SUPPLEMENT - THAILAND-VIETNAM IP FOCUS 2010 How to ride the franchising boom

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Thomas J Treutler of Tilleke & Gibbins considers the possibilities for franchises in Vietnam

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With Vietnam's entry into the World Trade Organisation (WTO), it is expected that franchising activity in the country will increase markedly over the next few years. There are presently a handful of major franchises operating in the country, including Kentucky Fried Chicken, Subway, Lotteria, Jollibee, Pho 24, Gloria Jean's Coffees, Buntamita and Cartridge World. These franchises view Vietnam as a strong potential market, as it is the 12th most populous country in the world, with a young dynamic population that places a high premium on reputable international brands. In the past, Vietnamese law did not provide a clear basis for franchising arrangements, but the passage of Decree No 35 and Circular No 09 in 2006 laid the groundwork for franchising to develop in Vietnam.

The current laws and regulations governing franchising in Vietnam include the following:

- Commercial Law No 36/2005/QH11 passed by the National Assembly on June 14 2005 (Commercial Law);
- Decree No 35/2006/ND-CP of the Government dated March 31 2006 detailing implementation of the Commercial Law 2005 regarding franchising (Decree No 35);
- Circular No 09/2006/TT-BTM of the Ministry of Trade dated May 25 2006 providing guidelines on procedures for registration of franchising activities (Circular No 09); and
- Decision No 106/2008/QD-BTC of the Ministry of Finance dated November 17 2008 on regulating collection rates, policies for collection, payment, management and use of fees collected from registration of franchising (Decision No 106).

A foreign franchisor is not required to have a legal presence in Vietnam and is permitted to franchise in Vietnam without establishing a business entity in Vietnam. However, a foreign franchisor is required to have been in business for one year prior to franchising in Vietnam. A Vietnamese master franchisee must also have been in business under the foreign franchise for one year prior to sub-franchising in Vietnam. A foreign franchisor registers its activities with the Ministry of Industry and Trade (MOIT), while a local franchisor registers with the local Department of Industry and Trade. As discussed in further detail below, the Vietnamese franchisee shall have at least 15 days to review a disclosure document and the franchise agreement, but this requirement may be waived by the Vietnamese franchisee. The franchise agreement must be in Vietnamese and may be translated into English.

The regulations appear to require that a franchisee be a company rather than an individual. A franchisee is defined as a business entity that is granted a franchise. A prospective Vietnamese franchisee must be registered to engage in a line of business that is suitable and consistent with the goods or services contemplated by the franchise agreement. If the franchisee is a primary franchisee and wishes to sub-franchise, the franchisee shall operate a franchise for at least one year before it may sub-franchise. Franchisees may assign their franchise to another franchisee provided that the franchisor approves and the assignee satisfies the same requirements of the original franchisee.

An application to register franchising activities in Vietnam shall include the following:

- an application for registration of franchising activity in the form prescribed by the MOIT;
- a franchise description document in the form prescribed by the MOIT (which requires the franchisor's most recent audited financial report);
- a notarised copy of the business registration certificate or certificate of incorporation of the foreign franchisor certified by the competent body of the place where such foreign franchisor was established; and
- notarised copies of certificates of trade mark registration in Vietnam and/or overseas.

If these documents are in a foreign language, they must be translated into Vietnamese and notarised, and notarised and consularised in the case of business registration certificates or certificates of incorporation. At present, the fee to file a franchising application with the MOIT is D16,500,000 ($900). In theory, within two business days from the date of receipt of an incomplete or invalid application file, the MOIT shall provide written notice to the applicant to supplement and complete such file. Also in theory, within five business days from the date of receipt of a valid and complete application file, the MOIT shall register the franchising activity of the applicant and provide written notification to the applicant. In practice, delays are common and foreign franchisors should expect to wait up to three months for a completed review of their application dossier.

Franchisors are required to observe a number of disclosure requirements. For example, the franchisor must provide a franchise description document (similar to a disclosure document) and a model franchise agreement to a potential franchisee for the potential franchisee to review for 15 days prior to signing the franchise agreement, unless the parties agree otherwise (see Decree No 35, Art 8.2). Circular No 09 provides a standard form for the franchise description document.

The franchise description document requires information such as general information about the franchisor, initial investment and costs payable by the franchisee, other financial obligations of the franchisee, obligations of the franchisee to buy or lease equipment as designated by the franchisor, description of the market of goods/services to be franchised, terms of the franchising agreement, protection of trade marks and other intellectual property rights by the franchisor and pending litigation.

The law also prescribes a duty to update changes to the contents of a franchise description document. Specifically, the franchisor has an ongoing obligation to inform the relevant franchising registration authorities (that is the Ministry of Industry and Trade and/or local Service of Industry Trade) within 30 days when there are changes regarding the contents of the franchise description document (see Decree No 35, Art. 21).

The following disclosure information is subject to the duty to report changes to the relevant franchising authorities:

- Legal status of the franchisor (Decree No 35, Art 19.3(a));
- Name of the franchisor (Circular No 09, Appendix III, Part A, Point I.1);
- Address of the franchisor (Circular No 09, Appendix III, Part A, Point I.2);
- Telephone and fax (Circular No 09, Appendix III, Part A, Point I.3);
- Date of establishment of the franchisor (Circular No 09, Appendix III, Part A, Point I.4);
- Information on whether the franchisor is a master franchisor or master franchisee (Circular No 09, Appendix III, Part A, Point I.5);
- Type of business of the franchisor (Circular No 09, Appendix III, Part A, Point I.6);
- Sector of franchising (Circular No 09, Appendix III, Part A, Point I.7);
- Information on the registration of franchising activities at authorized government agencies (Circular No 09, Appendix III, Part A, Point I.8);
- Rights to use trademarks or service marks and any intellectual property of the franchisor (Circular No 09, Appendix III, Part A, Point II.1);
- Details on the trademarks and services marks and rights with respect to intellectual property registered under the law (Circular No 09, Appendix III, Part A, Point II.2); and
- Certificates of protection for industrial property in Vietnam or in foreign countries (Decree No 35, Art 19.3(b)).

The franchise description document is required to contain the following information related to intellectual property: (i) rights to use trade marks and other intellectual property (for example patents); and (ii) details on any relevant registered trade marks and other intellectual property.

In general, as a pre-requisite to franchising in Vietnam, the foreign franchisor should have a registered trade mark in Vietnam, otherwise it will not have enforceable trade mark rights in Vietnam. As a best practice, the foreign franchisor should have the registration for its trade marks in its own name as the registrant. If the local franchisee is the registrant of the trade mark, complications may arise if a dispute occurs between the foreign franchisor and the franchisee. Additionally, it is a best practice for the parties to execute and register a trade mark licence agreement.

A foreign franchisor is not required to have a legal presence in Vietnam and is permitted to franchise in Vietnam without establishing a business entity in Vietnam such as a limited liability company. Note that a Vietnamese limited liability company is subject to corporate income tax (CIT) at the rate of 25%. A foreign franchisor that does not establish a business entity in Vietnam will be considered a foreign contractor in Vietnam on the basis of the franchise agreement signed with Vietnamese franchisees. All fees generated under the franchise agreement, including royalties, administrative fees, advertising fees are subject to foreign contractor tax, rather than CIT at the rate of 25%. The two components of foreign contractor tax are Value Added Tax (VAT) and CIT (although at a rate much lower than 25%). VAT is calculated as follows:

> Amount of VAT payable = (VAT taxable turnover) x (VAT rate as % of taxable turnover) x (VAT rate)

In the case of franchising, the VAT rate as a % of taxable turnover is 50% and the VAT rate is 10%.

CIT is calculated as follows:

> Amount of PIT payable = (CIT taxable turnover) x (CIT rate as a percentage of taxable turnover)

The CIT rate as a percentage of taxable turnover may be 1% for food services which fall under the category of trading under the CIT regulations.

Vietnam has put in place a straightforward, simple yet solid, legal framework for franchises to legally operate in the country. With a population of 88 million people, nearly half of whom are under the age of 25 years old, it is likely that foreign franchises will continue to look to Vietnam as a high growth, high potential market, and it is therefore expected that franchising activity will continue to be strong in the coming years.

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