

具有中国特色的特许经营 FRANCHISING WITH CHINESE CHARACTERISTICS:

法律的分析比较概况 A Comparative Introduction to the Law

Paul Jones

Jones & Co. 钟保禄律师事务所 Джоунс и Ко.
pjones@jonesco-law.ca
416-703-5716

China Franchise Summit
Beijing
April 10, 2008

NEW REGULATION – 条例 (Tiaoli)

中华人民共和国国务院令 第485号

People's Republic of China State Council
Ordinance No. 485

《商业特许经营管理条例》 "Commercial Franchise Administration Regulation"

已经2007年1月31日国务院第167次常务会议通过，现予公布，自2007年5月1日起施行。
adopted on January 31, 2007 at 167th Regular Meeting of the State Council, in effect from May 1,
2007.

NEW ADMINISTRATIVE MEASURES – 办法 (Banfa)

商务部令2007年第15号

商业特许经营备案管理办法

Ministry of Commerce 2007 Decree No. 15

Commercial Franchise Registration Administrative
Measures

商务部令2007年第16号

商业特许经营信息披露管理办法

Ministry of Commerce 2007 Decree No. 16

Commercial Franchise Information Disclosure
Administrative Measures

Franchising in China

北京市海淀区基层人民法院

Haidan District Court – Beijing

January 2005 to May 2006 - 47 franchise cases

36% classed as deliberate fraud – 17 cases – all about sale of franchises

32% classed as breach of contract – 15 cases

30% classed as non-compliance with system standards by the franchisee – 14 cases

2% classed as vague drafting – 1 case

Franchising in China

黄海燕 (Huang Haiyan) v. 北京汉森美容有限公司 (Beijing Hansen Cosmetology Limited Co.) 北京朝阳区人民法院 (Beijing Chaoyang District People's Court) (2005) 朝民初字第 24486 号 (November 16, 2005)

该信息披露义务的要旨在于使加盟商能够在掌握了各种信息的程度上作出正确的判断，是决定加盟商能否客观认识特许经营权及能否公平交易的基础。信息披露的目的在于防止欺诈、促进公众的整体利益和促进投资分析。因此，在特许经营中，特许人违反信息披露义务，也构成欺诈。

Franchising in China

The essence of the duty to disclose is to enable the prospective franchisee to decide whether it understands the business objectives and its rights, and whether the franchise offer is fair. The goal of such disclosure is to prevent fraud and therefore to promote investment analysis and the general public welfare. Therefore in franchising if a franchisor violates the disclosure requirement, this also constitutes fraud.

China's Legal System

- China has been developing a civil law system since the Qing Dynasty
- **1986** 中华人民共和国民法通则 (Zhonghua Renmin Gongheguo Minfa Tongze – General Principles of the Civil Law of the People's Republic of China)
 - **General Principle:** 第四条 民事活动应当遵循自愿、公平、等价有偿、诚实信用的原则. (Article 4 - In civil activities, the principles of voluntariness, fairness, making compensation for equal value, **honesty** and credibility shall be observed.)

China's Legal System

- 1999 - 合同法 (Hetong Fa - Contract Law)
Good Faith

第六条当事人行使权利、履行义务应当遵循诚实信用原则。

Article 6 The parties shall observe the principle of **good faith** in exercising their rights and fulfilling obligations.

China's Legal System

Pre-Contractual Good Faith

第四十二条 当事人在订立合同过程中有下列情形之一，给对方造成损失的，应当承担损害赔偿责任：（一）假借订立合同，恶意进行磋商；（二）故意隐瞒与订立合同有关的重要事实或者提供虚假情况；（三）有其他违背诚实信用原则的行为。

China's Legal System

Art. 42 In the making of a contract, the party that falls under any of the following circumstances, causing loss to the other party, shall hold the liability for the loss.

- (1) engaging in consultation with malicious intention in name of making a contract;
- (2) concealing intentionally **key facts** related to the making of the contract or providing false information;
- (3) taking any other act contrary to the principle of **good faith**

Civil Law & Common Law

Differences:

- Common Law

- law is developed from decisions in individual cases, or is set out precisely in statutes
- vagueness in drafting is strongly avoided – “bright line” test
- rule in contract formation is ***caveat emptor*** or “buyer beware”

- Civil Law

- law is developed from general principles and then applied to specific matters
- the general principles are often set out in a code
- the rule in contract formation is frequently “pre-contractual” good faith” – also known as ***culpa in contrahendo***

Civil Law & Common Law

German Civil Code

- In 2002 Germany amended its civil code (Bürgerliches Gesetzbuch or BGB) to codify the doctrine of *culpa in contrahendo* (fault in negotiating).
- § 241(2) Das Schuldverhältnis kann nach seinem Inhalt jeden Teil zur Rücksicht auf der Rechte, Rechtsgüter und Interessen des anderen Teils verpflichten.

(An obligation may require each party to have regard to the other party's rights, legally protected interests and other interests) ...

Civil Law & Common Law

German Civil Code cont'd

§ 311 Ein Schuldverhältnis mit Pflichten nach § 241(2) entsteht auch durch...
(2) die Anbahnung eines Vertrags, bei welcher der eine Teil im Hinblick auf eine etwaige rechtsgeschäftliche Beziehung dem anderen Teil die Möglichkeit zur Einwirkung auf seine Rechte, Rechtsgüter und Interessen gewährt oder ihm diese anvertraut, ...

(An obligation with duties in accordance with § 241(2) also arises as a result of...

(2)preparations undertaken with a view to creating a contractual relationship if one party permits the other party to affect his rights, legally protected interest or other interest or entrusts them to that party, ...)

Civil Law & Common Law

German Decisions

Landgericht Kaiserslautern – Aktenzeichen 4 O 607/00, 26 Mai 2004

Die Klägerin hat aus dem Gesichtspunkt der *culpa in contrahendo* wegen Verletzung vorvertraglicher Aufklärungs- und Informationspflichten einen Anspruch gegen die Beklagte auf Schadensersatz. Der Franchisegeber hat bei Verhandlungen über den Abschluss eines Vertrages die Verpflichtung, den anderen Teil über Umstände aufzuklären, die zur Vereitelung des Vertrages zweckgeeignet sind und für die Entschließung des anderen Teils von wesentlicher Bedeutung sind (vgl. OLG Rostock 1996, 13 ff. m. w. N.). Zu solchen Umständen gehören, ohne dass es weiterer Begründung bedarf, insbesondere Angaben über die Gewinnerwartung und Rentabilitätsberechnung.

Civil Law & Common Law

German Decisions cont'd

Landgericht Kaiserslautern – Aktenzeichen 4 O 607/00, 26 Mai 2004

The Plaintiff has a claim against the Defendant based on the doctrine of culpa in contrahendo because of its breach of its pre-contractual duty to provide education and information, which breach gives rise to compensation. Before concluding a contract the Franchisor has an obligation to explain to the other party facts that would thwart the purpose of the contract and that are of substantial importance to the other party in the resolution of the negotiations (see Rostock High Court 1996, ff. m.w.N.). Such circumstances include particularly, without further justification, information regarding expected profits and financial feasibility.

Civil Law & Common Law

Québec Civil Code

6. Toute personne est tenue d'exercer ses droits civils selon les exigences de la bonne foi.

7. Aucun droit ne peut être exercé en vue de nuire à autrui ou d'une manière excessive et déraisonnable, allant ainsi à l'encontre des exigences de la bonne foi.

1375. La bonne foi doit gouverner la conduite des parties, tant au moment de la naissance de l'obligation qu'à celui de son exécution ou de son extinction.

Civil Law & Common Law

Québec Civil Code cont'd

6. Every person is bound to exercise his civil rights in good faith.

7. No right may be exercised with the intent of injuring another or in an excessive and unreasonable manner which is contrary to the requirements of good faith.

1375. The parties shall conduct themselves in good faith both at the time the obligation is created and at the time it is performed or extinguished

Civil Law & Common Law

Québec Decisions

Cadieux c. St-A. PhotoCorporation, Cour supérieure, 9 avril 1997

La bonne foi est le fondement de toute relation contractuelle. Elle doit gouverner la conduite des parties...La réticence ou l'omission de lui révéler la réalité entourant le studio a vicié le consentement donné: ce motif justifie l'annulation du contrat de franchise et le remboursement des sommes versées.

Good faith is the basis of all contractual relations. It should govern the conduct of the parties...The hesitation or omission of the defendant [franchisor] to reveal the reality regarding the studio vitiated the consent given: this justifies the annulment of the franchise agreement and the reimbursement of payments made.

Common Law Franchise Regulation

Development in the U.S.

- *Caveat emptor* or buyer beware does not work in the sale of securities – 1929 – *Securities Act of 1933*
- Too difficult for the buyer to conduct the investigation
- After World War II franchising grew rapidly in the U.S.

Common Law Franchise Regulation

Development in the U.S.

- 1971 – first franchise law – California’s *Franchise Investment Law*
- 1979 – Federal Trade Commission (“FTC”) – Franchise Disclosure Rule
- common law regulation- has a specific list of items to be disclosed – no requirement to disclose all material facts – matches U.S. securities law
- for example – no requirement to disclose historical sales figures or earnings claims

Civil Law & Common Law

SUPREME COURT OF CANADA

Martel Building v. Canada – [2000] – common law

Iacobucci and Major JJ. - In many if not most commercial negotiations, an advantageous bargaining position is derived from the industrious generation of information not possessed by the opposite party ...

It would defeat the essence of negotiation and hobble the marketplace to extend a duty of care to the conduct of negotiations....

...as a general proposition, no duty of care arises in conducting negotiations...

... a duty to bargain in good faith has not been recognized to date in Canadian law.

Civil Law & Common Law

Bank of Montreal v. Bail Ltée – [1992] – civil law

- under the previous *Code civil du Bas-Canada*

Gonthier J. –

The obligation to inform is now well established in Québec law...I believe that it is possible to outline a general theory of the obligation to inform based on the duty of good faith in the realm of contracts...

The advent of the obligation to inform is related to a certain shift that has been taking place in the civil law. While previously it was acceptable to leave it to the individual to obtain the information before acting, the civil law is now more attentive to inequalities in terms of information, and imposes a positive obligation to provide information in cases where one party is in a vulnerable position as regards information, from which damages may result.

Civil Law & Common Law

ABB Inc. v. Domtar, 2007 SCC 50

the duty to inform derives instead from the general principle of good faith (*Bank of Montreal v. Bail Ltée*, arts. 6, 7 and 1375 C.C.Q.) and the principle of free and informed consent. ...

This duty encompasses any information that is of decisive importance for a party to a contract, as Gonthier J. stated in *Bail*. It is therefore easy to imagine a situation in which a seller would be in breach of the duty even though no latent defect exists.”

New Regulation – 条例

General

- Applies to franchising activities conducted inside China (does not include Hong Kong or Macau)
- Persons involved in Franchising shall follow the principles of voluntariness, fairness honesty and good faith

New Regulation – 条例

Qualifications

特许人从事特许经营活动应当拥有成熟的经营模式，并具备为被特许持续提供经营指导、技术支持和业务培训等服务的能力。

特许人从事特许经营活动应当拥有至少2个直营店，并且经营时间超过1年。

Article 7 - To be engaged in franchising a franchisor shall have a mature business model, and shall be able to provide franchisees with continuous operational guidance, technical support, training and other services.

For a franchisor to be engaged in franchising it must have at least 2 directly-operated company-owned stores and have operated them for at least 1 year

Unresolved Question: Must the locations be directly owned?

New Regulation – 条例

Franchise Agreement – Article 11

1. Parties' basic information
2. Franchising provisions and term
3. Types of fees, method of payment
4. Standards of operation and technical support
5. Quality standards and guarantees
6. How promotion and marketing will occur
7. How complaints will be dealt with
8. How the agreement will be amended, cancelled or terminated
9. Default provisions and liability
10. Dispute settlement mechanisms
11. Other items agreed upon

New Regulation – 条例

Franchise Agreement

- Article 12 – right of rescission or “cooling off” period
- Article 13 – minimum term of three years – unless agreed
- Article 14 – operating manual and support
- Article 18 – no assignment without franchisor consent, confidentiality

New Regulation – 条例

Information to be Disclosed

– 30 days in advance

Article 22

(一) 特许人的名称、住所、法定代表人、注册资本额、经营范围以及从事特许经营活动的基本情况；

(1) the franchisor's name, place of business, legal representative, registered capital, the scope of its franchise business and basic information about its franchise activities;

Similar to Item 1: *The Franchisor, Its Predecessors, and Affiliates* in the new FTC Rule format in the U.S.

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(二) 特许人的注册商标、企业标志、专利、专有技术和经营模式的基本情况；

(2) basic information about the franchisor's registered trademarks, business logos, patents, proprietary technology and operational or business format model;

Similar to Item 13: Trademarks and Item 14: Patents Copyrights and Proprietary Information in the new FTC Rule format in the U.S.

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(三) 特许经营费用的种类、金额和支付方式（包括是否收取保证金以及保证金的返还条件和返还方式）；

(3) the type, amount and method of payment for franchise fees, (including whether security deposits are required and the conditions and method of refunding a security deposit);

Similar to *Item 5: Initial Fees* and *Item 6: Other Fees* in the new FTC Rule format in the U.S.

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(四) 向被特许人提供产品、服务、设备的价格和条件;

(4) the costs and the terms and conditions for the products, services and equipment provided by the franchisor;

The requirements of Article 22(4) of the Tiaoli and Article 5(4)(1) to (3) of the Disclosure Banfa are similar to *Item 8: Restrictions on Suppliers* of the U.S. FTC Rule but do not have the specific focus on amounts (proportion) nor on the possible conflict of interest on the part of the officers of the franchisor that are in the U.S. Rule.

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(五) 为被特许人持续提供经营指导、技术支持、业务培训等服务的具体内容、提供方式和实施计划；

(5) detailed content, delivery methods and implementation plan regarding the continuous services to be provided to the franchisee, including operating guidance, technical support, training and other services;

Although some of this information would be disclosed under *Item 9: Franchisee's Obligations* and *Item 11: Franchisor's Obligations* in the U.S., the wording here is different from the U.S. disclosure requirements

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(六) 对被特许人的经营活动进行指导、监督的具体办法;

(6) detailed method of guidance and supervision regarding the franchisees' operations;

Although some of this information would be disclosed under *Item 9: Franchisee's Obligations* and *Item 11: Franchisor's Obligations* in the U.S., there really is no equivalent wording in the U.S. disclosure requirements

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(七) 特许经营网点投资预算；

(7) the investment budget for a franchise location;

Chinese does not have definite and indefinite articles. A number of translators, including those at MOFCOM, have translated this sentence using “the,” thereby implying that the investment budget to be provided should be specific to the location proposed to the franchisee.

Article 22(7) of the Tiaoli and Article 5(7)(1) of the Disclosure Banfa together require something similar to *Item 7: Initial Investment* under the U.S. rules

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(八) 在中国境内现有的被特许人的数量、分布地域以及经营状况评估;

(8) the number and location of existing franchise outlets within the territory of China, their distribution by region, and an assessment of their business performance;

Before the release of the Disclosure Banfa there was a debate as to the meaning of 经营状况评估 (assessment of their business performance). Common law lawyers read this in a restrictive manner, some suggested that a table of the locations opened and closed would be sufficient.

In the U.S. *Item 19: Financial Performance Representations* disclosure of the financial performance of the locations (previously known as “earnings claims” is optional.

New Regulation – 条例

Information to be Disclosed

Article 22 (8) cont'd

Then in late April the Disclosure Banfa was released
Article 5(8)(2) requires:

2、对被特许人进行经营状况评估情况，特许人披露被特许人实际或预计的平均销售量、成本、毛利、纯利的信息，同时应当说明上述信息的来源、时间长度、涉及的特许经营网点等，如果是估算信息，应当说明估算依据，并明示被特许人实际经营状况与估计可能会有不同

2. Information regarding an evaluation of the operations of the franchisees. The franchisor shall disclose information regarding the franchisees actual or estimated average gross sales, costs, gross profits and net profits, and describe the relevant time periods and source of the data and the outlets involved. If the information is estimated, the basis for such estimates shall be provided and explained and shall expressly state that actual business operations may be different from the estimates.

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(九) 最近2年的经会计师事务所审计的财务会计报告摘要和审计报告摘要；

(9) summaries of the financial statements and audit reports, audited by an accounting firm, for the most recent 2 years;

This is similar to *Item 21: Financial Statements* in the new FTC Rule format in the U.S. However the U.S. Rule specifies the standards under which these must be prepared.

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(十) 最近5年内与特许经营相关的诉讼和仲裁情况；

(10) franchise related lawsuits and arbitrated matters for the last five years and their status;

This is similar to *Item 3: Litigation* and *Item 4: Bankruptcy* in the new FTC Rule format in the U.S. However “bankruptcy” is not specifically mentioned.

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(十一) 特许人及其法定代表人是否有重大违法经营记录;

(11) whether the franchisor or its management legal representative have been convicted of serious illegal operations;

This is similar to *Item 3: Litigation* in the new FTC Rule format in the U.S.

New Regulation – 条例

Information to be Disclosed

Article 22 cont'd

(十二) 国务院商务主管部门规定的其他信息。

(12) other information specified by the
Commerce Department of the State Council.

There is nothing comparable to this in the U.S.
Rule

New Regulation – 条例

Information to be Disclosed

第二十三条 特许人向被特许人提供的信息应当真实、准确、完整，不得隐瞒有关信息，或者提供虚假信息。

特许人向被特许人提供的信息发生重大变更的，应当及时通知被特许人。

特许人隐瞒有关信息或者提供虚假信息的，被特许人可以解除特许经营合同。

Article 23 – The information provided by the franchisor to the franchisee shall be true, accurate and complete and shall not conceal any relevant information, or provide any false information.

If there is a significant change in the information provided by the franchisor to the franchisee, the franchisor shall promptly inform the franchisee.

Promotion & Marketing

第十七条 特许人向被特许人收取的推广、宣传费用，应当按照合同约定的用途使用。推广、宣传费用的使用情况应当及时向被特许人披露。

特许人在推广、宣传活动中，不得有欺骗、误导的行为，其发布的广告中不得含有宣传被特许人从事特许经营活动收益的内容。

Article 17 – Fees for promotion and marketing of the franchise system shall be applied in accordance with the terms of the franchise agreement. Promotional and marketing expenses shall be promptly disclosed to franchisees.

A franchisor shall not engage in deceit or misleading behavior in the promotion or marketing of the franchise. A franchisor shall not make claims in its advertising about franchisee earnings from their franchise operations.

Promotion & Marketing

Qingdao Sudai Beauty Chain: (August 24, 2007). The picture shows a placard with the earnings claim. A law suit has been commenced, according to a news report.



Filing or Registration

第八条 特许人应当自首次订立特许经营合同之日起15日内，依照本条例的规定向商务主管部门备案。。。。。

Article 8 – In accordance with the provisions of this Regulation a franchisor shall register at the relevant commercial department within 15 days after signing its first franchise agreement....

The Chinese phrase “备案” (bei an) literally means to “set up a file” or “set up a record” and this Article is often translated accordingly.

Filing or Registration

Documents Required to be Submitted:

Tiaoli -

1. Business license or registration certificate
2. Standard form of franchise agreement
3. Franchise operating manual
4. Marketing plan
5. Undertaking regarding compliance
6. Other prescribed documents

Filing or Registration

Documents Required to be Submitted:

Banfa — (items not already mentioned in the Tiaoli)

1. Basic information regarding the system
2. Location of all outlets in China
3. Trademark registration certificate
4. Evidence of having operated two stores for one year
5. Table of contents of the operating manual
6. Evidence of other required approvals

Liability & Enforcement

Tiaoli - Articles 24 – 30 specify the administrative fines

No specific provision regarding private right of action. In civil law generally and Chinese law in particular a private right of civil action in court always exists.

Court decisions under the new Tiaoli are not yet available

Liability & Enforcement

Under Previous Banfa (December 31, 2004)

刘红朝 诉 古拉索(北京)科教文化有限公司

北京市朝阳区人民法院 November 18, 2005

一方以欺诈的手段使对方在违背真实意思的情况下订立的合同，受损害方有权请求法院撤销合同。

Where one party has deceived the other party and caused it to enter into a contract against its will, the injured party has the right to request that the court set aside the contract.

Liability & Enforcement

Liu Hongchao v. Gulasuo Education and Culture

Beijing Chaoyang District Court (November 18, 2005)

此外，依据商务部2004年12月31日颁布《商业特许经营管理办法》的要求，特许人在签订特许经营合同前应当以书面形式向被特许人披露其基本信息资料。设立该披露义务旨在使加盟商能客观地知悉特许人的经营情况，了解投资的风险，其目的就在于防止欺诈，促进行业的发展，保护投资人的利益。

Liability & Enforcement

Liu Hongchao v. Gulasuo Education and Culture cont'd.

In addition, according to the “Commercial Franchise Administrative Measures” promulgated by the Ministry of Commerce on December 31, 2004 before signing the franchise agreement the franchisor shall disclose basic information to the franchisee in a written format. The establishment of the disclosure obligations to franchisees is to ensure that the franchisees will be objectively informed of the franchisor’s operations and understand the risks of investment, thus preventing fraud and promoting the development of the industry and protecting the interests of investors.

Liability & Enforcement

Liu Hongchao v. Gulasuo cont'd.

综上，依据《中华人民共和国合同法》第五十四条第二款、第五十八条之规定，判决如下：

一、撤销二00五年五月二十日，古拉索(北京)科教文化有限公司与刘红朝签订的加盟合同

In summary based on the Contract Law of the People's Republic of China Article 54(2) and Article 58 the court decides that:

The contract signed on May 20, 2005 between Gulasuo (Beijing) Education & Culture Company and Liu Hongchao should be revoked;

Questions

1. Can a foreign franchisor franchise directly into China or must it set up a Chinese corporation?
2. If a foreign franchisor does not own or operate any locations, but its affiliate (关联公司) does, is it qualified to franchise in China?
3. What auditing standards are acceptable for the financial statements that are to be disclosed? Are financial statements audited in accordance with U.S. Generally Accepted Accounting Principles (GAAP)?
4. Can an experienced foreign franchisor set up a shell corporation with few assets for international franchising and still qualify as a franchisor in China?

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