

**LEGAL ASPECTS OF FRANCHISING IN VIET NAM***(The Vietnam Economic Times, June 2006)*by Diep Hoai Nam  
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With the rise in consumer income, strong GDP growth and new franchising legal instruments recently introduced, the conditions are becoming more favorable for foreign franchisors wanting to expand to Vietnam. On the busy streets of Hanoi and Ho Chi Minh City there are more and more franchise and franchise-like businesses operating such as Pho 24 restaurants, KFC and Lotteria outlets, Kinh Do Bakeries, A Lo Tra tea houses and Trung Nguyen cafes.

Previously, franchises were operating in Việt Nam with little legal guidance on how they can properly enter the market. This is not surprising as the franchising concept is new to the country, in fact the concept has only recently received formal legal recognition in the Commercial Law of 14 June 2005. Further, Decree 35-2006-ND-CP triggering the implementation and regulation of franchising activities in the Commercial Law only came into effect on 26 April 2006.

The literal English translation of franchising in Section 8 of the Vietnamese Commercial Law is “to sell a commercial right” (nhượng quyền thương mại), however, the Law aligns the franchising concept with a description similar to the Western notion by describing franchising as a commercial activity where the franchisee carries on a business in accordance with an established business system prescribed by the franchisor. The system may include trademarks, business or manufacturing know-how or other marketing concepts.

The new franchising Decree also introduces the master franchise relationship to the Vietnamese legal vocabulary. In this relationship, the franchisor permits the master franchisee (or secondary franchisor) the right to sub-franchise the business system to other franchisees usually with exclusive rights to manage the system in a specific geographic region.

The Decree was partly inspired by the mandatory Australia Franchising Code which regulates the conduct of franchise businesses in Australia. The Franchising Code is unashamedly pro-franchisee and this preference is also reflected in the new Decree although, the Decree provides a higher level of Government scrutiny and is somewhat more onerous on the franchisor. For example, the immediate impact of the Decree is that any existing and new franchise system must now be registered with the Ministry of Trade otherwise administrative penalties will apply.

In addition, overseas franchisors must operate their franchise business for at least one year in any country before it can enter the Vietnamese market. And a Vietnamese master franchisee can only sub-franchise once it has operated the business in Việt Nam for at least a year. This provision is similar to China’s franchising regulation but the Chinese regulation is more rigorous as the foreign franchisor must operate at least two franchise businesses in China for a year without loss before it can roll out the franchise system.

The above measures shows that Vietnamese law intends to protect local businesses by ensuring that they at least purchase a franchising system that has been tested in the market and its profitability and performance can be gauged. As this is a new investment vehicle for Việt Nam there is the unease that without scrutiny local businesses might purchase unprofitable franchise businesses that have been marketed in overly favorable terms.

Hence, there is the additional requirement in the Decree for the franchisor to disclose certain information about the franchise system. The need for information disclosure very much underpins the Australian Franchising Code which has the objective of protecting franchisees from unconscionable and misleading conduct as well as minimizing disputes between the parties.

Under the Decree the franchisor must provide a disclosure document to the franchisee 15 days before the franchise contract is signed. The content of the disclosure document is currently being finalised by the Ministry of Trade in a Circular which is expected to have two disclosure regimes based on information that the franchisor must disclose and those that are voluntary. It is proposed that the franchisor must disclose the following information:

- any initial fees, investment and other financial obligations payable by the franchisee;
- any requirement that the franchisee must purchase equipment or supplies from the franchisor;
- obligations of the franchisor including training and site selection;
- the right of the franchisee to use trademarks and other intellectual property.

Therefore, other crucial information about the franchise such as its financial performance and the extent of the franchise network need only be disclosed voluntarily. That information are compulsory in the Franchising Code as well as other important protective measures for the franchisee including the obligation of the franchisor to provide annual financial information about the use of the marketing and other cooperative funds. The Code even insists the franchisee consult an independent legal advisor, business advisor or an accountant about the franchise agreement prior to signing the contract. There is also an entitlement for the franchisee to have a seven days cooling off period before the franchise agreement takes effect.

What is also similar between the Code and Decree is that they both allow the franchisor to unilaterally terminate the franchise agreement on almost the same conditions such as when the franchisee is bankrupt, does not have a business license or has committed a serious crime which damages the reputation of the franchise business. Both legal instruments also allow the franchisee to assign the franchise business and stipulate the situation in which the franchisor can refuse the assignment.

### **General tips on Franchising in Viet Nam**

In Vietnam the maintenance and development of good personal and professional relationships is usually more important than the legal relationship. Hence, before negotiating the franchise agreement it is essential that the franchisor selects an appropriate franchisee. The preferred franchisee at least should have adequate investment capital, shows enterprise and good understanding of the local business and market conditions, is loyal to the franchise system and can help enforce the intellectual property rights of the franchise business.

The latter criterion is critical because the key risk when entering the Vietnamese market is the weak intellectual property rights enforcement regime. Further, a trustworthy franchisee means the risk of disclosing any business secrets associated with the franchise system is lower.

It is also important that the parties adopt all the provisions of the franchising Decree and soon to be released franchising Circular in their franchise agreement and negotiations, in particular the information disclosure requirements. The parties should also clearly define any territorial rights of the franchisee and the site requirements of the franchise business.

Parties should consider the process for resolving any future disputes that may arise, keeping in mind that contract enforcement through the Vietnamese courts are sometimes weak. Parties are encouraged to implant in the franchise agreement an obligation to firstly discuss and negotiate any disputing issues before considering the costly path of arbitration.

It is also wise for parties to initially consult their business or legal advisors about the franchise operations in Việt Nam. The use of marketing consultants is prudent as franchise businesses usually fail because the goods and services provided are not appropriately catered to the local consumer market. These advisors may also assist the overseas franchisor find a compatible franchise partner for their Vietnamese expansion.