



The Franchise Lawyer

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THE FRANCHISE LAWYER

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Message from the Chair

By Edward Wood Dunham
Forum Chair

As I write this, over 800 of our colleagues have already registered for the 31st Annual Forum on Franchising. Given the relentless bad news about the economy and the increasingly depressing (and expensive) experience of air travel, this is a remarkable statistic. Our strong attendance is a testament to the great plenary sessions, workshops and social events that our able program chairs, Peter Klarfeld and Joe Fittante, have put together. No doubt it also reflects the attractions of Austin, one of America's most appealing cities. But I can't escape the feeling that there is something more at work here – something more fundamental about the Forum that helps explain the enduring loyalty and extraordinarily high participation rate of our members.

In this election season, virtually every candidate for federal office laments the partisan rancor that has paralyzed Washington and prevents our national government from coming to meaningful grips with a whole host of pressing problems. But for all the post-partisan talk, some just can't seem to walk the post-partisan walk: from too many candidates we still hear reflexive, negative partisanship, focused on issues that really don't matter very much. To our great good fortune, this description obviously does not fit the Forum, and it occurs to me that this may be the ultimate key to our success. We bring together lawyers with wildly divergent, deeply felt views, secure in the knowledge that those views will receive a respectful hearing and interested feedback from program audiences and journal readers eager to explore the major, substantive legal issues that affect their clients' businesses. We don't always meet this goal, but it speaks volumes that our occasional lapses into rote, franchisor vs. franchisee bickering stand out as much as they do, and produce such adverse reactions from our members. Overall, the level of discourse is extraordinarily high in its intellectual and practical content, and almost always civilized in its manner. Sometimes, Forum members even change their minds as a result of an article in the *Franchise Law Journal* or an annual meeting workshop! That may be unusual in this day and age, but it is clearly a good thing, since sensible people, including in particular lawyers, should always reserve the right to get smarter in light of new experiences and exposure to new ideas.

In these old-fashioned virtues, the Forum is reminiscent of the best characteristics of legal practice in certain towns, counties and small cities, where opposing counsel can zealously represent the interests of their clients without demonizing their adversaries, and business can get done, both inside courtrooms and conference rooms and at more convivial locations, on a foundation of mutual respect and trust. I know from personal experience that when the lawyer on the other side of one of my cases is active in the Forum, the odds are very high that we will be able to conduct ourselves in this fashion, to the significant benefit of our respective clients.

Our tradition of respectful, "big tent" inclusiveness dates back to the Forum's beginnings. Our membership has always included far more franchisor lawyers than franchisee lawyers. Yet the first Chair of the Forum, Harold Ward, was a franchisee lawyer, and three of the four chairs who followed him – Lee Abrams, Andy Selden and Rupert Barkoff – have also spent substantial parts of their distinguished careers representing franchisees. In Austin, the members present will be asked to endorse the nomination of Ron Gardner to a two year term as Forum Chair, commencing in August 2009. As many of you know, Ron too is a franchisee lawyer. There is probably no more zealous, effective advocate of franchisee interests than Ron, but there is also no one more devoted to the Forum and to maintaining our winning formula of high academic standards, collegial dialogue, and outstanding social events. I look forward to his leadership, and hope to see you in Austin.

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Message from the Editor-In-Chief

By Eric H. Karp

Welcome to the October 2008 edition of *The Franchise Lawyer*. I am pleased to have commenced my duties as Editor-In-Chief and with this issue and express my profound gratitude to my predecessor, Genevieve Beck of Carlson Hotels Worldwide, for her invaluable assistance in showing me the ropes.

Included in this issue are descriptions of each of the publications, divisions and other groups within the Forum. We present this information to introduce all members to the leaders and activities of the Forum and to provide opportunities to volunteer and get involved.

It is the goal of *The Franchise Lawyer* to be informative and timely with respect to the latest developments in franchising, including new cases, legislation and regulations as well as Forum and Division news. *The Franchise Lawyer* is published during the first weeks of October, January, April and July. Articles are generally 800 to 1,600 words in length and footnotes are not required.

I am ably assisted by three Associate Editors, Jennifer Brown Moore of Greenberg Traurig in Atlanta MooreJ@gtlaw.com, Max Schott of Gray Plant Mooty in Minneapolis Max.Schott@gpmlaw.com and Glen Plattner of Bryan Cave in Santa Monica glenn.plattner@bryancave.com.

Proposals from potential authors are always welcome. You can reach me at ekarp@kwrlaw.com or the Associate Editors as above. I look forward to seeing you in Austin.

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Divisions and Publications within the Forum



1. Women's Caucus - Carol Anne Been, Chair

The Women's Caucus supports the membership, participation and advancement of women at the Forum, including placement into leadership positions. Our main event is the Women's Caucus Breakfast which takes place during the annual Forum. With attendance of nearly 150 women, the Breakfast provides an excellent opportunity for our female members to network and discuss issues relevant to their practices. This year, we are fortunate to have Justice Harriet O'Neill of the Texas Supreme Court address the Breakfast on issues of work/life balance. She is an award-winning justice, author and speaker; a former complex commercial litigator and mediator; and she coaches her daughters' sports teams. We also will initiate an informal mentoring program at the Breakfast this year, matching women who are available to mentor with those women who would like to have someone to turn to for questions or support.

The Women's Caucus also teams with the Corporate Counsel Division in planning and hosting the Community Service Event in connection with the annual Forum. This year, volunteers from the Forum will visit LifeWorks, an organization that provides counseling, job training and shelter services for youth and families in the Austin

area. We will participate in a fall clean-up project, which will consist of gardening, landscaping and general yard work, with indoor work available in the event of rain. We also encourage charitable contributions from individual members and their firms or companies to be made to LifeWorks.

All female Forum members are invited to join the Women's Caucus and participate in the Breakfast. If you have any questions or ideas for the Women's Caucus, please feel free to contact any of our Steering Committee members: Jane Cohen jane@janecohen.com, Tami McKnew nmcknew@lwfm.com, Christina Noyes cmnoyes@gustlaw.com, Jacqueline Vlaming jacquelinev@coverall.com, Karen Satterlee ksatterl@starbucks.com, Shelley Weatherbie sweatherbie@davismullen.com and Carol Anne Been cbeen@sonnenschein.com.



2. Diversity Committee - Joseph J. Fittante, Jr., Chair

The Franchise Forum is committed to increasing and promoting its diversity membership. To that end, the Forum created a Diversity Committee approximately 3 years ago to advise the Governing Committee on different methods for promoting diversity throughout the Forum. This Committee meets on a periodic basis to recommend steps that the Forum can take in an effort to increase its diverse membership base, promote involvement in Forum activities, and place current Forum members of diverse ethnic and racial groups on the pathways to leadership.

In an effort to provide networking opportunities for Forum membership, including diverse members, the Diversity Committee will be hosting a Wine and Cheese Reception to be held on Friday October 17, from 4:00 to 5:00 PM at the upcoming 31st Annual Forum on Franchising. Please feel free to stop by to renew old acquaintances and make new ones. We look forward to seeing you there.

The Diversity Committee is currently made up of 5 individuals, including a member of the Governing Committee. If you have suggestions for the Committee or are interested in involvement opportunities, feel free to contact any of the existing members of the Committee: Joe Fittante at jfittante@larkinhoffman.com, Kavita Patel at Kavita.Patel@hilton.com, Kendall Tyre at tyre@nixonpeabody.com, Amy Cheng at amy.cheng@chengcohen.com and Gerald Wells at Gerald.Wells@dlapiper.com.



3. Corporate Counsel Division - Kathie S. Lee, Director

The Corporate Counsel Division (the "Committee") is open to all in-house corporate counsel that are members of the Forum. Our members represent corporate counsel from large, mid-size and small in-house legal departments. The Committee is managed by a Director that is appointed for a two year term and six steering committee members that are invited for a rotating two year term. The Committee is focused on issues that impact in-house counsels.

In the past, the Committee has organized several webcasts on current issues affecting in-house counsel and plans to continue this practice in the future. Some topics under consideration for upcoming webcasts include the impact of the credit crunch and the impact of the rise in bankruptcies on franchising.

The Committee also works closely with the Women's Caucus on an annual basis to identify and manage a Community Service Event for attendees at the annual meeting of the Forum. In addition, the Committee sponsors a networking breakfast meeting or a networking cocktail for in-house counsel at the annual meeting of the Forum. These meetings provide in-house counsel with opportunities to network and share best practices. The Committee also recommends speakers and topics for the annual meeting of the Forum.

Please feel free to contact Kathie Lee at Kathie.lee@starwoodhotels.com if you are interested in becoming more actively involved with the Committee.



4. Litigation and Alternative Dispute Resolution Division - David S. Sagar, Director

The Litigation and Alternative Dispute Resolution Division of the Forum (“LADR”) is led by a diverse group of seven Forum members serving three year terms. LADR’s primary objective is to serve the Forum’s membership through the study and presentation of traditional and non-traditional approaches to resolving legal disputes in franchise relationships and increasing both the receptiveness to these approaches and the skills used by practitioners of these methods. The members of LADR also are encouraged to participate in Forum-related activities, such as proposing intensive programs and workshop topics for the Forum, speaking at the Forum, contributing articles to *The Franchise Law Journal* and *The Franchise Lawyer* and organizing and presenting teleseminars on relevant topics.

Although LADR’s focus is on litigation and alternative dispute resolution, all Forum members are members of LADR and all are invited to participate in any LADR-sponsored activity. Indeed, LADR welcomes input from Forum members and those who may be interested in serving on LADR should share their interest with the Forum or Division Chair, David Sager at dsager@daypitney.com.



5. Solo and Small Firm Network - Howard E. Bundy, Chair

The Solo and Small Firm Network of the Forum exists to give franchise attorneys who practice solo or are employed by firms with ten or fewer attorneys an opportunity to network and exchange ideas with others similarly situated.

During the 2008 Forum in Austin, the Solo and Small Firm Network will meet for breakfast on Friday, October 17, 2008 from 7:30 until 9:00 AM. If you practice as a solo or in a small firm, we encourage you to attend and participate. Members of this Network are essentially the program, as they share their experiences with their colleagues and, in exchange, learn from them. Regardless of the stage your practice is in, you will likely learn from others in ways that will benefit your practice.

This year, the Solo and Small Firm Network will focus on how to leverage knowledge, technology and networking to level the playing field—in both litigation and transactional work, as well as in Forum leadership and practice development. As in recent years, the format of the Solo and Small Firm breakfast will be round-table discussions. You will join a table with people with common interests and concerns. You may come away with new ideas and approaches that help you to improve your practice and your profitability.

In assuming leadership of the Solo and Small Firm Network this year, we have sought to carry forward with the good work of those who have gone before us and to build upon the foundation they have so ably laid. Looking to the future, we are looking for opportunities to expand the mutual benefits and support available to solo practitioners and small firms. We welcome your participation and hope that, if you are a solo practitioner or with a small firm, you will join us for breakfast. For more information, please feel free to contact Howard Bundy at bundy@bundylawfirm.com.



6. Franchise Law Journal - Deborah S. Coldwell, Editor-In-Chief

The *Franchise Law Journal* is a scholarly publication of the Forum, published quarterly. The *Journal* informs and educates its members by soliciting, editing and publishing articles, columns, case notes, and reviews about recent developments in the law that affect franchise and distribution systems. The *Journal* seeks to reflect the diversity of its membership and tackles issues on the franchisor and franchisee sides of current issues.

Articles submitted for publication should be appropriate for a law review article, although the *Journal* often provides more practical advice. Articles should be 25 - 30 double spaced pages in length (or 5,000 - 7,000

words). The *Journal* accepts some shorter articles (i.e., book reviews and case notes), but those are the exception. If an author writes a shorter article, it might be appropriate for *The Franchise Lawyer*.

There are six associate editors and six topic and article editors on the Editorial Board of the *Journal*. The Forum Chair, after consultation with the Editor-in-Chief, appoints members to the *Journal*. In order to be considered for an editorial position, an applicant must write an article for the *Journal*, a paper for the Annual Meeting, or a chapter in a monograph or book for the Forum.

The Journal is always looking for aspiring authors who have something to share with the membership of the Forum. Please feel free to contact our Editor-in-Chief, Deborah Coldwell at Deborah.Coldwell@haynesboone.com. You can also learn more about writing for the *Journal* by going to our website located at http://www.abanet.org/forums/franchising/franchise_law_journal/submission.html.



7. International Franchise and Distribution Division - Michael K. Lindsey, Director

The (“IFDI”) is the youngest of the Forum’s divisions, formed in 2004 for the purpose of focusing the Forum’s efforts in the field of international franchising and distribution. Our mission statement includes a commitment to provide leadership in this field in a variety of ways, including the development and presentation of educational programs, the publication of books and articles, and outreach to international franchising and distribution practitioners in the U.S. and other countries. Through our efforts, the Forum can now count a number of new non-U.S. members, who we anticipate will make substantial contributions to the Forum’s programming, perspective and collegiality.

IFDI-initiated programs have been presented at each annual Forum since IFDI’s formation, and at conferences sponsored by the ABA Section of International Law and Practice, the International Bar Association and the Ontario Bar Association. We have also presented a teleseminar on China’s franchise regulations and, at this year’s annual Forum in Austin, we will present a special breakfast program on international franchise expansion, a discussion that will be led by experienced general counsel from three companies, two U.S. and one Canadian.

IFDI Steering Committee members have served as authors and editors of the Forum’s *International Franchise Sales Laws* book, which addresses disclosure requirements in countries around the world and was published in loose-leaf format to facilitate updates reflecting developments in this ever-changing field. They have also published articles in the Forum’s *Franchise Lawyer* and *Franchise Law Journal* publications.

Our goals for the next two years include the continuation of our significant contributions to annual Forum programming, the exploration of additional joint programming possibilities with bar and specialty industry organizations around the world, monitoring of international developments, publication of book updates as those developments warrant, and continued outreach to other practitioners in our field. Forum members who would like to get involved in any of our projects should contact Michael K. Lindsey at MichaelLindsey@paulhastings.com or any IFDI Steering Committee member listed on the IFDI web page that can be reached from the Forum’s home page.



8. Young Lawyers Division - Leslie Curran, Director

Every two years, the Young Lawyer’s Division (“YLD”) of the ABA appoints a Liaison to the Forum. The Liaison works with the Forum’s Governing Committee to identify and offer valuable input on issues that relate to the Forum’s young and new members. On a quarterly basis, the Liaison reports on these efforts to the YLD.

For the annual Forum meeting, the Liaison organizes what has become a “Don’t Miss It” event for the Forum’s new and young members – the Newcomers’ Networking Night. The event combines great food and drink with great local entertainment, and it serves as an excellent opportunity for new and young members to meet new people and re-connect with friends. In addition, the Liaison oversees the Friends

of the Forum Program, which pairs seasoned attorneys with new attendees. With these programs, we hope to integrate new attendees into our group and begin to establish long-term business and personal relationships!

Given the ever-increasing demands placed upon attorneys, one of the greatest challenges facing the legal profession is engaging young and new attorneys in professional and industry organizations. For the coming year, one of my primary goals as the YLD Liaison to the Forum is to encourage new and young attorneys to get more involved in the Forum and to identify ways to facilitate that involvement. In connection with this effort, I would like to see seasoned attorneys – those who have been practicing and attending the Forum for years – encourage the new and young attorneys they work with to step up and get involved!!

For new and young attorneys, if you have suggestions for the Forum or if you want to get involved, please contact the members of the Forum's Young Lawyer's Committee: Leslie Curran at lcurran@plavekoch.com or 703.774.1215, Adam Ekberg at aeberg@starbucks.com, Ryan Whitfill at Ryan.Whitfill@dlapiper.com or Jacob Kraus at jrkraus@faegre.com. We look forward to hearing from you!

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Look Before You License-Recent Amendments to Korean Franchise Laws Increase Burdens on Cross-Border Franchisors

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Jung Won Park and Philippe Shin

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With a population of 50 million people (12 million in the greater Seoul area alone) and a Gross Domestic Product per capita of US\$19,400, Korea is one of the largest economies in the industrialized world and represents a market that cannot be ignored by US companies. Not only has the spending power of Korean consumers been increasing steadily since the 1988 Olympic Games, Korean consumers generally perceive western brands quite favorably - Starbucks and Coffee Bean & Tea Leaf are omnipresent in bustling Seoul along with other prominent US consumer brands (including a considerable number of chain restaurants like California Pizza Kitchen and Cold Stone Creamery). It is important to note, however, that many Korean franchisees are large, sophisticated companies with bargaining power equal to their US franchisors. Last year's amendment to the Korean Franchise Act introduced a number of requirements that provide significant protections for the franchisee's interests. This article provides a brief summary of the regulatory framework for franchising in Korea and a summary of the amendments, as well as a few cautionary pitfalls and tips for cross-border franchisors interested in franchising in Korea.

Regulatory Framework for Franchising in Korea

South Korea first adopted a franchise disclosure and relationship law in 2002, under Korea's Act on Fairness in Franchise Transactions (the "Franchise Act"). The Franchise Act was subsequently amended in 2007, with an effective date of February 4, 2008, as the country's franchise sector experienced significant growth. Many of the specific mechanics of the statute's implementation are included in the "Presidential Decree to Implement the Act on Fairness in Franchise Transactions" (the "Presidential Decree"). The current Presidential Decree, which also took effect on February 4, 2008, details requirements regarding fees, termination, specific disclosure requirements and other items included in the Franchise Act. (Business Franchise Guide (CCH) ¶ 7170).

Most of the revised provisions of the Franchise Act apply to any franchise agreement entered into on or after February 4, 2008, and to any earlier franchise agreement that is renewed after February 4, 2008. The

amended provisions are significant from the perspective of the cross-border franchisor.

Summary of Amendments and Effective Dates

• Disclosure Statement Registration Requirement

Perhaps the most significant amendment to the Franchise Act is the requirement that franchisors register a disclosure document with the Korea Fair Trade Commission ("KFTC"). Under this registration requirement, which took effect on August 4, 2008, a franchisor must provide each prospective franchisee with a copy of the registered disclosure document at least 14 days prior to the signing of the franchise agreement or receipt of the franchise fee. (See Chapter III, Article 7 of Act on Fairness in Franchise Transactions). A franchisor must set aside adequate time for the registration process (i.e., a first-time registration could take approximately two months) in order to prevent any unexpected delay in its business plan.

The information that must be included in the disclosure document is similar to that required for the Franchise Disclosure Document ("FDD") in the United States. As a practical matter, most of the information required can be pulled from a franchisor's FDD, with the exception of information regarding criminal sanctions by the KFTC against the franchisor. Prior to this amendment, although the Franchise Act did require franchisors to provide information to prospective franchisees, there was no registration requirement.

On June 17, 2008, the KFTC issued the Model Disclosure Document ("MDD"), which provides a format that franchisors may use for purposes of registration. The information required to be disclosed about a franchisor (as set forth in the MDD) include: (1) general corporate information; (2) a description of the franchised business; (3) past records of violations of law committed by the franchisor and its high-level employees; (4) the franchisees' obligations; (5) terms and conditions applicable to franchisees; (6) a detailed procedural description on how a franchisee may start its business and the time required for such procedure; and (7) a description of the franchisee training program. Franchisors may amend the MDD after registration, provided that the amended MDD includes all mandatory disclosure. (KFTC Regulation on MDD, Section 4).

• Mandatory Delivery of Disclosure Statement to Franchisee

Prior to the Amendment, franchisors were required only to provide a disclosure document to parties making a written request to the franchisor. The amended Franchise Act removes the requirement for a written request and requires the franchisor to provide a disclosure document to any party that negotiates or discusses execution of a franchise agreement with the franchisor. (See Act on Fairness in Franchise Transactions, Chapter I, Article 4). Perhaps even more significant than the new delivery requirement is the franchisee's ability to rescind the franchise agreement and demand a refund of the franchise fee if the disclosure statement contains false or misleading information or omits material information. (See Chapter III, Article 10 of Act on Fairness in Franchise Transactions).

• "Cooling Off" Period After Delivery of Disclosure Statement

Article 7 of the amended Franchise Act now contains a "cooling off" period similar to that of the FTC Rule. (See 16 C.F.R. § 436.2(a)). The franchisor may not accept any franchise fee or execute the franchise agreement until 14 days after delivery of the disclosure document. (See Chapter III, Article 7 of Act on Fairness in Franchise Transactions). The period may be shortened to seven days – the "sophisticated franchisee" exception – when the prospective franchisee is represented by a certified franchise transactions consultant registered with the KFTC or a lawyer. (See Chapter III, Article 7 of Act on Fairness in Franchise Transactions). In the event a franchisor does not follow the 14 day cooling off requirement, the franchisee can demand the refund of any franchise fees paid within two months of the execution of the franchise agreement. (See Chapter IV, Article 10 of Act on Fairness in Franchise Transactions).

• Expanded Definition of Franchise Fees

The amended Franchise Act broadens the definition of "Franchise Fee" to include (1) costs of fixtures and trade dress elements, (2) rent paid to the Franchisor, as well as (3) any other amounts to be paid to the franchisor for the franchisee to acquire or maintain franchise rights. (See Chapter I, Article 2, Item 6 of Act on Fairness in Franchise Transactions). Prior to the amendments, "Franchise Fees" only included any guaranty deposit, any royalty payments for the use of the trademarks and charges assessed by the franchisor for support and training.

• Partial Escrow of Franchise Fees

Under the amended Franchise Act, the franchisor must set aside and deposit a portion of the initial franchise fees in an escrow account maintained with a qualified custodian. The portion of the franchise fees

that has to be escrowed consists of membership fees, training fees, franchise contract deposit, trademark license fees, and other fees for support and assistance.

The qualified custodians include: (1) financial institutions within the meaning of the Banking Act, (2) postal offices engaging in the deposit insurance business, (3) insurance companies within the meaning of the Insurance Business Act, and (4) trust companies within the meaning of the Trust Business Act. (See Article 5-6 of Presidential Decree).

• ***Prohibition on Competition with Franchisee***

The amended Franchise Act includes language prohibiting a franchisor from establishing competitive businesses or entering into franchise relationships with other parties that may compete with an existing franchisee. (See Chapter III, Article 12 of Act on Fairness in Franchise Transactions).

• ***Revised Provisions Regarding Renewal and Termination of Franchise Agreements***

The amended Franchise Act forces franchisors to renew franchise arrangements with existing franchisees who request a renewal within three to six months before the scheduled expiration of the franchise agreement unless there is "just cause" for nonrenewal. The amended Franchise Act gives several examples of "just cause," including (1) the franchisee's breach of its confidentiality obligation (e.g., unauthorized disclosure of intellectual property of the franchisor, including its trade secrets), (2) the franchisee's failure to participate in the franchisee training program, (3) the franchisee's payment default, and (4) the franchisee's failure to follow the franchise system standards. (See Chapter III, Article 13 of Act on Fairness in Franchise Transactions). In cases where a franchisor sends a default notice, the amended Franchise Act requires a clear statement of exactly which provisions have been breached. Prior to the amendments, the franchisor was required to give three written default notices before any termination; however, under the amendments, only two notices are required. The default notices must affirmatively warn the franchisee that the franchisor will terminate the franchise agreement if the franchisee fails to cure the default. (See Chapter III, Article 14 of Act on Fairness in Franchise Transactions).

The Franchise Act and its Presidential Decree also list certain other grounds upon which renewal of a franchise agreement may be refused without prior notice. These grounds include: (1) a bankruptcy filed by or against either the franchisee or the franchisor, or a compulsory execution proceeding or reorganization proceeding filed by or against the franchisee or the franchisor, (2) dishonor of notes or checks issued by either the franchisee or the franchisor due to bankruptcy or otherwise, and (3) the franchisor's inability to continue its franchising business due to a significant reason. (See Article 15 of the Presidential Decree)

• ***International Franchise Agreements***

Although there are numerous cross-border franchising arrangements in Korea, the amendments do not include any specific language addressing a non-Korean resident franchisor. Furthermore, the Act does not specify an official language requirement for the franchise agreement.

Pitfalls for United States Franchisors in Korea

The problems facing a foreign franchisor are not specific to the United States; any non-Korean franchisor will face the same issues. Although the regulatory framework is fairly extensive, especially in light of the recent amendments, franchise law is still fairly new in Korea. As a result, there is very little court or KFTC precedent upon which franchisors or franchisees may rely. This underscores the tremendous importance of a detailed and complete disclosure statement. Additionally, all cross-border franchisors should remember the following when franchising in Korea:

- Register the MDD with the KFTC prior to the receipt of any franchise fee or the signing of a franchise agreement;
- Remember there is a two month review period required for a first-time registration;
- Remember that a portion of the franchise fees must be escrowed with a qualified custodian;
- Franchisors have no termination right during the initial 10 years with their franchisees unless they can demonstrate "just cause;"
- Franchisors must give a clear written notice of default and opportunity to cure to the franchisee at least twice prior to any termination.

Franchisors that do not comply with the KFTC may face strict penalties. On October 1 the KFTC launched a major investigation into 200 franchise operators in 15 types of businesses for illegal trading practices. The KFTC noted that of the 200 franchise operators, 20 have advertised through the internet and franchise exhibitions without registering the necessary documents. Additionally, the KFTC will be investigating signs of

irregular trading practices such as unfair termination of contract and refusal to provide operational support to franchisees. The KFTC's investigation will include internet and telephone surveys as well as onsite investigations of various franchise operators. (See Choi He-suk, Watchdog Probes Franchise Operators, The Korea Herald, October 1, 2008, available at http://www.koreaherald.co.kr/NEWKHSITE/data/html_dir/2008/10/01/200810010049.html) A franchisor that discloses false or misleading information or omits to disclose material information will be subject to imprisonment not to exceed 5 years or a fine not to exceed 150 million Korean Won (approximately US\$135,000). A franchisor who fails to comply with a correctional order from the KFTC will be subject to imprisonment not to exceed 3 years or a fine not to exceed 100 million Korean Won (approximately US\$90,000). Also, a franchisor that fails to deposit the required portion of franchise fees in escrow or receives franchise fees or executes a franchise contract in violation of the "cooling-off" requirement will be subject to imprisonment not to exceed 2 years or a fine not to exceed 50 million Korean Won (approximately US\$45,000). The franchisor, even though a legal entity such as a corporation, may be deemed criminally liable for failure to comply with the KFTC. The individuals (directors or officers of the corporation, or other employees) who actually committed the breach of the regulations may also be held criminally liable. If identifying a specific individual is not possible, a "representative director" (i.e., the president) may be deemed responsible. Notwithstanding the foregoing, violations of this type of administrative regulation (especially when liability is attributed to a "representative director" rather than a specific individual for actual wrongdoing), have historically resulted in a fine rather than a prison term.

Tips for Franchisors Entering Korean Market

While there is no standard for "plain Korean," consider drafting the franchise agreement in a manner that is easy to understand for non-lawyers. Although many US franchisors will deal with sophisticated Korean franchisees, in the event the franchisee is a "small" or unsophisticated party or someone with little international experience, a franchisor may want to consider providing an unofficial Korean translation of the MDD and franchise agreement. This not only creates goodwill with the franchisee, but could also help avoid confusion later on during the franchise relationship. Additionally, since there is no official language requirement under the KFTC, the franchise agreement should include a provision regarding the official language and construction and interpretation of the franchise agreement (whether or not the parties agree to have translations made for their convenience). The franchise agreement should also address which party will bear the burden of paying for any unofficial translations of the franchise agreement and other documents. Training raises another issue with respect to language – which may be an issue for both sophisticated and small franchisees alike. While the franchisee may speak English or the franchisor may speak Korean, the operators or employees of the parties may not. Franchisors may need to provide training in both Korean and English. The franchise agreement should address who bears the cost of providing interpreters for training. Finally, as in any international transaction, it is crucial for a prospective foreign franchisor in Korea to consult with competent local counsel experienced in antitrust law.

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