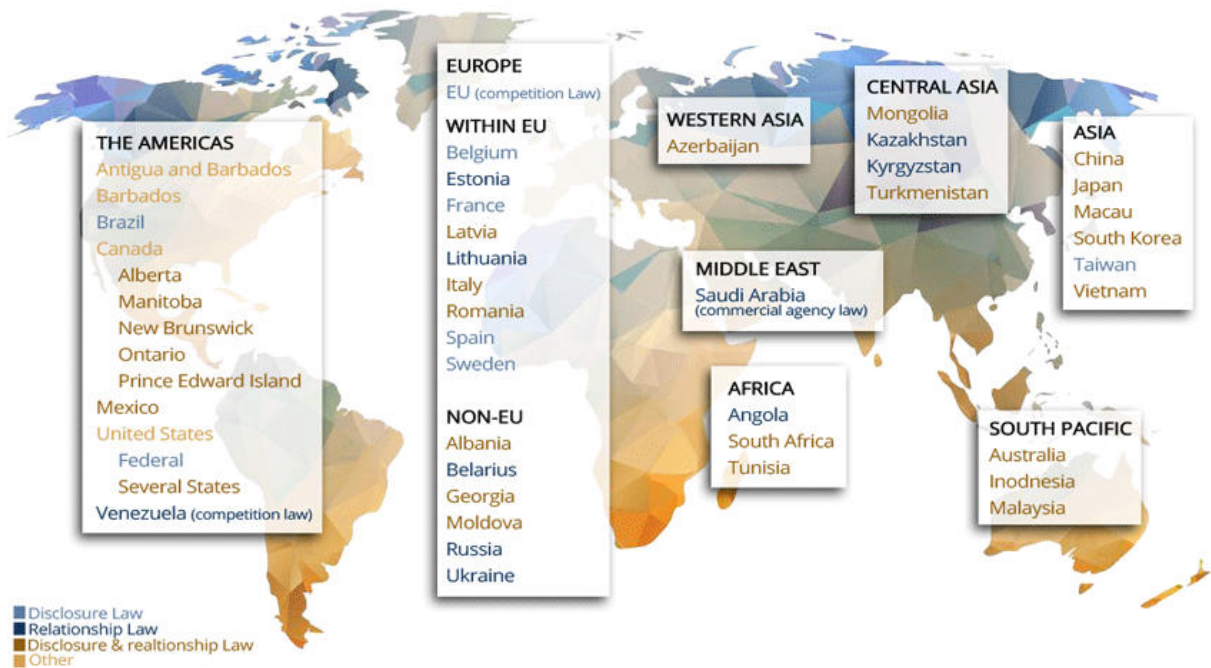




INTERNATIONAL RESOURCES ABSTRACT

Laws and agencies that regulate the offer and sale of franchises



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Which laws and government agencies regulate the offer and sale of franchises?

The provisions governing franchise activities can be found primarily in the following laws and regulations:

- Administration of Commercial Franchise Procedures (promulgated by the Ministry of Commerce on 30 December 2004 and effective as of 1 February 2005);
- Administration of Commercial Franchise Operations Regulations (promulgated by the State Council on 6 February 2007 and effective as of 1 May 2007);
- Administration of Commercial Franchise Operations Registration Procedures (promulgated by the Ministry of Commerce on 7 November 2011 and effective as of 1 February 2012); the old Administration of Commercial Franchise Operations Registration Procedures (Decree No. 15, 2007) of the Ministry of Commerce, which came into force on 1 May 2007, was repealed simultaneously;
- Administration of Information Disclosure for Commercial Franchise Operations Procedures (promulgated by the Ministry of Commerce on 18 January 2012 and effective as of 1 April 2012); the old Administration of Information Disclosure for Commercial Franchise Operations Procedures (Decree No. 16, 2007) of the Ministry of Commerce was repealed simultaneously; and
- Administration of Foreign Investment in Commercial Sector Procedures (promulgated by the Ministry of Commerce on 16 April 2004 and effective as of 1 June 2004).

The government agency in charge of administration of franchises is MOFCOM and its local counterparts.

What are the exemptions and exclusions from any franchise laws and regulations?

There is no exemption or exclusion under current Chinese franchise laws and regulations.

Does any law or regulation create a requirement that must be met before a franchisor may offer franchises?

The franchisor must satisfy the '2+1' requirement, namely, the franchisor must already have at least two existing stores and must have been engaged in the franchised business for more than a year. The two existing stores can be anywhere in the world – they do not have to be in China. The franchisor must have the necessary business resources, such as a registered trademark, enterprise logo, patent or proprietary technology.

Are there any laws, regulations or government policies that restrict the manner in which a franchisor recruits franchisees or selects its or its franchisees' suppliers?

Not at the moment



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In the case of a sub-franchising structure, who must make pre-sale disclosures to sub-franchisees? If the sub-franchisor must provide disclosure, what must be disclosed concerning the franchisor and the contractual or other relationship between the franchisor and the subfranchisor?

Under a sub-franchising structure, the sub-franchisor is obligated to disclose to the sub-franchisee that it is a sub-franchisor, that it has obtained the necessary operational resources (for example, trademarks) from the original franchisor, and that it has obtained (or will obtain) permission from the original franchisor to grant a sub-franchise to the sub-franchisee. In addition, it should disclose to the sub-franchisee all other information disclosed to it by the original franchisor. The sub-franchisee may also have to disclose certain information to the original franchisor where it is stipulated in the original franchise agreement or the original franchisor is directly involved: for instance, whether the original franchisor will provide training to the sub-franchisees, or whether the sub-franchisees must purchase certain goods or services from the suppliers designated by the original franchisor.

Is there any obligation for continuing disclosure?

According to the Administration of Information Disclosure for Commercial Franchise Operations Procedures and Administration of Commercial Franchise Operations Regulations, in the case of any material change to the disclosed information, the franchisor shall notify the franchisees of such change in a timely manner.

How do the relevant government agencies enforce the disclosure requirements?

If a franchisor violates the disclosure requirements, its franchisee may report the violation to MOFCOM or its local counterpart.

Upon verifying the violation, MOFCOM (or its local counterparts) will request that the franchisor remedies it and a monetary fine of between 10,000 and 50,000 renminbi will be imposed on the violating franchisor. In the case of a serious violation, a fine of between 50,000 and 100,000 renminbi will be imposed and MOFCOM will make a public announcement regarding the violation.

In addition to any laws or government agencies that specifically regulate offering and selling franchises, what are the general principles of law that affect the offer and sale of franchises? What other regulations or government agencies or industry codes of conduct may affect the offer and sale of franchises?

As a written franchise agreement must be signed, the PRC Contract Law (promulgated by the National People's Congress and effective as of 1 October 1999) and relevant judicial interpretations will apply to formation, interpretation, performance and liabilities related to the franchise agreement.

In addition, as mentioned in question 19, the PRC Civil Code (adopted at the Fourth Session of the Sixth National People's Congress, promulgated by Order No. 37 of the President of the People's Republic of China on 12 April 1986, and effective as of 1 January 1987) is another critical source of law: adjudicators



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frequently refer to its doctrines and principles when the specific franchise statutory provision is in absence.

Do other laws affect the franchise relationship?

In addition to the Contract Law and the Civil Code that govern the validity, interpretation, performance and other areas of a franchise agreement, the franchisor and franchisee shall also comply with several other laws, including advertisement law (in respect of advertising), trademark law (in respect of trademark protection and licensing), and some regulatory requirements, such as Regulations on Prohibition of Pyramid Selling.