

Fair Trade Commission Disposal Directions (Policy Statements) on the Business Practices of Franchisers

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1. Background

In recent years, franchise businesses have grown rapidly in Taiwan, increasing both in scope of operations and the types of industries involved. The increase in franchise businesses and operations has seen a corresponding increase in competition restriction and unfair competition issues in transactions between franchisers and franchisees.

In order to maintain the trading order in the franchise market and ensure fair competition among franchise businesses, the FTC has compiled and analyzed patterns of conduct of franchisers that could be considered in violation of the Fair Trade Law, and established this set of Guidelines for franchisers to follow.

2. Terminology

The terms in these Guidelines are defined as follow:

- (1)The term "franchiser" refers to an enterprise in a franchise relationship that licenses the trademark or operational approaches, and assists or counsels the management of franchisee business, and collects the corresponding costs for such services from the franchisee.
- (2)The term "franchisee" refers to the other enterprise in the franchise relationship described in the preceding paragraph that uses the trademark or operational approaches licensed by the franchiser, receives assistance or counsel from the franchiser, and pays the franchiser the corresponding costs for such services.
- (3)The term "franchise relationship" refers to an ongoing relationship in which a franchiser licenses a franchisee through a contract to use its trademark or operational approaches, and

assists or counsels the franchisee to manage the business, while the franchisee pays the corresponding costs for such services. However, the purchase of products or services (hereinafter referred to as The Products) at wholesale rates or lower for resale or leasing is not included under this arrangement.

- (4) The term "preparation to enter a franchise relationship" refers to the payment of certain fees by the trading counterpart, and the signing of documents related to entry into a franchising relationship such as a draft agreement, appointment, or letter of intent in advance of the franchiser and trading counterpart entering a franchise relationship, and agreement that withdrawal from the relationship shall result in forfeiture of all fees paid or liability for compensation.
- (5) The term "payment of corresponding costs" refers to the franchise fee, licensing fee, training charges, as well as expenses for the products and capital equipment a franchisee is required to pay the franchiser or fiduciary to establish and maintain the franchise relationship.

3. Information Disclosure Guidelines

Franchisers providing their trading counterparts important franchise information in writing within 10 days or a reasonably determined timeframe prior to entering into the franchise operation relationship, shall not be considered to be withholding important information and therefore not considered in violation of Article 24 of the Fair Trade Law.

Examples of important franchise information, as stated in the preceding paragraph, include the following:

- (1) Startup costs: such as the cost or estimated total franchise fees, training, merchandise purchases, capital equipment, and interior decoration, paid to the franchiser or designee.
- (2) Operating expenses: such as licensing fee calculation and payment, and regularly paid expenses for management guidance, the purchase of merchandise or raw materials, including the corresponding items and estimated amounts, paid to the franchiser or designee.
- (3) Trademark rights, patents and copyrights involved, their contents, periods of validity, extent of authorization, and corresponding restrictions.

- (4) Contents and methods of operational assistance, training, and guidance.
- (5) Plans for setting up other franchisees of the same franchise system in a franchisee's existing area of operation.
- (6) Statistical data on the number and locations of franchisees of the same franchise system in the same county/city, and the statistics on the ratio of contract nullifications and terminations made during the previous year.
- (7) Restrictions applied to the franchise relationship during the contract period:
 - A. Terms regarding the supply of merchandise, raw materials, capital equipment and interior appointments and related matters (such as designated specifications, and names of suppliers or contractors.)
 - B. The items and quantities of products or raw materials to be purchased.
 - C. Other restrictions with regard to the franchise operation relationship.
 - D. Interior decoration must be conducted by a contractor designated by the franchiser, according to given specifications.
 - E. Other restrictions on franchise operation relationships.
- (8) Conditions for the alteration, termination and nullification of franchise contracts and manners of conduct.
- (9) If such financial forecast data such as projected business turnover or projected profits is available, methods of calculation or actual current franchisee operational performance should be supplied for corroboration.

Data in the preceding items may be provided via disc or other electronic media with written permission of trading counterpart.

4. Contract Review and Establishment

Contracts entered between franchisers and trading counterparts concerning the franchise operation relationship may not include such obviously unfair conduct as:

- (1) Prior to entering into a written contract regarding franchise operation, franchisers are required to allow at least 5 days or a reasonable timeframe determined in line with each case for trading counterparts to review the contract.

(2) In cases under which the contract is not given to the trading counterpart within 30 days of signing, where a delay is caused by circumstances not attributable to the franchiser (e.g. the franchisee is located on an outlying island or remote area, real estate mortgage procedures not attributable to the franchiser, or that are attributable to the franchisee, resulting in failure to produce the contract), shall not be subject to this restriction.

5. Post-contract Restriction of Competition

After having entered a franchise operation relationship, franchisers may not abuse their relative advantageous status on the basis of the dependence of their franchisees, and engage in any of the following conduct:

- (1) differentiated treatment in regards to price, trading terms or whether to engage in transactions with various franchisees or other businesses at the same competition level without justifiable cause.
- (2) demanding franchisees purchasing merchandise to purchase other goods (i.e. tie-in sales) without justifiable cause.
- (3) demanding without justified cause that franchisees purchase specific quantities of goods or raw materials, and disallowing the return of goods, and where such quantities exceed the volume the franchisee is capable of selling within a reasonable number of business days or surpasses the inventory quantity a franchisee requires.

6. Legal Effects

An enterprise violating the terms and conditions of Item 3 and Item 4, sufficient to affect the trading order, can be considered in violation of Article 25 of the Fair Trade Law.

An enterprise violating the terms and conditions of Item 5 Subparagraph 1, and that is suspected of restricting competition, can be considered in violation of Article 20 Subparagraph 2 of the Fair Trade Law.

An enterprise in violation of Item 5 Subparagraph 2 and Subparagraph 3, and that is suspected of restricting competition, can be considered in violation of Article 20 Subparagraph 5 of the Fair Trade Law.

7. Other Regulations on Unfair Competition

In addition to being subject to these Disposal Directions, franchiser business practices shall also abide by the "Fair Trade Commission Disposal Directions (Guidelines) on Handling Cases Governed by Article 21 of the Fair Trade Law," "Fair Trade Commission Disposal Directions (Guidelines) on Handling of Cases of Comparative

Advertising," and "Fair Trade Commission Disposal Directions (Guidelines) on the Application of Article 25 of the Fair Trade Law."