

## Principles of Japanese Franchising Law

### PRINCIPLES OF JAPANESE FRANCHISING LAW

Franchising has developed extensively in **Japan**, the two main sectors being food stores and service franchises and has been regulated first in 1973 and more precisely in 2002.

A general duty of disclosure is provided for in the 1973 Medium-Small Retail Business Promotion Act and is administered by the Ministry of International Trade and Industry (MITI). They were modified in April 2002.

On 24 April 2002, the *Japan Fair Trade Commission (JFTC)*, the competition authority of Japan, published guidelines on franchising which revised and replaced the guidelines originally issued in 1983. The new guidelines consist of three parts: a general description of franchising, provisions for the disclosure of necessary information at the time of the offer of a franchise and a part on vertical restraints between a franchisor and its franchisees.

According to the second part of the guidelines, the failure to provide necessary information shall constitute deceptive customer inducement, which is one of sixteen types of “unfair trade practices” listed by the ordinance under the Antimonopoly Act, and shall be subject to a cease and desist order by the JFTC. The aggrieved party is also entitled to raise a suit for injunction against such an act. The guidelines list the following as examples of the items to be disclosed:

1. the conditions regarding the supply of goods to the franchisee (e.g. recommendation of the supplier),
2. the details of the assistance to be offered the franchisee, such as a description of the assistance to be offered, its manner, frequency and costs,
3. the nature, amount and conditions of repayment, if any, of the fee to be paid at the time of entering into a franchise agreement,
4. the amount, method of calculation, as well as the timing and manner of payment of royalties,
5. the description of any settlement arrangement between the franchisor and the franchisee, as well as the interest rate of any loan to a franchisee offered by the franchisor,
6. whether or not the franchisor is prepared to indemnify the franchisee for its deficit or to render assistance to the operation of a franchised unit that is not doing well,
7. the terms of the franchise agreement and the conditions of its renewal, resolution as well as termination; and,
8. whether or not the franchisor in the franchise agreement reserves a right to operate a unit on its own or to grant another franchise close to the franchisee and whether or not the franchisor plans to do so.

The guidelines also require that if the franchisor provides the franchisee with the projected sales or profits, such projection shall be made in a reasonable manner, on the basis of reliable data. The underlying data as well as the way in which the projected sales or profits are worked out must be disclosed to the franchisee.

As regards the vertical restraints imposed by a franchisor upon its franchisees, the third part of the guidelines observes that, if these restraints go further than is needed to duly operate the franchised business, they can be condemned as an abuse of a dominant position (i), as dealing on restrictive terms (ii) or as retail price control (iii).

In the first of these cases (i), when the franchisor holds a dominant position as against its franchisee, requirements in the franchise agreement or acts of the franchisor under it, such as:

- Restraints on the sources of supply,

- Quotas on the amount to be purchased by a franchisee,
- Requirements to offer services that are not prescribed in the franchise agreement; or
- A prohibition to engage in a competing business after the termination of the franchise agreement to a greater extent than is necessary for the protection of the know-how provided by the franchisor, can fall under the category “abuse of a dominant position”, which is listed as an unfair trade practice. The franchise agreement as a whole, rather than each of its clauses or each act of the franchisor, can also constitute an “abuse of a dominant position.” The points to be examined in this regard are, to name but a few, restraints on the goods to be offered or on the manner of sale, the sales quotas, restrictions on the right of the franchisee to terminate the franchise agreement, and the term of the agreement.

Secondly (ii), if a franchisor requires its franchisee to purchase goods or materials from either itself or a designated supplier, such a requirement may, if there are anti-competitive effects, be found to constitute a “dealing on restrictive terms”, which is listed as an unfair trade practice.

Thirdly (iii), the fixing of a retail price by a franchisor, as opposed to its indicating a suggested price, shall be illegal per se if the franchisor supplies goods to the franchisee. If the franchisor is not itself supplying the goods, it may fall under the category of “dealing on restrictive terms”.

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