) The case of a serious or repeated breach of contract, if, as a result, it is unreasonable to maintain contractual relations

(b) Wherever circumstances arise that seriously hinder or render impossible the operation of the agreement.

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- The rescission is effected through a written document specifically laying out the causes justifying it and must be drawn up no more than one month after the occurrence of such facts (article 31).
- The contract may always be terminated by mutual agreement (article 25).

1.4.12. Claim to Compensation for Breach of Contract

- Irrespective of the right to terminate the agreement, either party is entitled to compensation for damages arising from the other party's breach of obligations (article 32).

1.4.13. Claim to Compensation for Termination of Contract

- Irrespective of the right to compensation mentioned above, upon termination of the contract the agent is entitled to "clientele compensation", provided that all the following conditions have been met (article 33):

(i) It has been responsible for attracting new clients or has significantly increased the volume of business with existing clients;

(ii) The principal derives a significant benefit from the agent's activity after termination of the contract; and

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(iii) The agent has lost commissions on negotiated contracts with the clients mentioned in (i), above, as a result of termination of the agreement.

- The compensation in question is not due if the agent has given cause for termination or agreed to assign its position to a third party.
- The right to clientele compensation is lost if the agent, within one year after termination of the contract, does not communicate to the principal its intention to make such a demand.

1.5. Franchising Agreement ("Contrato de Franquia")

1.5.1. Legal Framework

1.5.1.1. Portuguese Legal Framework

- Although franchising agreements are widely utilised in Portugal, there is no national legislation dealing with them specifically. The application of national legislation on competition is of particular interest in this matter.

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1.5.1.2. European Union Legislation

- Franchising agreements, particularly cross-border ones, must also comply with European Union competition law, namely Article 101 of the EF Treaty on concerted practices and agreements between companies and community legislation implementing such provisions.
- Indeed, typical franchise agreement clauses, like those granting the franchisee exclusivity in a given territory, or exclusive access to the franchisor's know-how, may be deemed incompatible with the aforementioned provisions.

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- The European Commission, however, recognised the importance of franchising as a means of economic development by optimising sales and investment and reducing costs.
- Thus, under its power to exempt, by regulation, certain categories of agreements from being subject to application of Article 101 of the Treaty, the Commission adopted Regulation (EEC) No. 4087/88 of 30 November 1988 on the application of Article 85.3 of the Treaty to categories of franchise agreements, which was later replaced by Commission Regulation (EC) No. 2790/1999 of 22 December 1999 on the application of Article 101.3 of the Treaty to categories of vertical agreements and concerted practices (block exemptions).

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- Furthermore, the European Franchising Federation (EFF) - a non-profit organisation comprised of the national franchise associations of several European countries - adopted the "European Code of Ethics for Franchising" ("Código Europeu de Deontologia do Franchising"), which sets out detailed criteria for franchising agreements, as well as detailed conditions to be observed by the contracting parties. EFF members undertake to impose on their own members the obligation to apply, and abide by, the provisions of the "European Code".

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1.5.2. Main Characteristics

- The main characteristics of a franchising agreement provide that an individual or legal entity (franchisor) authorises another (franchisee) to utilise a trademark, logo or symbol belonging to the franchisor and to use its know-how, products or services.

- The franchisor provides technical assistance to the franchisee in connection with the licensed goods, in return for remuneration or payment of fees by the franchisee. The agreement may be valid only for a given territory.

- Franchising agreements may also provide that the franchisee will be bound to acquire certain of the franchisor's products, and to comply with a determined set of rules and regulations.
- These rules will generally be linked to quality standards of the services or products to be delivered.

1.5.3. Termination

- The franchise agreement can be terminated pursuant to the general rules applicable to contracts in Portugal. Recourse to legal provisions on termination of agency agreements (referred to above) is admissible. However, that depends chiefly on the specific terms of the franchise agreement.

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1.6. Intermediation Agreement (“Contrato de Mediação”)

1.6.1. Legal Framework

- Intermediation agreements in general are also unregulated in Portugal; there are, however, certain types of intermediation agreement that have their own specific regulation, such as intermediation in the purchase and sale of property, which is regulated by Decree-Law 77/99 of 16 March, as amended by Decree-Law 258/2001 of 25 September, or financial brokerage, which is regulated by Decree-Law 262/2001 of 28 September and Securities Market Supervisory Authority Regulation 12/2000 of 23 February.

1.6.2. Main Characteristics

- The parties to a mediation agreement undertake to find an interested party for a given deal and to introduce this third party to the other party in the agreement, in order to discuss the possibility of doing business.

- Contrary to the commissioner and commercial agent, the mediator's relationship to the parties in the deal is one of interdependence.

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1.6.3. Representation

- In this regard, it is worth noting that mediation does not involve representation of any of the parties, as in fact it acts in the interest of both parties and not for one of them alone.

1.6.4. Remuneration

- The mediator only acquires the right to receive remuneration if the deal is concluded as a result of its intervention. Such remuneration often consists of a commission calculated on the basis of the value of the said deal.

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1.7. Commercial Concession ("Contrato de Concessão Comercial")

1.7.1. Legal Framework

- Commercial concessions are another type of commercial agreement, which, although not regulated by specific provisions, are nevertheless widely used in Portugal. They are very similar to agency agreements and the Portuguese courts' case-law has consistently held that the legal framework for agency agreements, as defined by Decree-Law 178/86 of 3 July, and amended by Decree-Law 118/93 of 13 April, also applies, by analogy, to commercial concession agreements.

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- The legal framework is very similar to those implemented in all other EU Member States, because it draws its provisions from Council Directive 86/653/EC of 18 December 1986, concerning self-employed commercial agents.

1.7.2. Main Characteristics

- The main characteristics of commercial concession agreements provide that one of the parties (the grantee) undertakes to buy from the other party (the grantor) goods manufactured and/or distributed by the grantor in order to re-sell them within a specified zone. Usually, the grantee must pay a share of the profits obtained in such re-sales to the grantor.
- Under most concession agreements the grantee undertakes to re-sell the grantor's products exclusively.

1.7.3. Representation

- Notwithstanding the above, commercial concession agreements differ from agency agreements in the sense that the grantee will always act on its own behalf and in its own name, acquiring ownership of the goods in order to resell them to third parties and bearing all risks arising from their commercialisation.

- By contrast, in the agency agreement the agent will always act on behalf of another party.

1.7.4. Termination of the Contract

- Termination of the contract without just cause gives rise to compensation for damages.
- Given the similarities between commercial concession agreements and agency agreements, termination of commercial concession agreements is often regulated with recourse to the application of the provisions on contract termination of the agency agreement's legal framework.

1.7.5. Compensation

- Also in view of the abovementioned similarity between commercial concession agreements and agency agreements, Portuguese courts have consistently held that the grantor at the end of the contract is bound to pay to the grantee compensation in view of results achieved by the grantee in the formation of clientele ("clientele compensation").

- The compensation is calculated in equitable terms, taking into consideration the benefits received by the grantor in view of the grantee's performance.

1.8. Leasing ("Locação Financeira")

1.8.1. Legal Framework

- Lease agreements are often used for financing the acquisition of fixed or non-fixed assets. They are regulated by Decree-Law 149/95 of 24 June, as amended by Decree-Law 265/97 of 2 October and by Decree-Law 285/2001 of 3 November.

1.8.2. Main Characteristics

- The main characteristics of lease agreements provide that the lessor undertakes to supply property or equipment to another party (the lessee), in accordance with its instructions. In exchange, the lessee will remunerate the lessor by instalments and maintain ownership of the goods until the end of the agreement.

- At such time, the lessee typically has the option to acquire the equipment or property, by paying a so-called residual value, determined in accordance with criteria laid out therein.

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- The lessor may be a leasing company (regulated by Decree-Law 72/95 of 15 April, amended by Decree-Law 285/2001), a Financial Credit Institution (regulated by Decree-Law 186/2002), or a bank.

- The lessor is not responsible for any imperfections or faults of the leased goods and the lessee can act directly against the seller or manufacturer. Risk of the goods being destroyed is also the lessee's responsibility.

1.8.3. Form of Agreement

- Lease agreements are laid out in writing. However, in the case of leased fixed assets a notary public will also certify the signatures of the parties as well as the existence of a valid construction licence or habitation permit.
- Where a non-fixed asset subject to mandatory registration (e.g., a car or a boat) is the object of the lease agreement, complete details of each of the signatory's identity cards or the equivalent is required. In either case the agreement must be registered with the relevant registration office.

1.8.4. Duration of the Agreement

- Lease agreements may have a maximum legal time frame equivalent to the leased asset's estimated economic lifetime, however, not exceeding 30 years.
- In the absence of an indication of the agreement's legal timeframe, the latter shall be presumed to be equal to 18 months (for non-fixed assets) or 7 years (for fixed assets). There are also minimum duration periods.

1.8.5. Termination of the Agreement

- Agreements can be terminated by either party on grounds of breach of contract, pursuant to the general rules on contracts provided for in the Portuguese Civil Code.
- However, the rules on rental agreements which might apply to lease agreements, since both share common traits, do not apply to lease agreements, as expressly determined by Decree-Law 149/95.

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- Lease agreements can also be terminated by the lessor upon the lessee's death or liquidation (if it is a company), or if the lessee becomes insolvent. Anticipated termination of the agreement is also admissible where the lessee pays - with the lessor's approval - all remaining instalments, including the residual value.
- As with most contracts, a leasing agreement can be terminated at any time, by mutual consent of the parties.

1.9. Factoring

1.9.1. Legal Framework

- Decree-Law 171/95 of 18 June regulates the main aspects of factoring contracts and factor companies, as they are credit institutions, and are regulated by the General Regime of Credit Institutions and Financial Companies ("Regime Geral das Instituições de Crédito e Sociedades Financeiras - RGICSF").

1.9.2. Main Characteristics

- Factoring contracts provide for the assignment of short term credits which originate in the sale of products or the rendering of services in the internal or external market.

- Such contracts may be made with or without credit risk transfer, depending on the contract. If the contract does not expressly regulate this aspect, general rules of credit assignment apply, which means the credit risk will be transferred to the acquirer (factor).

1.9.3. Form of Agreement

- Factoring agreements must be made in writing and will regulate the timeframe and mode of the transaction carried out between the factor and the accounts receivable selling company.

- The transfer of credits under a factoring contract must be accompanied by the respective invoices or equivalent documents.

1.9.4. Duration of the Agreement

- The contract may have a limited or an unlimited duration. Usually it has a duration of one year and may also contain a renewal clause.

1.9.5. Termination of the Agreement

- Agreements may be terminated by either party on grounds of breach of contract, pursuant to the general rules on contracts contained in the Portuguese Civil Code.

1.10. Conclusion

- Commercial contracts form the basis of every commercial transaction in business and must attain multiple objectives, allowing companies a large degree of flexibility when outlining their commercial plans or when establishing a relationship with other companies.

- In this instance, an understanding of contract formation and effective drafting are essential for individuals and corporate bodies alike, to compete effectively in today’s increasingly competitive and complex business environment.

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