



PRC Retail Newsflash
14 November 2006

**Newsflash: New Measures Addressing Fair Trade Relationships
between Retailers and Their Suppliers**

On 15 November 2006, the *Administrative Measures Regarding Fair Trade between Retailers and their Suppliers (Measures)* will take effect. The Measures were jointly promulgated on 13 October 2006 by the Ministry of Commerce, the National Development and Reform Commission, the Ministry of Public Security, the State Administration of Taxation and the State Administration of Industry and Commerce.

Overview

China's retail market has seen a tremendous increase in department stores that distribute a substantial amount of local and international products. In practice, large single-brand or multi-brand chain/department store retailers have been the dominant players in this industry and, accordingly, often take advantage of their suppliers, which are dependent on their distribution channels. Therefore, these Measures have been promulgated in order to regulate monopolies in the retail sector and facilitate fair competition between retailers and their suppliers.

"Retailers" in the Measures refer to those enterprises and their branches that directly sell merchandise to consumers, and which have an annual sales amount of more than RMB10m. "Suppliers" in the Measures refer to enterprises, their branches or even individual entrepreneurs registered with the local Administration of Industry and Commerce that directly supply retailers with merchandise and related services, including producers and distributors, etc.

The key provisions of the Measures are summarized below.

Prohibited Activities

Retailers are prohibited from engaging in any of the following activities:

- **Forced allocation of sales profits:** forcing suppliers to share sales profits with the retailer (unless agreed upon by the parties), or collecting its shared portion of sales profits on the basis that its sales target amount has been achieved, where in fact it has not.
- **Restricting prices:** setting a limit on the price of merchandise sold by suppliers directly to consumers or retailers. That is, a retailer may not restrict the suppliers from selling its merchandise in any other department store or chain store branch at a retail price lower than that for the same item sold by the retailer itself.

- **Employment:** requesting suppliers to allocate sales staff to work in the retailer's operating premises (e.g., department stores) unless (a) such staff only provide services in respect of the merchandise provided by the suppliers; or (b) both the suppliers and the retailer in question have reached an agreement in respect of the work scope, working hours and term with respect to each staff member, and the retailers shall bear all employment-related costs in this regard.
- **Unreasonable fees:** charging suppliers fees for signing/renewing contracts; renovating or decorating stores which are not affiliated with or related to the suppliers or the suppliers' merchandise; holidays, anniversaries, new openings, re-openings, IPOs, mergers and acquisitions, when the retailer does not provide any additional promotional services.

Where a retailer collects any promotional sales service fees from suppliers, it must obtain the suppliers' prior consent, and the parties must have entered into a contract (which contract must state the category, content and term of the service; category, calculation standards, amount and payment method of the promotional fees, and liabilities for breach, etc). A retailer is required to issue invoices to suppliers for all promotional service fees it charges. This provision may be useful to suppliers when negotiating contracts with retailers, as a means to protect their own interests.

- **Overdue payments:** failing to pay suppliers within 60 days of receiving their merchandise.
- **After-sales service restrictions:** restricting the provision of merchandise or post-sale services by suppliers to other retailers is prohibited.
- **Wear-and-tear expenses:** forcing suppliers to assume liability to merchandise wear and tear, unless the supplier expressly consents to the same in its contract with the retailer.

Although the Measures focus on the actions of retailers, they also specify 2 activities in which suppliers are prohibited from engaging, namely: forcing the sale of merchandise that was not ordered by a retailer, and preventing a retailer from selling merchandise that has been supplied by other suppliers.

Penalties

Unless otherwise specified by PRC law, penalties for violating the Measures include fines of up to RMB30,000 and the issuance of a public announcement of the violation.

Commentary

Given that it has become the general practice for retailers to effectively dictate the terms of their contracts with their suppliers, the Measures finally provide suppliers with a somewhat stronger bargaining position during negotiations with retailers. However, the penalties imposed on retailers that engage in the abovementioned prohibited activities are likely to have little effect, as the profits obtained by retailers from the sale of merchandise are generally much higher. Moreover, violation of the Measures does not invalidate the supply contracts between retailers and their suppliers. Accordingly, there has been much skepticism regarding the effectiveness of the Measures.

We trust that you find the above summary useful. If you have any questions regarding the Measures, please contact June Lei of TransAsia Lawyers (jlei@TransAsiaLawyers.com).

Beijing

Suite 2218 China World Tower 1
1 Jianguomenwai Avenue
Beijing 100004, China
Tel: (86 10) 6505-8188
Fax: (86 10) 6505-8189/98

Shanghai

Unit 1101 Platinum
233 Tai Cang Road
Shanghai 200020, China
Tel: (86 21) 6141-0998
Fax: (86 21) 6141-0995/6

<http://www.TransAsiaLawyers.com>

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