



PRC Retail Law Newsflash
25 June 2007

NEW ADMINISTRATIVE RULES ON THE FILING OF COMMERCIAL FRANCHISES

This issue is a follow-up to our Newsflash of 30 April 2007.

Further to the promulgation of the State Council's *Administrative Regulations for Commercial Franchises* (**Franchise Regulations**) on 6 February 2007, the Ministry of Commerce (**MOFCOM**) promulgated on 30 April 2007 the related *Administrative Rules for the Filing of Commercial Franchises* (**Filing Rules**) to consolidate and regulate the legal framework for franchising in China. Both sets of legislation became effective as of 1 May 2007.

Key Provisions of the Filing Rules

• **Online Filing System**

Articles 3 and 5 of the Filing Rules provide that a franchisor engaging in commercial franchise activities in China must provide the MOFCOM with basic information on its business including the following:

- basic information on its franchise;
- locations of all of its stores in China;
- its market plan;
- copies of the registration certificates of the trademarks, patents and other business resources relating to its business operations; and
- a sample franchise contract.

To this end and, pursuant to Article 10 of the Franchise Regulations, the MOFCOM has set up an online filing system on its website to publish such information together with a list of names of those franchisors which have complied with this disclosure requirement.

However, as of the date of this Newsflash, no information relating to any franchisor has been published on the website.

- **Grace Period**

For a franchisor which has been engaging in franchise business before 1 May 2007, a 1-year grace period is given for it to complete the filing procedures, *i.e.*, it must complete all filing procedures before 1 May 2008. In contrast, all other franchisors must complete the filing procedures within 15 days after the execution of the first franchise contract between the franchisor and franchisee in China.

- **Annual Report**

Article 19 of the Franchise Regulations requires franchisors to furnish the MOFCOM within the first quarter of each year a report relating to the conclusion of any franchise contracts in the preceding year. In this regard, the Filing Rules also stipulate that franchisors must report to the MOFCOM before March 31st of each year, information of any franchise contract that has been revoked, renewed or modified during the preceding year.

- **Revocation of Filing**

The Filing Rules set forth certain conditions based on which the MOFCOM may revoke the filing of a franchise. These conditions mainly involve severe misconduct by the franchisor, *e.g.*, conducting illegal business operations, deliberate concealment of any relevant information or providing false information. Details of such revocation will also be listed on the MOFCOM's website.

- **Filing Rules extend to Direct Offshore Franchises**

Article 17 of the Filing Rules applies to an overseas franchisor operating a franchise business in China, and which definition also extends to those franchisors from Hong Kong, Macao and Taiwan.

Commentary

- The Filing Rules outline the specific information and documents that are required to be filed by franchisors to the MOFCOM. These requirements are, *inter alia*, intended to provide potential franchisees with the relevant information of the franchisors to enable them to make an informed decision before entering into any franchise contracts. It is, however, not to be considered as a pre-requisite to an approval of a franchise business in China.¹
- The Filing Rules provide some useful clarification on the interpretation of Article 7 of the Franchise Regulations. As discussed in our previous Newsflash of 30 April 2007, Article 7 of the Franchise Regulations provides confusingly that “A franchisor engaged in franchising activities shall own at least 2 directly-operated stores (in operation for more than 1 year)”. As a result, it was unclear as to whether direct franchises in China by overseas franchisors without a local onshore entity would be permitted.

This uncertainty is remedied by Article 5(6) of the Filing Rules which allows a foreign franchisor to apply for a certificate from the MOFCOM stipulating that it has satisfied the

¹ The filing requirement as prescribed in the Filing Rules is not a pre-requisite to an approval of a franchise business in China. It is merely a compulsory obligation required by the MOFCOM to identify a franchise operator in China. At present, the undertaking of a franchise business does not require any approval, license or permit from the MOFCOM.

requirement prescribed in Article 7 of the Franchise Regulations. Under such circumstances, if any of the franchisor's direct sales stores is located outside of China, it must provide with the application to MOFCOM a notarized business certificate of that store (with a Chinese translation) and endorse by the local PRC embassy or consulate. As such, the Filing Rules (in particular Articles 5(6) and 17), read as a whole and taken together with the Franchise Regulations, confirm that it is possible to set up direct franchises in China without the need to have a local store presence.

Indeed, based on our recent discussion with the MOFCOM, an application for the establishment of such a direct franchise has already been allowed.

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We trust that you find this newsletter useful. If you have any questions on this subject or any other area of retail law, please contact:

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Full English translation of any aforementioned PRC legislation as well as other rules and regulations are available for purchase upon request.

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