Establishing and Maintaining an International Compliance Program

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I. INTRODUCTION

A franchisor’s sales team is often pushing to close the next deal and plant the franchisor’s flag in the next non-U.S. jurisdiction. Despite the usual race against the clock to finalize and execute the franchise agreement before the end of the relevant accounting period, a franchisor’s lawyers must continue to safeguard that the franchisor has the best tools to enforce the rights that the franchisor has so fiercely negotiated.

Before a franchisor enters into cross-border franchise relationships, its attorneys must ensure that the franchise agreements provide an adequate platform to support the on-going operation of the franchise business. Unlike transacting business in the United States, the ability to enforce one’s rights under an international franchise agreement is exponentially more complicated because of a variety factors, including foreign laws and legal systems, language barriers, logistics, and cost. Indeed, enforcing an international franchise agreement is substantially more challenging than simply hiring an attorney to go to the local courthouse at the corner of 5th and Main to obtain an injunction against the franchisee to enforce compliance with the terms of the franchise agreement or to terminate such franchise agreement and cause the franchisee to pay any amounts due and properly de-identify its business. The franchise agreement must contemplate cross-border enforcement, compliance with mandatory laws and must be adequately reviewed and analyzed for local jurisdiction enforceability.

This paper will focus on the three principal categories: (a) operational compliance, (b) compliance with foreign regulatory filing requirements; and (c) legal compliance, all to ensure that the products and services delivered to the consumer represent the promise of the brand, which is, after all, the key to any successful franchise program.

II. OPERATIONAL COMPLIANCE

A. Brand Training

In order to ensure that the product of the brand is being delivered to the consumer as intended, it requires that management and staff level employees operating the franchised business have adequate training to execute on the brand promise. This often requires that training materials and programs be translated into the franchisee’s language to ensure that the franchisee’s employees understand the brand requirements when English is not their first language. From a contractual perspective, it is simple enough to require a franchisee to: (i) attend all mandatory training programs, (ii) engage and train adequate staff to operate the franchised business, and (iii) pay for all translations of system materials, including assigning all rights in such translations to the franchisor. (See Appendix 3 for sample clauses that implement these requirements.) Although these contract clauses may look similar to their domestic counterparts, implementing such requirements and enforcing contractual remedies in an international context is an entirely different story.¹

¹ Most cross-border franchise agreements provide for some form of international arbitration as a mechanism for resolving disputes, with a carve out for injunctive relief (which may or may not be enforceable, depending on local law and should be verified at the onset with local counsel before negotiating the franchise or master agreement, including the ability to enforce arbitral awards within the jurisdiction). Going to the time, trouble, and expense of obtaining an arbitral award, and then proceeding in the courts of the local jurisdiction to enforce operational requirements is an ineffective mechanism, at best, for ensuring compliance.
The problem is not with such typical contractual provisions, but the process through which they are implemented. The process must be sustainable and efficient to ensure that the materials are translated accurately, the franchisor retains its rights in its proprietary information, and the brand compliance message is communicated to the franchisee’s employees.

1. **Translations**

Simply requiring that the franchisee pay for and control the translations dis-incentivizes the franchisee from doing so (i.e., a franchisee would be put in a position to invest funds in translation of a training program without an incentive to carry out such training). In the absence of an obligation and a process to require the franchisee to translate and carry out brand training prior to a franchisor’s confirmation that such brand training was delivered to the franchisee’s employees, the franchisee will often provide the untranslated English materials to its employees (who may have difficulty reading such materials) or rely on translations of poor quality (e.g., internet based translations) and not invest the funds required to have the brand training materials properly translated and delivered to its employees.

If the franchisee commissions a translation and delivers such translation to the franchisor, then the franchisor must invest additional funds to confirm the accuracy of the translation in order to avoid the risk of later being estopped from objecting to the accuracy of the translation. Further, as noted above, in many jurisdictions the translation may be considered a derivative work because it is not exact and the translator or the franchisee may obtain ownership rights in the materials if the proper assignment of rights does not take place, and the franchisor could find itself unable to prevent a franchisee or translator from using the materials in (or being sold to) a competitive business.²

As such, from an operational perspective, a franchisor must have a system in place for (a) requesting a copy of the translated materials before opening as part of a pre-opening checklist from the franchisee depending on whose responsibility it is to obtain it (either a franchisee or master franchisee), and (b) obtaining the proper assignments and verifying with local counsel (and translator if a local translation service is used) that the assignment is effective. If the franchisor receives the translation, reviews it and there are revisions, then such revisions must be communicated back to the franchisee and in that process, there will be a second opportunity to request assignments.

The best approach to ensure translation and training both take place is to separate payment from translation and delivery of materials and training. The franchisee may be required to pay its fair share as a reimbursable expense to the franchisor for the cost of developing and maintaining a web-based site that contains the training materials that have been translated by the franchisor.³ The costs to provide the materials should, from an accounting perspective, be treated as an expense with a direct benefit to the franchisee and should not be

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² For example, a Chinese character translation will have characters that have similar meanings but will be substantively different than the English version from which it was translated.

³ As a side note, for trainings that use system-universal training materials, such as food preparation, food safety, etc., those can be done as videos with voice-over for different languages, as each new jurisdiction is franchised and a new translation is required, fairly efficiently and inexpensively. Such training videos, depending on the subject matter, can be animations and demonstrations with no language at all, if the subject permits.
treated as income to the franchisor, and therefore potentially not subject to withholding tax (if any is required by the jurisdiction).

By adopting this approach, the franchisor gains control of the quality and accuracy of the translation and its intellectual property rights in the materials. The materials on the site can be individualized training for different positions (e.g., kitchen, bar, restaurant, front office, engineering, management, financial and accounting, etc.) or as materials for the franchisee to conduct group training at its location (essentially, train the trainer materials). The web-based site will have an electronic record of who accessed the site, when the site was accessed, and the materials accessed, and thus further support franchisor’s continued exercise of control over its intellectual property.

2. **Training**

Utilizing the web-based training materials described above, on a periodic basis, the franchisor can prepare a report and determine who has been utilizing the training materials, and, by default, who has not. As part of the quality assurance program, the franchisee should be required to self-certify that the trainings have been conducted and if the reports do not correspond with the self-certification, the franchisor can determine if the franchisee has misrepresented its compliance to the franchisor. The failure to complete training and a self-certification may trigger additional inspections of the franchised business at the franchisee’s cost.

The same principle applies for requiring the franchisee’s key personnel to attend periodic mandatory trainings. In order to increase the likelihood of attendance, a franchisor may contractually require the franchisee to pay the cost of such mandatory training regardless of whether they attend. In such situation, the franchisee may decide to attend since it will be incurring the related cost nonetheless, subject, however, to the franchisee perceiving at least some value in the training that exceeds the incremental travel and lodging costs for the representative to attend. Attendance of such mandatory training may be treated as an element of the franchisor’s quality assurance program and a franchisee’s failure to attend mandatory training or to deliver the training materials may be treated as an additional breach to the franchise agreement. As such, in the event that a franchisee operates a franchised location which fails performance standards, then the franchisor may rely on the franchisee’s breach of its training obligations to place the franchisee on default of the franchised location.

To further support a franchisee’s compliance, a franchisor may periodically notify franchisees of any changes in applicable standards, training programs, or advertising and marketing programs. Such notices are helpful to (a) facilitate compliance by ensuring that franchisees are aware of any changes in requirements and programs and to remind them to conduct the training and comply with standards, and (b) evidence that the franchisee was aware (or should have been aware) of current compliance requirements. After such general electronic notifications have been sent, within a reasonable period of time, the franchisor’s training officer should review the web-based site to verify if the training has been completed and then send a personalized notice to the franchisee that has not yet complied.

With respect to a master franchisee training subfranchisees, the franchisor must either develop the training materials, or confirm the accuracy of the materials. In addition, the franchisor must ensure that it owns the related intellectual property rights and obtains appropriate and necessary consents and assignments to protect its interests in the materials used for that purpose.
In the present environment, franchisors should consider whether such centralized training materials used for the training of employees could materially increase the franchisor’s exposure to vicarious liability (including joint employer). Unlike franchise training program under which the franchisor trains the franchisee and then the franchisee trains its employees, the web-based centralized training programs enable franchisors to train franchisee’s employees directly. As we discussed above, doing so on a number of topics makes a lot of sense, both in terms of ensuring the quality of the trainings provided, as well as protecting the franchisors’ rights in these materials. However, this does represent an increased degree of involvement by the franchisor in the training of the franchisee’s employees. A detailed discussion of the relevant issues is beyond the scope of this paper, but franchisors should consider the balance between these two concerns in determining the training necessary to achieve the desired business result versus the potential exposure in providing it.

B. Local Advertising

All franchisors must have a mechanism for controlling the use of the franchisor’s trademarks and advertising messages and contractual requirements to approve a franchisee’s proposed advertising. (See Appendix 3 for sample clauses that implement these requirements.) To encourage compliance, franchisors first and foremost must provide sample shell advertising with the trademark usage (including text, color and positioning of the trademark) and text for at least the typical ads that a franchisee might need. It is easy to have a myriad of typical sizes and approved samples available on a franchisor’s website, including for frequently celebrated holidays and other special occasions where advertising is required. As the franchisor develops and approves more content, it may consider making such content available to other franchisees as well.\(^4\) From a process perspective, the franchisor does then not have to approve materials used regularly in the franchisee’s business.

This obviously is more complicated in the international context due to the need to translate into local language the stock language prepared by the franchisor, and the reverse for the franchisor to review foreign language advertising prepared in the various jurisdictions where franchisees are located. Franchisees are entrepreneurs, and notwithstanding the amount of advertising materials the franchisor provides, the franchisee will likely wish to develop its own. Franchisees will often ask for deemed approval if the franchisor fails to respond within a timely fashion to the franchisee’s request for approval. Once advertising contracts have been signed and materials placed, removing them is difficult, and in the international context powers of attorney granting the franchisor the right to act on behalf of the franchisee are not typically used or accepted. The franchisor should always retain the right to withdraw approval for materials approved but exercise it sparingly.

Franchisors are often tempted to rely on a master franchisee to control the local market advertising. With too much discretion and too little franchisor involvement, the master franchisee can begin to think as though it is the master franchisee’s “own brand in the market”. Franchisors should continue to review in-country marketing materials to be sure that they are comfortable with the advertising prepared or permitted by franchisees and that they are not

\(^4\) Note that if franchisor is using any stock art or materials prepared by a franchisee, or will be using on websites controlled by franchisor materials prepared by franchisee, franchisor should require that franchisee deliver to franchisor proper authorizations regarding franchisee’s rights to utilize the works, including worldwide use rights for the materials used on the website.
drifting from the brand message or using the trademarks in an unauthorized manner, which could damage the brand or adversely affect a franchisor’s continued rights in the trademarks.

Franchisors should use services that continuously search trademark registries for applications being submitted by third-parties – including, not surprisingly, franchisees – that would infringe on the franchisor’s trademarks.\(^5\) On finding such applications by franchisees, the franchisor must immediately demand that the applicant cancel or assign the application. If the franchisee fails to respond immediately, the franchisor must timely file an opposition action and commence default procedures against the infringer. The same pre-use approval should apply to franchise sales advertising by a master franchisee and, while outside of the scope of this paper, to compliance with local jurisdiction’s franchise disclosure laws, if applicable.\(^6\)

The same adage of the more the franchisor provides with respect to advertising, the fewer compliance issues arise is particularly applicable to a franchisee’s web presence. If franchisees are permitted to have websites using the franchisor’s trademarks, then the franchisor should have clear standards for content, and require as a condition of the approval, the assignment of the URL if the URL contains the franchisor’s tradename. When the franchisor becomes aware of unauthorized websites or URLs being used by franchisees, the franchisor must take immediate action to have rights in the URLs assigned to the franchisor, and the website either conformed to standards or taken down.

The franchisor should also engage a service to track its brand on social media where references to the brand are likely to be present (Twitter, Instagram, Trip Advisor, Yelp, etc. depending on the business). While such services are not inexpensive, the need to monitor the franchisor’s brand and the social media presence of its franchisees is ever-increasing.

C. Customer Data

While the specific regulatory and compliance requirements of laws such as the European Union General Data Protection Regulation (“GDPR”) are outside of the scope of this paper, the answer to the age-old dispute between franchisors and franchisees as to who owns the customer data is being answered around the world by regulators – the customer owns it.\(^7\) Franchisors and franchisees through their loyalty programs and sophisticated property management and point of sale systems have been collecting, analyzing, and using the personal data of the customers to determine how best to satisfy the needs of those customers and to market to them to get them to return again and again. How that data is stored, secured, transferred, retained, and used is coming under greater scrutiny. This is particularly the case with respect to a data subject’s contact information that franchisors and franchisees wish to use

\(^5\) There are various watch service subscriptions, such as, Clarivate Analytics/CompuMark, Corsearch, and others, including watch services in China that review for Chinese character marks. It is particularly relevant to continuously monitor trademark registries in China due to the prevalence of trademark squatters there. It is useful to have outside IP firms specializing in international trademark registration reviewing the raw data to determine which notices are of importance to the franchisor.


\(^7\) Regulation (EU) 2016/679 (General Data Protection Regulation); OJ L 119, 04.05.2016; cor. OJ L 127, 23.5.2018.
for direct marketing, such as, facsimile numbers, email addresses, cellular phone numbers, credit card data, among others.

Franchisors and franchisees must have strict standards as to how the personal data it obtains from data subjects will be handled to meet the requirements of GDPR or other applicable privacy laws, including privacy statements, statements of individual rights and to be informed how the personal data will be used, the data subject’s consent to use such data (where required), and processes for dealing with the data subject’s rights of access and rights to be forgotten. Depending on the nature of the franchised business franchisors and franchisees may obtain and track certain data that is deemed to be “sensitive personal data”, such as genetic, biometric and health data, as well as personal data from which racial and ethnic origin, political opinions, religious or ideological convictions can be ascertained. The use of this personal data is subject to even a higher level of scrutiny and protection. The franchisor should have mechanisms in place to protect and comply with legal requirements with respect to any data transferred between the franchisee and franchisor and their respective vendors. The consequences of non-compliance are significant and if the franchisor is found to be liable for not having adequate protections in place, the claims could certainly exceed the value and ability to collect under any indemnity from the franchisee (e.g., under the GDPR, regulatory fines can up to 20,000,000 Euros or 4% of worldwide annual turnover, whichever is greater). This again is an area where franchisors must have its own policies for complying and requiring franchisees to comply with such laws with respect to the system, but balance its vicarious liability exposure to avoid dictating how the franchisee must comply with its own obligations under such laws.

D. Suppliers

Most franchise systems categorize into four categories the supplier restrictions placed on franchisees related to the materials, furniture, fixtures, equipment, products, and supplies utilized to create the products offered by the franchisee: (i) those purchased in accordance with standards and specifications; (ii) those purchased from suppliers approved by franchisor; (iii) those purchased from designated suppliers; and (iv) those purchased from franchisor or its affiliates. The needs of the system for conformity, the size of the system, the sophistication of its franchisees, the franchisor’s purchasing arrangements and the supply chain will dictate the types of restrictions and compliance mechanisms to be utilized.

For example, for sophisticated franchisees experienced in the market, or if the franchisor is new to market, having detailed standards and specifications and allowing the franchisee to source either locally or in accordance with its own supply arrangements for importation based on the franchisee’s knowledge of import restrictions and regulations may be the easiest approach. This strategy then requires greater efforts for confirmation on the front end that the items proposed to be used by franchisee meet the standards and specifications.

For the build out of the franchised location, a franchisee would be required to submit color boards, material samples and manufacturer specifications for all items used. Once they

8 Again, well beyond the scope of this paper, but in summary, many US based franchisors will be relying on compliance with Privacy Shield certification with respect to the transfer of data between Europe and the US, as opposed to entering into form data transfer agreements and binding corporate rules as provided under GDPR.

9 While predominantly a US focused article, Joyce G. Mazero and Leonard H. MacPhee, Setting the Stage for a “Best in Class” Supply Chain, 36 Franchise L.J. 219 (Fall 2016), contains an excellent outline of the issues to be considered by franchisors in establishing their supply chain.
are reviewed and accepted, the franchisor is agnostic whether the franchisee purchases the items locally, from eastern Europe with little to no import duty based on free trade agreements, or Vietnam where the cost of production is so low that the items still cost less, notwithstanding the duty imposed. Then the franchisee is free to negotiate its own arrangements.

The specifications can rely on brand-specific quality for standards compliance and the franchisee is free to purchase from its own suppliers or oftentimes through optional volume purchasing contracts negotiated between the franchisor and the manufacturer or approved suppliers. While these permissive buying arrangements reduce the inherent conflict between the franchisor and franchisee over forced-line purchasing arrangements, unless the franchisee chooses to purchase through the franchisor’s optional purchasing programs, the franchisor is reliant on inspections and customer feedback to determine non-compliance.

At the opposite end of the spectrum, are franchisors with sophisticated supply chain arrangements where the franchisor has taken on the responsibility of analyzing the benefits and burdens of import restrictions against locally sourced suppliers, negotiated arrangements with manufacturers to take advantage of the manufacturer’s supply chain or negotiated additional supply chain links for logistics, and back-up with in-market suppliers and transportation. They have sophisticated purchasing portals where franchisees can purchase, and the franchisor and franchisee can track, the type and quantity of cups, straws, napkins, and food products purchased and where they are at any moment in the supply chain from the manufacturer to the counter and customer. These types of supply chain controls give the franchisor the ability to confirm compliance with product requirements and to monitor the franchisee’s performance and under-reporting by comparing purchases with sales.

The more proscriptive the franchisor is with respect to from whom franchisees can obtain their supplies the more the regulatory hurdles the franchisor must address from import restrictions (including, duties and tax) to competition laws that prohibit restrictions on purchasing and supplier arrangements that would have an anti-competitive effect. Further, once the franchisor takes on the obligation for the supply chain on a centralized basis, when there is a break in the chain the consequences can be significant.

For example, in February 2018, KFC had a breakdown in logistics for the delivery of chicken to its United Kingdom stores resulting in the temporary closing of 450 of its stores in the UK because of lack of chicken. The breakdown was the result of a logistics issue when KFC switched its delivery contract from Bidvest to a tri-party arrangement between KFC, DHL and Quick Service Logistics.11

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10 The Australian Competition and Consumer Act 2010 (CCA) S 47 deals with exclusive dealing and is just one example of laws that regulate supplier restrictions in franchise arrangements. The Australia Franchising Code of Conduct, (Industry Codes – Franchising) Regulation 2014 No. 168 is promulgated under the CCA. The UK Competition Act 1998, s.2, and Article 101(1) Treaty on the Functioning of the European Union (TFEU) also prohibit agreements that prevent, restrict or distort competition.

11 As of the date of this paper, the authors were unable to find any reported cases where franchisees were litigating claims against KFC in connection with the supply chain breach and only news articles describing the situation, and many referring to the masterful job KFC (Yum Brands) did in managing the public relations fall-out of the supply chain breakdown. Alexandra Topping, People have gone Chicken Crazy: what the KFC crisis means for the brand, The Guardian (February 24, 2018), https://www.theguardian.com/business/2018/feb/24/people-have-gone-chicken-crazy-what-the-kfc-crisis-means-for-the-brand; Kevin O’Marah, 3 Supply chain Lessons from the KFC Fowl-up, Forbes (March 1, 2018), https://www.forbes.com/sites/kevinomarah/2018/03/01/three-supply-chain-lessons-from-the-kfc-
E. Quality Assurance and Site Inspections

System standards must be adhered to in order to meet consumer expectations and can be measured and verified through several means. Every franchise agreement will have an inspection right and obligation to participate in a quality assurance program (if the franchisor has one). (See Appendix 3 for sample clauses that implement these requirements.)

Site inspections can be implemented through a variety of means, including, for example: (a) announced on-site inspections, which enable the franchisee to prepare and organize records for inspection, (b) un-announced inspections where representatives inspect the franchised location during business hours for cleanliness, condition, functioning of equipment, use of un-approved products, food safety, fire and life-safety, among others, and (c) mystery shoppers where no formal contact is made with the franchisee or manager and a report is submitted post-inspection (such inspections are typically more focused on customer service and independent observation). Obviously, implementing such an inspection regime with respect to the international portion of a franchise system is much more expensive compared to the domestic portion of the system. In that sense, it is quite understandable that franchisors that choose to utilize a master franchise model transfer much of the inspection burden onto the local master franchisee (in exchange for a fee split, of course).

Complete inspections should be conducted at least annually, to the extent feasible. Franchisors can use a carrot and stick approach with respect to the payment for inspection costs – no charge if franchisee passes and franchisee pays if it does not. Minimally, if a re-inspection is required because of the number of items found to be non-compliant, the franchisee should pay for re-inspection.

Inspections of the franchised location can be completed by a master franchisee (although, the franchisor must trust that the master is providing an accurate report). Inspections can also be conducted by an independent consultant with pre-prescribed criteria, typically contained on a tablet, that the consultant can simply check “yes” or “no” with very limited questions determined by the subjective opinion of the consultant. The consultant can take digital pictures that are attached to the digital report that is transmitted to the franchisor and the franchisee at the same time.

In determining compliance with brand standards as part of a comprehensive quality assurance program, franchisors will often combine the inspection report with customer satisfaction surveys. Health and safety items, depending on the importance, can result in an automatic failure. If the franchisor wishes to rely on the quality assurance program for default and termination of what it considers to be unacceptable non-compliance with standards, the franchisor should test the program for application variables to confirm it is being applied on a relatively consistent basis system-wide, and the degree of variation between passing and failing is material and demonstrable. Otherwise, if the program decision to default and terminate is not supportable from an evidentiary basis, the franchisor runs the risk of the termination of the individual franchisee being determined to be arbitrary and liability to the franchisee for damages and the whole quality assurance program subject to challenge.

fowl-up/#70baaf981cb1; Cat Rutter Pooley, KFC runs out of Chicken in Logistics Fiasco, Financial Times (February 19, 2018), https://www.ft.com/content/223d4df0-1595-11e8-9376-4a6390adbb44.
F. Change in Ownership

As further explained below, franchisors go to a great deal of effort to complete background checks and corporate due diligence to determine the ultimate beneficial owners of the interest of their franchisees to establish who controls the business and to comply with the Patriot Act and U.S. Executive Order 13224 (the “Executive Order”), including the requirement that none of the persons with whom it is transacting business are on the list of Specially Designated Nationals and Blocked Persons List maintained by the Office of Foreign Assets Control of the US Department of the Treasury (as described in greater detail below). Franchise agreements require the franchisee to identify who the owners of the franchisee are, contain representations of compliance with the restricted persons lists, and require the franchisee to provide notice to the franchisor of changes in the ownership structure. Additionally, depending on the nature of the transfer of ownership, certain franchise agreements require consent of the franchisor and compliance with a variety of conditions (which vary depending on whether the change of ownership is to affiliates and related persons or constitutes a change in control).

1. Unauthorized Changes of Ownership

It is not that unusual to find that franchisees have transferred interests without notice to the franchisor and without the franchisor’s consent. These transfers can range from transfers of minority interests by and among family members and transfers related to bringing in minority investors - to complete transfers of all of the assets of the franchised business to affiliated entities, all of which are done in violation of the agreement. The former is obviously of less concern, particularly if they are persons who are already cleared in the franchisor’s restricted persons compliance program. New minority interest holders must undergo a complete diligence and background check. A franchisor that requires a franchisee to pay the cost of the diligence and background check, as well as any related legal fees can more easily dis-incentivize some unauthorized transfers.

The latter is obviously a significant issue, as the entity operating the business and using the intellectual property is not the entity authorized to do so and a material default of the franchise agreement has occurred. That said, the main concern is rectifying the situation if there are no other defaults. The material transfers of the business often come to light through one of the following four scenarios: (a) when the franchisee provides its annual confirmation of insurance, the franchisee’s name does not appear on the insurance certificates, (b) when a franchisee’s accounting department requests that the franchisor provide a billing invoice in the name of a different entity, (c) when a franchisee notifies the franchisor of a corporate name change, or (d) when a lender requests a comfort letter or estoppel certificate for an entity that does not match the franchisor’s records.

When this occurs, the franchisee should immediately receive a formal notice of breach under the franchise agreements and a notice sent to the address of the new entity that they are unauthorized users of the trademarks and system and that the franchisor reserves all rights. The issue is often just sloppiness in franchisee’s maintenance of corporate formalities. Putting the franchisee in formal default without understanding the full picture could cause unintended

12 USA PATRIOT Act, Pub. L. No. 107-56, 115 Stat. 272 (2001). Companies with offices doing business in the United Kingdom must comply with the Terrorist Asset Freezing Act of 2010 and with offices doing business out of the European Union member countries, the European Financial Sanctions List, all of which may be searched through the use of services routinely, as noted below.
consequences for the franchisee. For example, a default of the franchise agreement could cause a default of the franchisee’s loan, which may result in the franchisee’s lender demanding payment of such breached loan agreement. Further, a default of the franchise agreement could cause the franchisee’s landlord to claim a default of the lease agreement in an attempt to terminate the lease agreement or re-negotiate the amount of rent. These issues are often resolved amicably and quickly with the franchisee by appropriately documenting the transfer, but it is important to convey the importance of compliance with the transfer provisions.

2. **Authorized Changes of Ownership**

   A best practice in this area is to routinely audit a franchisor’s system information by requiring the franchisees to certify every few years that the ownership information in the franchise agreement is correct. This will often ferret out minority interest changes that have occurred (as well larger issues). It is a rare occasion where a complete change of control has taken place without notice and consent. Franchisees generally understand the non-transferability of the franchised business and a buyer or its lender has usually reviewed the franchise agreement and understands the need for consent.

   When the franchisor receives a notice of intent to transfer a controlling interest in the franchised business or franchisee, the franchisor should immediately respond and request all information necessary to consent to the transfer to prevent any claim that the franchisor has failed to timely respond and interfered with the franchisee’s sale. The franchisor must complete its diligence process, which can be lengthy and costly in the international context given the need for local counsel to read and interpret a franchisee’s formation documents and sale and purchase documents that are customarily in the local language. In addition, the franchisor should demand the franchisee comply with any and all conditions of transfer, including, for example, bringing the franchised business up to standards, moving the buyer to the new form of franchise agreement, making any transfer payments, signing a general release and complying with applicable franchise laws.

G. **Development Schedules**

   If the franchisor has entered into area development arrangements or master franchise agreements for its international expansion plans, it is the exception, not the rule that the franchised locations open for business in accordance with the development schedule. Delays in the development and opening of franchised locations in many foreign jurisdictions are the norm, as planning and obtaining applicable permits is often times more difficult and subject to changes in political viewpoints of differing administrations.

   In the international context, as with domestic transactions, it is imperative to timely document delays and whether they are accepted, and if not, whether the result is a cancellation or reduction of development rights. In many civil law jurisdictions, franchisors will be generally held to a standard of dealing of commercial reasonableness, regardless of the terms of the development agreement. So, for example, if a franchisee has been diligently pursuing the development of a location, and the franchisee is delayed for reasons beyond its control – planning, permitting, construction has unearthed an archeological find, for example – the courts may see the franchisor’s action to cancel or reduce those rights as unreasonable. Further, course of conduct is also determinative in that if the franchisor has accepted a delay before and not objected and allowed the franchisee to continue to develop it may be estopped in the future, particularly if the franchisee has continued to spend money with the expectation that it would be permitted to go forward. So, from a compliance perspective, it is important for the franchisor to
be clear and have documented its willingness to accept the delays or not (and in many jurisdictions – act with commercial reasonableness regardless of the precise timing of the contract).

III. GOVERNMENT FILINGS

The need to undertake a myriad of government filings and other compliance tasks when a franchisor expands internationally is one of the biggest differences between domestic franchising and international franchising, and a challenge which the franchisor's staff and their legal advisors are often ill-equipped to tackle.

To effectively deal with this challenge, it could be useful to keep in mind the three concepts outlined below. These three concepts often underpin franchisors’ operations manuals in addressing various aspects of the system requirements. They provide a useful framework in providing the context of this discussion regarding foreign regulatory filings.

**Policy.** A franchisor should have a corporate policy mandate regarding these government filings. It is difficult to see anything other than compliance being such a mandate.

**Standard.** By standard, we mean the degree or level of achievement, in support of the policy of being in compliance. In other words, the standards define the key factors in considering the compliance goal, and outline how that goal can be measured. As anyone who has engaged in international franchising knows, often times, the foreign regulations are not clearly defined, some of the requirements could be impossible to comply with, and the legal consequences of non-compliance varies. A franchisor must set its own standard when it comes to foreign regulatory compliance issues. This standard will then guide its staff and legal advisors in arriving at conclusions that reflect its policy.

**Procedure.** A procedure sets forth a particular course of action or way to proceed, which is guided by the standard, with the goal of achieving the policy. Procedures provide information about how to do something; however, they must be considered with the guidance of the standard. In addition to setting the standard that will support its compliance policy, franchisors must establish a set of procedures that will implement the compliance policy. The focus of the discussions in this part of the paper is to lay out a framework that will help a franchisor establish such a set of procedures.

In the last four decades, there has been a proliferation of franchise laws around the world. Franchisors and their legal advisors are by this point quite familiar with those foreign laws and regulations that require pre-sale disclosure; if not the detailed disclosure requirements country-by-country, at least the notion that disclosure is required in advance of franchise transactions in certain countries, and the need to analyze and comply with these disclosure requirements. There also have been many good summaries, surveys, and handbooks about these international franchise disclosure laws and regulations. By their very nature, however,

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14 See, e.g., Andrew P. Loewinger and Michael K. Lindsey, International Franchise Disclosure Laws, ABA 25th Annual Forum on Franchising, Oct. 9 – 11 (2002); Richard M. Asbill and Jane W. LaFranchi,
these publications focus on the “getting the deal through” aspect, and to a large degree do not deal with post-signing regulatory compliance issues. There have been surveys published regarding the signing formalities and post-signing regulatory obligations. But they take a more “micro” approach in detailing various requirements that exist in a select group of countries.

We will take a slightly different approach here. What we provide in Appendix 1 is not a summary of the post-signing regulatory filing requirements in various countries; rather, it is a checklist of various concepts that should be examined (guided by the franchisor’s relevant policy and, more importantly, standard). Actually, it is more of a procedure than a traditional checklist, as we try to annotate various topics with details that will help a franchisor and its legal advisors in examining them. It is intended to be a living document, not an exhaustive survey – as the franchisor enters any specific international market, the inquiries outlined in this procedure are intended to serve as the beginning of the process, and additional details should be added when new issues are encountered.

After examining this checklist, it will become abundantly clear that most of the requirements stem from the contractual relationship between the franchisor and the franchisee. It doesn’t necessarily mean that the franchise agreement itself needs to be filed. Rather, because the franchise agreement represents a bundle of different rights and obligations, various subject-specific laws and regulations will require some sort of filing with respect to the relevant aspect of the franchise relationship – e.g., trademark license, payment, tax remittance, etc.

While some of these requirements are only relevant to cross-border franchise transactions where the franchisor is a foreign entity (e.g., filings related to foreign exchange controls), a significant number of these requirements apply equally to domestic and international franchise transactions. This is often one area that is overlooked by international franchisors and their advisors – they focus on those regulatory requirements that are specific to cross-border transactions but sometimes neglect to pay enough attention to regulatory requirements that do not distinguish between domestic and international transactions.

Lastly, while these filings by and large do not affect the substance of the franchisor-franchisee relationship as embodied in the franchise agreement, and therefore could be dealt with post-signing (or at least after the completion of the substantive negotiation of the contract terms), there are two important caveats:

- One, given the need to register the franchise contract in various countries, it is essential to have a general understanding of these requirements before designing the template agreements to be used internationally to facilitate such filings and reduce the related costs. As an example, this examination often leads franchisors to abandon the single-unit franchise agreements they use for

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domestic transactions in favor of multi-unit franchise agreements, which often help reduce the number of filings in foreign jurisdictions. However, it should be noted that a single agreement governing the development and operation of multiple franchisee units may not be the right structure for some systems and franchisors. There are many other factors that will need to be considered in arriving at a sensible template approach for a franchisor, but it would be a mistake not to treat the complexity and cost of foreign regulatory filings as one of those factors.

- Two, in some instances, the regulatory filings give rise to government fees and/or taxes that are quite substantial, or reflect substantive restrictions on economic terms. These factors would need to be carefully considered before signing a franchise agreement in the relevant jurisdiction, and cannot be left aside until after the parties have signed on the dotted line. By then, it would be too late to allocate the regulatory compliance cost.

Therefore, while it is true that most of the tasks identified through the checklist will be accomplished post-signing, it is of critical importance to understand all tasks and their ramifications before embarking on any cross-border franchise arrangement, for they may impact the agreement structure and/or terms, in a few cases substantially.

IV. LEGAL COMPLIANCE

In addition to ensuring a franchisee’s compliance with operational requirements and complying with government filing requirements, a cornerstone of a healthy relationship between a franchisee and a franchisor also calls for a franchisor to closely monitor the franchisee’s compliance with certain laws of mandatory application, including, among others, anti-corruption

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16 For example, in Argentina, certain legal instruments supporting commercial transactions (including franchise agreements) are subject to stamp tax. Unlike most other jurisdictions, where the stamp tax rate is quite low or subject to a manageable cap, the stamp tax in Argentina is around 1% in most provinces (1.2% in the Province of Buenos Aires), and there is no cap. As such, a long-term, multi-unit franchise agreement could be subject to a significant amount in stamp tax. To further complicate the matter, the stamp tax tends to be a “local” or “provincial,” rather than “national” or “federal,” tax, which means that a multi-unit franchise agreement that contemplates operation in various locales could be subject to stamp taxes in multiple provinces. Lastly, stamp taxes are by and large paid up-front, with no mechanism for refund if the agreement is terminated early (or, in some jurisdictions (including Argentina), even if the agreement never went into effect because the conditions precedent were not satisfied). Because of these complications, before (not after) finalizing the economic terms of the franchise agreement, franchisors must seek clarification on the stamp tax amount, and whether there are any legally permissible means to structure the relationship so that it is not subject to stamp tax in a certain jurisdiction; and if there are such tax avoidance strategies, whether they conform to the franchisor’s relevant standards regarding foreign regulatory and tax compliance.

17 As an example, in Pakistan, the foreign exchange related filings with the local bank and foreign exchange authority reflect a tightly controlled foreign exchange remittance regime that is quite uncommon at this point in most other countries, and that many say are unconstitutional. It limits the upfront fee payment to $100,000, and royalty at 5% of a subsect, not all, of the franchisee’s gross sales. In addition, it limits the approved payment period to 5 years, and when the time comes for extension of that 5-year period, the parties are required to justify the extension to the government/State Bank of Pakistan. See, Foreign Exchange Manual, State Bank of Pakistan (January 31, 2002).
laws, including the US Foreign Corrupt Practices Act of 1977 (“FCPA”)^18, and anti-terrorism laws, including the Executive Order. Franchisees’ compliance with such laws of mandatory application reduces potential liability on the part of the franchisor and its decision makers.

A. **Legal Framework**

1. **FCPA**

The FCPA originally prohibited U.S. companies and individuals from making improper payments to foreign officials, parties, or candidates, in order to obtain or retain business. The FCPA was later expanded through certain amendments in 1998. As a result of such amendments the jurisdiction of the U.S. government was expanded to prosecute (a) foreign companies and nationals who assist in the payment of bribes in the United States, and (b) U.S. companies for the acts of foreign subsidiaries or agents who assist in the payment of bribes. The FCPA has two main components. The first is a prohibition of making payments to any foreign official and certain other parties for the purpose of obtaining or retaining business, with the term “foreign official” and other elements of the FCPA being interpreted broadly. The second component requires companies to keep accurate financial records and maintain internal controls. Such safeguards reduce the likelihood of improper payments being made and permit the detection of any such payments.

a. **Anti-Bribery Provisions of the FCPA**

The FCPA prohibits any person from corruptly making an offer, promise, or authorization of payment of any money, gift, or anything of value to any foreign official, political party or official thereof, or candidate for political office for purposes of: (a) influencing or inducing any act or omission of an individual, or securing any improper advantage; or (b) inducing such individual to use their influence to affect any act or decision of a foreign government or instrumentality in order to obtain or retain business for any person. The FCPA also prohibits any such proscribed payments made through a third party.

A “foreign official” is an officer or employee of a non-U.S. government, or public international organization (“PIO”), or anyone acting in an official capacity relating to such government or PIO. This includes persons who perform traditional governmental or administrative functions, as well as employees of an entity that the government controls or has an ownership interest in. Such employees may still qualify as a foreign official even if they perform business-related functions for an entity engaged in commercial activities. A foreign official may also include an official of a foreign political party or a candidate for public office.

The term “corruptly” is used in the FCPA in order to make clear that the intention must be to induce the recipient to misuse their position in order to wrongfully direct business, obtain preferential legislation, or secure an improper advantage. The word suggests an improper motive or intent to wrongfully influence the recipient.

To be in violation of the FCPA, the person must “know” the corrupt payment is being offered. However, the knowledge element does not require “actual” knowledge. Knowledge exists when the person is aware that a “result is substantially certain to occur” or has a “firm

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belief that such circumstance exists.” As such, conscious disregard, deliberate ignorance or willful blindness will not avoid liability.

A company may be fined up to U.S. $2 million for each violation of the anti-bribery provision of the FCPA. Under alternative sentencing provisions, these penalties can be increased significantly. Any employee, agent, officer, director or stockholder, who acts on behalf of a franchisor and violates the FCPA, may be fined for each violation up to U.S. $100,000 or up to twice the amount of the gross gain or loss derived by any person from the offense, or imprisoned for up to five years, or both. Any company and any employee, agent, officer, director or stockholder of such franchisor who violates the FCPA may be personally subject to a civil penalty of not more than U.S. $10,000 for each violation, as well as civil injunctions. The FCPA prohibits a company from directly or indirectly paying a fine imposed upon an individual. In addition to these penalties, there may be collateral penalties and fines, including disgorgement of profits attributable to contracts secured through bribe payments, appointment of a government-imposed monitor on company activity, and negative publicity.

b. Books and Records Provisions of the FCPA

All U.S. or foreign companies whose shares are listed on a U.S. stock exchange must maintain a system of internal accounting controls and make and keep books and records that accurately, fairly, and truly reflect their assets. No undisclosed or unrecorded fund or account may be established.

This system must reasonably assure that (a) executed transactions are approved by management; (b) transactions are recorded to permit preparation of accurate financial statements and accountability for assets; (c) access to assets are approved by management; (d) appropriate auditing functions are conducted; and (e) any improper payments can be identified.

The books and recording provision does not require the knowledge element discussed above. Moreover, there is no “materiality” standard, which means that even unintentional or immaterial misstatements can give rise to liability. Both diligence and vigilance are required to produce and maintain accurate books and records.

Willful violations can result in penalties of up to $25,000,000 per violation for companies and $5,000,000 for individuals. Non-willful violations can result in a maximum fine of U.S. $1 million and/or imprisonment of no more than ten years for individuals, and a maximum fine of U.S. $2.5 million for companies. Individual penalties cannot be reimbursed by a company. Additionally, there may be collateral penalties and fines, including disgorgement of profits, government-imposed compliance monitoring of company activity, and negative publicity.

c. FCPA and Franchising

With this background, U.S. franchisors should keep in mind that the FCPA has been greatly expanded in recent years with U.S. authorities attempting to hold companies liable for
the acts of other parties in their supply chain. The majority of FCPA enforcement actions in 2017 involved some use of third parties.

A prominent example involves Eli Lilly and Company (“Eli Lilly”), a pharmaceutical company who entered into a distribution agreement with a local distributor in Brazil and later settled an FCPA action with the Securities and Exchange Commission (“SEC”) for $29.4 million U.S. dollars as a result of the distributor’s corrupt payments to local Brazilian officials. Due to Eli Lilly’s close relationship with the Brazilian distributor, the SEC found that Eli Lilly should have taken additional actions (which we mention below) when such Brazilian distributor requested increased price discounts. Ultimately, the price discounts freed up certain funds that the distributor later used to pay the bribes.

As with a distributorship relationship, a franchise relationship involves two independent parties dealing at arm’s length for commercial gain. In both scenarios the parties have an ongoing relationship where they are part of each other’s supply chain, with the franchisee and the distributor making ongoing payments to the franchisor and principal, respectively, and engaging in marketing and other activities on behalf (to a certain extent) of the U.S. franchisor or principal. With such similarities in mind and given the Department of Justice’s and SEC’s broad interpretation of the FCPA, a franchisor can never be too careful when protecting itself against FCPA risks arising from its international franchisees.

2. **U.S. Executive Order 13224**

The Patriot Act was established in response to the tragic events taking place in the U.S. on September 11, 2001, with the Executive Order being enacted two weeks after the attacks. The Executive Order prohibits “any transaction or dealing by United States persons, or within the United States” with persons or companies who are suspected terrorists or associated with suspected terrorists (the “Blocked Persons”). It is noteworthy that this law prohibits transactions or dealings with “suspected” terrorists, which effectively eliminates the U.S. government’s burden to prove that an individual is a terrorist by lowering the threshold to “suspected” terrorist.

Further, a violation of the Executive Order needs not be purposeful. Rather, a non-willful violation may still subject a franchisor to civil penalties and fines, while a willful violation may

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subject a franchisor’s officers, directors, and agents to criminal penalties of up to 10 years of prison.

The Office of Foreign Assets Control of the US Department of the Treasury created and maintains the Specially Designated Nationals And Blocked Persons List. While such list originally contained only twenty-seven names, it now contains hundreds of names and is regularly updated by the Office of Foreign Assets Control. However, the Specially Designated Nationals And Blocked Persons List is now more easily searchable with the release of the Sanctions List Search Application. Additionally, various other countries have also created ongoing lists along the same lines as the Specially Designated Nationals And Blocked Persons List and there are certain services that can easily search the various databases in a matter of minutes.

The ease of access to such list makes it virtually impossible for a franchisor to claim that it did not have actual or constructive knowledge that it is doing business with a specially designated individual. However, in addition to checking such list, we recommend franchisors to perform a more detailed background check as described further below.

B. Compliance Tools

1. Due Diligence

In light of a franchisor’s potential risk of liability under the FCPA, Executive Order, and other laws of mandatory application, it is of utmost importance that a franchisor closely monitors its compliance, as well as its franchisees’ compliance, with such laws. The first step, which is due diligence on the potential franchisee’s background, should take place long before the franchise agreement is executed. In addition, as described in Section II above, at least some due diligence should be carried out throughout the franchise relationship to ensure the franchisee parties have not changed. In the event of a change in the franchisee’s ownership or the prospect of a new franchisee, then the franchisor should perform due diligence with respect to such new parties. Because due diligence is an ongoing concern, we provide certain guidelines and related best practices.

At the outset, the franchisor should carry out strategic due diligence that will identify with whom the franchisor is doing business. To understand with whom the franchisor is doing business, a franchisor must ascertain with precision who are the entities and individuals that own the franchisee entity, up to the level of identifiable individual shareholders, partners, members, or beneficiaries that are individuals and not legal entities (the “Owners”). Such information may be obtained and confirmed first hand upon the franchisor’s detailed review of the corporate charter and shareholder’s registry of each of the franchisee and its Owners. Such review should also reveal whether a franchisee or any of its Owners allows the issuance of bearer shares or has granted any rights or options to third parties which may result in a change of ownership.

23 For example, Mexico created a similar list with the same purposes as the U.S. Blocked Persons List. See, Silber Mesa, Crean Lista Negra de Terroristas en Mexico, El Universal (Dec. 8, 2015), http://www.eluniversal.com.mx/articulo/periodismo-de-investigacion/2015/12/8/crean-lista-negra-de-terroristas-en-mexico.
Once the ownership structure has been identified, a franchisor should conduct a detailed screening of the franchisee and each Owner, including a background check. For certain franchisees in high-risk markets, a franchisor may decide to engage an experienced investigator to conduct the background checks to ensure that the franchisee has represented itself accurately in their paperwork. The background check will help the franchisor understand reputational and other risks, including whether the franchisee or any of its Owners have in the past had any proceedings or accusations in the corruption and terrorism fields, or have been placed on a list of Blocked Persons.

A background check should at least include a review of printed and online media, as well as a search of court records, including civil, criminal, bankruptcy filings, as well as any liens and judgments entered against the franchisee or Owner. Such records should be checked in the jurisdiction where the franchisee or Owners are located and any other known locations. The breadth and depth of such background check must be adjusted depending on the franchisee and its owners. For example, to the extent that any of the individual Owners of the franchisee is a high net worth business leader with political influence, then such background check must contain additional checks. Additionally, an experienced investigator will help the franchisor understand which sources of information may be credible depending on the jurisdiction where the franchisee or its Owners are located.

In addition, such background checks will likely provide certain information to the franchisor regarding whether the franchisee or any of its Owners is a political figure, such that he or she may fall under the broad definition of a “foreign official” under the FCPA. While it is not against U.S. law for a franchisor to enter into a franchise agreement with a franchisee that is owned directly or indirectly by a foreign official, there are certain additional safeguards that a franchisor may put in place to reduce the risk of any improper payments being made for the benefit of the franchisor.

In the event that a franchisee is owned, directly or indirectly, by a foreign official or a party related to a foreign official, then a franchisor may include additional language in the franchise agreement to obtain the franchisee’s representation and warranty that it will not use such position or relationship to gain commercial advantage. Another tool that a franchisor may use is a questionnaire. A questionnaire allows the franchisor to accurately identify any potential issues and monitor the relationship. For example, if the franchisee’s Owner works in the transportation authority, there may be risks that the franchisee could obtain certain permits using its relationship with the owner. Once such area of risk is identified, the franchisor should document any effort on its part to ensure that the franchisee has not taken advantage of its relationship with a foreign official.

As mentioned, it is important for a franchisor to carry out certain due diligence with respect to a potential subfranchisee. However, we also suggest that a franchisee should endorse any subfranchisee it recommends to the franchisor and should represent that it has conducted appropriate due diligence and that the subfranchisee has passed such scrutiny.

2. **Compliance Policy and Training**

Having a robust compliance program is key in the increasing global environment in which franchisors operate. As a baseline, a franchisor’s compliance policy should be a written
policy, which includes a code of conduct.\textsuperscript{24} In addition, franchisors should have detailed written policies covering issues such as bribery, corruption, trade, antitrust, data privacy, money laundering and accounting practices, as well as clear procedures and protocols for making sure these policies are followed and enforced (including detailed policies with respect to due diligence, as mentioned above). We also recommend, as a best practice, to have checklists and summaries of such compliance policy, which are targeted to the franchising aspect of the company, are easily accessible and are distributed to the right constituents within the franchisor, and, potentially, the franchisee.

While having an easily accessible, written policy is a baseline, one of the most critical elements of a strong compliance program is properly training the franchisor’s officers, employees, and potentially, franchisees (as discussed further below) on relevant laws, regulations, corporate policies, and prohibited conduct. When determining whether a franchisor’s training program meets its expectations for effectiveness, government authorities often scrutinize who a company trains, how the training was conducted and how often training occurs.\textsuperscript{25}

As such, a franchisor’s compliance training should be specifically tailored to the franchisor’s industry and, among others, identify factual scenarios that should raise red flags.\textsuperscript{26} Such factual scenarios generally surround a franchisee’s interaction with foreign officials. For example, a franchisor’s employees should be trained to pay close attention when a franchisee experiences unnecessary, non-customary delays when dealing with foreign officials, including, for example in the event imported goods are unnecessarily held by foreign officials, or in the event that requested permits are unnecessarily delayed. Further, as already mentioned, employees should be trained to closely monitor a franchisor with family ties to foreign officials, including providing clear guidelines for gift-giving and hospitality efforts. As a final example, a franchisor’s employees should be trained to insist upon receiving itemized reports of a franchisee’s marketing expenditures. We attach a sample Risk Assessment Questionnaire as Appendix 2, which should help a franchisor further identify any areas to address during compliance training.

Further, franchisors should aim to develop annual training plans in order to reiterate known compliance risks as well as explore any new areas of concern or any new legal developments, given how quickly enforcement trends and anti-corruption laws change.\textsuperscript{27} Any such new developments should be incorporated into annual compliance trainings. The plans should include schedules for tracking when employees complete required compliance training, and tools like reductions in performance scores for staff or supervisors who fail to complete required training can be used to encourage timely completion. As best practice, we recommend live training, especially to (a) the teams who are on the ground either to recruit new franchisees


\textsuperscript{25} Id.


\textsuperscript{27} Cunningham and Jezierski, Supra note 24.
or to monitor existing franchisees, and (b) the teams who are directly in contact with the franchisor’s local teams.

Any such training efforts should be thoroughly documented. Documenting the compliance training efforts would be helpful in the event of an investigation, in order to show the steps that the franchisor took to avoid corrupt practices.

In addition to performing annual compliance training for the franchisor’s employees, a franchisor may also consider training a key personnel from its franchisees. Such training could be conducted together with the brand training mentioned in Section II. above, and should be more along the lines of explaining the various U.S. laws of mandatory application under the assumption that each franchisee should have its own compliance policy and best practices. As with other aspects of a franchise relationship, increased control over a franchisee’s compliance-related practices also increases the franchisor’s related exposure.

3. **Contract Provisions**

Franchise agreements should include strict compliance covenants that at a minimum cover three core concerns: (i) adherence to the anti-corruption laws that are of most relevance to the relationship,(ii) broad audit rights, and (iii) termination rights.\(^{28}\) We provide in Appendix 3 certain sample contractual clauses addressing some (not all) of the main issues arising in each of the areas mentioned above. In the end, the contractual clauses should give a franchisor an undisputed right to terminate a franchise relationship in the event there are violations or attempted violations of the FCPA, Patriot Act, or other laws of mandatory application. In addition, franchisors may add contractual clauses requiring ongoing reports that could provide the franchisor with visibility into the franchisee’s operations (in addition to being a tool for calculation of royalty fees) and into any suspicious payments and missing funds that could indicate misappropriation or off-the-books transactions.

4. **People**

A successful compliance program “has a solid foundation of ethics and integrity that is fully endorsed by senior management,” including a high ranking compliance officer with the authority and resources to manage the program.\(^{29}\) Such compliance officers should have direct access to the board of directors and should promptly report any matter involving criminal conduct. In addition, a company’s board of directors should directly oversee the implementation of the compliance program, ensure that it is effective in addressing the risks mentioned above, and provide direct supervision of those responsible for implementing the program. The board should be familiar with the international growth and franchising efforts. Further, the compliance department should have a direct channel of communication with the franchisor’s employees who are on the ground or who monitor those on the ground. The franchisor’s employees working directly with franchisees are the most likely to identify and address any potential issues before they become compliance issues that put the franchisor at risk.

When determining whether companies maintain adequate oversight of their compliance programs, enforcement officials look for three key components: (i) monitoring, (ii) auditing, and

\(^{28}\) *Id.*

\(^{29}\) *Id.*
(iii) responding. “Monitoring is a commitment to reviewing and detecting compliance problems in real time, then acting quickly to remediate them, [while an] audit is a more limited review that targets a specific business component, region or market sector during a particular timeframe to uncover or evaluate certain risks.” A robust compliance program should include separate monitoring and auditing functions.

V. CONCLUSION

In conclusion, franchisors must remain attentive to the several aspects of their relationship with each of its potentially hundreds of franchisees. Each such franchisee must continue to be carefully monitored through the use of institutional policies and systems that allow the franchisor to monitor operational compliance, compliance with local filings, and further legal compliance. Such institutional policies must be accompanied by targeted training and committed personnel who help maintain the brand and legal standards. Finally, in the ever changing international arena, franchisors must continue to update their policies and systems, and continue to zealously advocate for the contractual protections that facilitate the franchisor’s rights to continue to maintain uniformity in its global brand.

30 Id.
### Appendix 1

**Government Filing Checklist**

<table>
<thead>
<tr>
<th>Topic</th>
<th>Practice Note</th>
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<tbody>
<tr>
<td><strong>1 Franchise Agreement Filings</strong></td>
<td>Unlike the franchise laws in the United States and other common law jurisdictions (e.g., Australia), in many civil law jurisdictions with specific franchise laws, filings after the execution of the franchise agreement are often required. Examples include Russia, Belgium, and Indonesia. Ukraine used to require such a registration filing (although implementation regulations were not issued for a decade), but scrapped the requirement as part of its gesture to more closely align with the West after the annexation of Crimea.</td>
</tr>
<tr>
<td><strong>1.1 Does the franchise arrangement need to be filed with any government agency pursuant to the requirements of specific franchise laws?</strong></td>
<td>It is important not to presume that the full franchise agreement must be registered. As the intent behind the agreement registration is to verify the existence of the relationship itself, rather than to record every single term or condition of the agreement, submitting a short-form or a summary, rather than the full franchise agreement, is often acceptable. If a short-form or summary is permissible, franchisors need to weigh the benefit of only presenting a short document (rather than the full-length franchise agreement) to the government, against the cost and complexity of preparing this additional document. It should not be assumed that a short form is always the best approach.</td>
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<tr>
<td><strong>1.2 If so, does the full franchise agreement need to be filed?</strong></td>
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</tbody>
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31 Grazhdanskii Kodeks Rossiiskoi Federatsii [GK] [Civil Code] art. 1028(2) (Russ.).


34 On Amendments to Several Legislative Acts of Ukraine regarding the Facilitation of Conditions for Doing Business (Deregulation), April 5, 2015.
1.3 If the full franchise agreement does not need to be filed, what information/terms will need to be included in the filings/documents submitted to the government?

If a short-form or summary is permissible, or alternatively the franchisor or the franchisee is required to fill out a form, such a document will likely have to contain certain mandatory information. It is important to find out what those mandatory requirements are to ensure that the document is sufficient, while not being unnecessarily long (which would defeat the purpose of not using the full franchise agreement).

In addition, it is possible that even though a summary or short-form is allowed, the franchise agreement itself must be included (e.g., the franchise agreement filing regime in Belarus under certain circumstances). It doesn't necessarily negate the advantage of submitting a short-form (e.g., it may still help avoid any substantive review of the franchise agreement itself), but it is certainly an important factor to consider.

1.4 Will the submitted documents have to be translated? If so, is there any requirement as to who prepares the translation?

In jurisdictions where English is not the official language, submissions will most likely have to be in local language. This means that the submitted franchise agreement, or the short-form agreement, will have to be in a bilingual form or accompanied by a local language translation. If this is the only reason to prepare a local language version of the agreement (whether the full franchise agreement or the short-form), then the franchisor should consider whether there are sufficient justifications to invest in a high-quality translation given the limited purpose. In some countries, however, the translation must be prepared by a certified translator (e.g., Indonesia), or certified by the translator as being accurate (e.g., China). Such requirements obviously limit the pool of potential service providers who can translate the document, and often lead to the use of a translator based in the foreign country, rather

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35 This is different from the mandatory language requirement that exists in certain jurisdictions (e.g., Indonesia, Quebec, and France). However, even in those jurisdictions that require documents to be in the local language, it is often permissible to use English as the only language or the governing language in a cross-border commercial agreement with a foreign party, or if the parties expressly waive the local language requirement.
1.5 Does the government agency engage in substantive review of the terms of the arrangement, with the possibility of demanding changes to the franchise agreement terms?

If the government agency engages in substantive review, this obviously poses a serious challenge to the deal process – how can parties execute a franchise agreement knowing that the government can demand changes to the agreement terms? The parties presumably will be guided by counsel in trying to preemptively address as much as possible all changes likely demanded by government officials. However, this may not always work. The franchise agreement should include provisions addressing situations where, post-signing, a government agency requests substantive changes to the agreement. For franchisors, it is important there is a safety valve that allows the franchisor to exit the franchise agreement if amendments demanded by the government officials (which almost always are in favor of local franchisees) change any fundamental aspect of the parties' bargain as reflected in the franchise agreement. The franchisor should also consider including a termination right if certain government filings are not approved within a set period of time.

If the franchisor is dealing with a jurisdiction that does engage in substantive review of the franchise agreement terms, in addition to making sure the agreement contains appropriate language addressing such review and the possibility of exit, the franchisor should also find out beforehand whether the relevant agency would allow a pre-filing clearance (i.e., reviewing and clearing the agreement in its draft form), or an informal review (i.e., an informal process that has no legal effect but would typically give the parties a good indication of the relevant issues).

than a US-based translation company.
<table>
<thead>
<tr>
<th>Topic</th>
<th>Practice Note</th>
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<tbody>
<tr>
<td>Trademark License Filings</td>
<td>Most countries determine priority of trademark rights on a first-to-file basis, rather than the first-to-use basis used in the US and a few other common law jurisdictions. In those first-to-file countries, often a registered trademark can be cancelled if it has not been used for a period of time (typically 3 or 5 years). Therefore, it is important for a franchisor to be able to defend such a non-use cancellation attack by utilizing the evidence of use of its trademarks by the local franchisee. In some jurisdictions, the method of establishing such a defense is to register or record the license of the trademarks. Franchisors should note that to accomplish such a registered user or trademark license recordal, it would be necessary to establish the “chain of title” starting from the owner of the registered trademark in the relevant country all the way to the franchisee. If the franchisor does not itself own the relevant trademark registrations, then the license from the trademark owner to the franchisor must be established first.</td>
</tr>
<tr>
<td>Must the license of the trademark from the franchisor to the franchisee be registered?</td>
<td>In virtually all jurisdictions that have this type of filing, it is not necessary to file the full franchise agreement for this purpose. Typically, a short-form (and, if necessary, bilingual) trademark license agreement or registered user agreement would suffice. Sometimes, it is only required that the parties complete an application form that asks for information about some basic terms of the trademark license (e.g., term, licensed area, license fee, the relevant parties, etc.). In a few jurisdictions, it is sometimes expected that the entire franchise agreement be attached as an exhibit to the short-form trademark license agreement, but franchisors should explore with their legal advisors to see if alternative approaches can be used to satisfy the officials handling the filings.</td>
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<td>What needs to be filed for this type of filing?</td>
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<td>2.3 If it is optional, is there any benefit of registering the license of the trademark?</td>
<td>The general trend is that more and more countries are taking the position that a registered user or trademark license filing is not legally required for the franchisor/licensor to later on use the evidence of use by the franchisee/licensee to defend against non-use cancellation attacks. Nonetheless, a franchisor would be well advised to inquire further to see if there are other benefits to undertake such a filing. In some countries, such a recordal of the trademark license entitles the franchisee to obtain the necessary foreign exchange approval to remit payments overseas. And in some cases, the franchisees would push for such a filing for its own reasons.</td>
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3 Technology Transfer/License Filings

3.1 Is the franchise agreement considered a technology transfer or technology license arrangement covered by the relevant legislation? Many developing countries have adopted technology transfer or technology license laws with the aim to protect the domestic transferees/licensees from the perceived exploitation by the foreign technology holders. Some of these laws are drafted very broadly to cover a business format franchise arrangement, as such an arrangement contemplates the provision of know-how by the franchisor to the franchisee. It is less so with regard to product distribution franchise arrangements, but this distinction may not matter much if the franchisor/supplier will also license know-how, or even license the franchisee to locally produce proprietary products. |

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36 For example, in Brazil, to obtain Central Bank’s approval of making payments under a cross-border franchise agreement, the agreement will first have to be filed with its trademark office – Instituto Nacional da Propriedade Industrial (INPI).

37 For example, until January 2018, franchisees in Argentina were only permitted to deduct trademark royalties for their corporate income tax filings, if the underlying trademark license arrangement is registered with its trademark office (Instituto Nacional de la Propiedad Industrial – INPI).
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<tr>
<td>3.2 Does such legislation require government filing of the executed agreement?</td>
<td>Most of these laws simply require that the terms of the agreement be consistent with the requirements under these laws. A few require filings to confirm compliance. For those few countries with filing requirements, given the goal is to confirm compliance, substantive review of the contractual terms is inevitable, and poses the challenges we discussed in #1.5 above.</td>
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4 Foreign Exchange Approvals

4.1 Does the foreign country regulate outbound payments?

The general trend is that exchange control restrictions adopted by a number of developing countries have been liberalized in recent years. In particular, royalty/franchise fee payments under franchise agreements have been treated as being automatically approved in many countries with foreign exchange restrictions (including, e.g., Argentina, India, Pakistan, China, South Africa, etc.), subject to certain limitations.

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38 As an example, in the Philippines, franchise agreements are treated as technology transfer arrangements regulated under its Intellectual Property Code. As such, if a franchise agreement contains terms that are not permissible under the Intellectual Property Code, the entire agreement would be deemed unenforceable in the Philippines. Franchisors could choose to register the franchise agreements with the Intellectual Property Office’s Documentation, Information and Technology Transfer Bureau (DITTB), which has also been vested with the power to grant exemptions of certain provisions often seen in franchise agreements.

39 Communication A 6244, the Central Bank of Argentina, May 19, 2017 (Arg.).


42 Foreign Exchange Management Regulations, State Council, August 5, 2008 (China).

4.2 If so, are filings with one or more government agencies required before the franchisee is permitted to make payments to the foreign franchisor?

Practice Note
A few countries still require filings with the government before such payments are permitted. Examples include Brazil, Russia, and Nigeria. By their very nature, filings to obtain exchange control approvals will have to be completed before any payments are made (at least with regard to payments from within the foreign country; funds outside of the country obviously are not subject to such country’s foreign exchange restrictions). So the timing of these filings are of crucial importance for timely payments.

4.3 Regardless of whether government filings are required, do the exchange control regulations impose limits on the type and amount of fees in franchise agreements?

It would be a mistake to assume that the only requirement under foreign exchange regulations for remittance of payments is to establish that the underlying franchise transaction is “genuine.” Some countries go further and regulate the type and amount of fees that are permissible. Before their exchange control regimes were liberalized, India and South Africa both capped the amount of royalties that can be paid by a domestic franchisee to a foreign franchisor. Currently, Pakistan is probably the most prominent example of such foreign exchange limitations. In addition, for countries such as Venezuela, although in theory franchise royalties can be remitted overseas, the franchisees’ ability to do so is limited by the country’s available foreign reserve – in Venezuela, currently that essentially means no royalty payments can be made through the “official” channels.

5. Tax Related Filings

5.1 Is there a stamp tax that needs to be paid in connection with the execution of the franchise agreement? If so, how is the amount calculated?

In some jurisdictions, a tax is levied on the transaction itself. It typically takes the form of a stamp tax or stamp duty. Most countries that have such taxes only levy them on certain types of legal instruments (e.g., loan, lease, mortgage, etc.) and franchise agreements are not covered. However, in a few jurisdictions (e.g., India, Myanmar, Argentina, and

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Malaysia), franchise agreements are subject to stamp taxes. For those few jurisdictions, it is important to find out what the amount is (or the methodology of calculating the taxable base), and who should pay it, before the agreement is finalized. In addition, if the amount of the stamp tax is significant, the parties need to explore whether there are legally permissible means to avoid creating legal instruments that would be subject to the stamp tax. Given its nature, stamp tax needs to be paid up-front, and is typically a joint obligation of both the franchisor and the franchisee.

5.2 Are the franchise fees (initial and ongoing) due under the franchise agreement subject to any transactional tax (e.g., sales tax, goods and services tax, value added tax), and/or withholding tax? If so, which party (franchisor or franchisee) is legally obligated to make the tax payments to the local tax authority?

Most (but not all) countries impose one or more taxes on the fee stream under the franchise agreement. It is important to find out what those taxes are, and how much. The parties can then reach a commercial agreement as to which party will bear the economic burden of what taxes. In a few countries with protectionist laws, it is not permissible to transfer the burden of certain taxes onto the local party unless an exemption has been granted by the government authority.45

5.3 Will the franchisor be required to file tax returns with the local tax authority and pay the local corporate income tax?

In most countries, this tax filing requirement only arises if the franchisor has a “permanent establishment” in the foreign country. 46 However, a few countries (e.g., Kuwait) require franchisors to file tax returns and pay corporate income taxes on the franchise fees they receive under the franchise agreements with the local parties.

5.4 Will the franchisor be required to submit their tax residency certificates in connection with any of the tax-related filings?

To the extent that the franchisor’s home jurisdiction (the US or another jurisdiction if the franchisor has established an international franchising structure outside of the US) has a tax treaty with the franchisee’s jurisdiction, sometimes it is necessary to present a tax

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45 For example, the Philippines does not allow any gross-up provisions in franchise agreements with respect to withholding taxes, and will only allow the franchisee party to bear the burden of the VAT tax if an exemption has been granted.

46 A detailed discussion on the PE issue is obviously beyond the scope of this paper. For an in-depth discussion, see, Tao Xu, Kenneth Levinson and Ned Levitt, Tax Issues in International Franchising, IFA/IBA Joint Conference (May 2015).
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<td>residency certificate in order to claim the benefits available under such treaty. In the US, for example, obtaining such a certificate from the Internal Revenue Service could be time consuming and the franchisor should plan ahead to avoid any delays.</td>
<td>These commercial agency or distributorship laws often are drafted very broadly, and could be interpreted to cover franchise agreements. However, the inquiry should not stop at the definitional elements. For example, in certain Central America countries, US franchisors may be able to avail themselves of the protections under CAFTA-DR and avoid the coverage of these countries distributorship laws, even if the definitional elements are met.</td>
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6. Commercial Agency Filings

6.1 If the local jurisdiction has a commercial agency or distributorship law, does it cover a franchise arrangement?

These commercial agency or distributorship laws often are drafted very broadly, and could be interpreted to cover franchise agreements. However, the inquiry should not stop at the definitional elements. For example, in certain Central America countries, US franchisors may be able to avail themselves of the protections under CAFTA-DR and avoid the coverage of these countries distributorship laws, even if the definitional elements are met.

6.2 If so, is the franchise arrangement required to be filed under such commercial agency or distributorship law?

This is a particularly relevant question in the Middle East, where several countries’ commercial agency laws only apply if the agreement is registered as such. However, in KSA and Kuwait, for example, franchise agreements are explicitly required to be registered under their commercial agency laws.

7. Product Approvals and Registrations

7.1 If the franchisor will be supplying products (e.g., key ingredients, proprietary equipment, etc.) to the foreign franchisee, do these products need to be approved by the foreign government for import into the country?

The key consideration to be made is whether the product itself or, more likely, the ingredient or component used or comprised in the product is prohibited (entirely or if used above certain level) or its use is made subject to notification or authorization. If authorization is required, the time, cost and likelihood of becoming authorized should be considered in planning the supply of the relevant product in the relevant foreign market.

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47 See, e.g., Cherry J. Hearn, Michael E. Santa Maria and Herbert S. Wolfson, *International Agency Laws: Ignorance is Not Bliss*, IFA 47th Annual Legal Symposium (May 2014).
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<td><strong>7.2</strong> Do the relevant products need to be submitted for testing?</td>
<td>The technical standards, specifications and criteria that apply to a product, ingredient or component in a foreign country are likely to be different. Compliance with them may be mandatory, for the benefit of the presumption of conformity with the legal requirements or a market practice. The supplier of the products should arrange for the products to be tested against the relevant requirements before they are shipped to the market. The choice of the testing lab is also to be considered as different consequences may follow (e.g., use of accredited bodies may not be legally required but their test results of non-accredited bodies could be challenged on the ground of their competency to carry out the test).</td>
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<td><strong>7.3</strong> Will the products be subject to other regulatory oversight?</td>
<td>Product specific requirements may exist for certain products, ingredients or components. Information on the product supplied may need to be retained by the person in the jurisdiction in which the product is supplied for a specific period of time and made available for inspection by the authority or to other entities within the supply chain. Details of the information and documents that need to be kept as well as the obligations to report or update those details and verify the products' compliance with the relevant requirements need to be understood and necessary arrangement should be made to meet such requirements.</td>
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<td><strong>8.</strong> Common Filing Issues</td>
<td>Typically, timing is not of any significant concern with respect to these post-signing government filings. After all, by definition, they occur after the signing of the franchise agreement and, therefore, would not delay the agreement signing. However, there are some important exceptions – e.g., the completion of the tax-related filing may be required before the franchisee is permitted to remit any payments to the franchisor; the foreign exchange approval may be required before the franchisee is allowed to purchase any U.S. dollar (or other “hard” currency) and pay the foreign franchisor; etc. Therefore, it is always important to get a</td>
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<td>basic understanding of the timing issue. In some jurisdictions, these filings can sometimes take a significant amount of time to complete – e.g., the trademark license filing in China can take 3-6 months or even longer (although it would not affect the payment of franchise fees), while the same filing in Russia can take 1-2 months (but the completion of such a filing is required before the franchisee is able to make payments to its foreign franchisor).</td>
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<td>8.2 How much are the government fees for the filing?</td>
<td>Most countries’ government filings only require modest filing fees. However, in a few cases, the filing fees could be significant, especially in situations where a filing would entitle the parties to receive monetary benefit (e.g., lower taxes or other tax benefits). Obviously, in those situations, it would be critical to find out, as early as possible, what the amount is; which party (franchisor or franchisee) benefits from such a filing; which party should pay for it; and when such payment would be required to be made – i.e., whether it has to be paid up-front regardless of any early termination of the agreement, or whether you can do it on a pay-as-you-go basis.</td>
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<tr>
<td>8.3 Which party (franchisor or franchisee) is responsible for making this filing?</td>
<td>For each of the government filings noted above, franchisors should ascertain which party (franchisor, franchisee, or both) actually has the legal burden of making such a filing. In practice, regardless of the technical legal burden, the parties should discuss the most sensible and efficient way to handle the filing, and how the cost will be allocated.</td>
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48 For example, in Argentina, the registration of the trademark license arrangements (including franchise agreements) with its trademark office (Instituto Nacional de la Propiedad Industrial – INPI) would reduce the withholding tax rate on trademark royalties from the standard 31.5% to 28%. But the INPI registration fee is 0.25% of the projected trademark royalty amount, which could be a significant sum.
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<tr>
<td><strong>8.4</strong>  What are the consequences if the filing is not completed?</td>
<td>It should not be assumed that failure to satisfy any of the government filing requirement would be fatal to the validity of the franchise agreement itself. Some filings do affect the legal validity of the agreement; others simply do not. Some failures are clearly subject to fines and other regulatory sanctions, while others do not specify any sort of penalty for failure to register. A franchisor must have a clear understanding of the legal ramifications before it applies its own standard and determine a course of action in dealing with specific filing requirements in foreign jurisdictions.</td>
</tr>
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<td><strong>8.5</strong>  Are the documents required to be apostilled or legalized?</td>
<td>In general, if the foreign country in question is a member to the Hague/Apostille Convention, then legalization is not necessary; apostille should suffice. Otherwise, legalization (which is often time consuming given that the documents will have to be legalized at the embassy of the foreign country) will likely be necessary for documents submitted to the foreign government for filing purposes.</td>
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49 For a list of countries that are members to the Hague/Apostille Convention, please see Hague Conference on Private International Law’s status report at: https://www.hcch.net/en/instruments/conventions/status-table/?cid=41.
Appendix 2

Risk Assessment Questionnaire

Please provide the information requested below with respect to ______________ and all of its world-wide subsidiaries (collectively the “Company”). If necessary, separate risk assessment questionnaires can be completed with respect to a Company subsidiary that has significant operations. If the Company’s annual report already addresses some of these questions, please submit and cross reference that report under the appropriate question. Please complete this questionnaire to the best of your knowledge.

1. Briefly describe the Company’s business and major sources of revenue.

2. List all of the countries in which the Company engages in business either directly or indirectly through branches, subsidiaries, joint ventures, representatives, or resellers.
   a. Briefly describe the Company’s operations in each country listed above.
   b. State how significant the Company’s presence is in each country listed above in terms of number of employees and/or revenue.

3. Does the Company maintain any contracts, licenses, or other business relations with non-U.S. governments, royal families, militaries, political parties, political candidates, or state-owned or controlled entities (including sovereign wealth funds, state universities, and/or state-affiliated hospitals or research institutions) (collectively, “Government Agencies”)?
   a. If yes, in which countries are those Government Agencies located?

4. Does the Company receive any grants or other funding from Government Agencies?
   a. If yes, in which countries are those Government Agencies located?
   b. Do Government Agencies or their employees/officials require the Company to spend a portion of the grants/funding on specific vendors/contractors?

5. Briefly describe what business interactions (if any) the Company has with public international organizations such as the United Nations, the World Health Organization (WHO), the World Bank, the International Finance Corporation (IFC), the International Monetary Fund (IMF), the Asian Development Bank (ADB), or the European Bank for Reconstruction and Development (EBRD) (collectively, “PIOs”).
   a. Do Company entities receive any direct funding from PIO’s?
   b. Do Company entities act as prime or subcontractors on projects funded or sponsored by PIOs?

6. Does the Company maintain any teaming arrangements, joint ventures, or partnerships with Government Agencies or PIO’s?
7. Does the Company provide any sponsorships to FIFA, the International Olympic Committee, or other international sports organizations or their affiliates (collectively, "ISO's")?

8. Does the Company use third-party agents, joint venture partners, representatives, licensees, consultants, distributors, resellers, brokers, finders, local law firms (other than AmLaw 100 firms), local accounting firms (other than Deloitte, KPMG, PwC, Ernst & Young, Grant Thornton, BDO, or RSM), or other contractors (collectively "Intermediaries") to interact with Government Agencies in relation to permits, licenses, approvals, concessions, taxes, immigration, customs, inspections, intellectual property registrations, or any other regulatory matters?

9. Does the Company use Intermediaries to support sales to or sponsorships with Government Agencies, PIO's, or ISO's?

10. Does the Company have a readily available list of the names of its Intermediaries and their country of location? (If yes, please provide.)

11. Has the Company engaged any Intermediary specifically at the request of a Government Agency, PIO, or ISO?

12. Does the Company perform any type of anti-corruption due diligence or screening of its Intermediaries that interact with Government Agencies, PIO's, or ISO's with respect to the Company's business?

13. Does the Company have written agreements with all of its Intermediaries that interact with Government Agencies, PIO's, and ISO's with respect to the Company's business?
   a. Do those written agreements contain any anti-corruption compliance clauses?
   b. Please identify any Intermediaries who do not maintain written agreements with the Company.

14. Does the Company observe a tender bid or other process when selecting Intermediaries and other vendors? (Please describe that process.)

15. How does the Company determine appropriate levels of compensation or discounts that it provides to its Intermediaries?

16. Are there any health care professionals ("HCPs"), key opinion leaders ("KOLs"), clinical research organizations ("CRO's") and/or other individuals/organizations that are employed by or affiliated with Government Agencies (including public hospitals, universities or research institutions) and serve as advisors, consultants, contractors, employees, or vendors of the Company?50
   a. What measures does the Company observe to ensure that those HCP's, KOL's, CRO's, or other individuals/organizations do not make or influence Government Agency business or regulatory decisions in favor of the Company?

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50 This question and its subparts are primarily directed at companies that are in the life sciences/healthcare industry.
b. Does the Company perform any type of anti-corruption due diligence on those HCP’s, KOL’s, CRO’s, or other individuals/organizations that interact with Government Agencies with respect to the Company’s business?

17. Does the Company perform anti-corruption due diligence when it acquires other companies, businesses, or assets that have international exposure?

a. Have corruption, fraud, or similar concerns been raised with respect to companies, businesses, or assets that the Company has acquired?

18. Is any owner, director, employee, intern, consultant, Intermediary, vendor, or contractor of the Company a current employee, official, member, or agent of a Government Agency, PIO, or ISO?

19. Is any owner, director, employee, intern, consultant, Intermediary, vendor, or contractor of the Company an immediate relative (spouse, parent, child, or sibling) of a current employee, official, or agent of a Government Agency, PIO, or ISO?

20. Does the Company directly or indirectly provide gifts, meals, entertainment, conference passes, or travel benefits to customers or employees, officials or agents of Government Agencies, PIO’s, or ISO’s?

21. Does the Company make contributions or reimburse employees or contractors for their contributions to political campaigns or charitable organizations affiliated with employees or officials of Government Agencies, PIO’s, or ISO’s?

22. Does the Company perform periodic or other internal or external audits of its financial and/or compliance practices? (Are there any written reports?)

23. Have any audits or other assessments revealed corruption concerns, fraud, legal violations, or internal controls weaknesses?

24. Has the Company received any internal or external complaints or accusations from any person connecting the Company to bribery, corruption, kickbacks, accounting, internal controls, money laundering, terrorist financing, fraud, embezzlement, racketeering, conflicts of interest, export controls, sanctions or similar matters? (Please respond to this question with respect to those matters that have not already been investigated and/or resolved.)

25. Has any Company owner, employee, agent, partner, Intermediary, vendor, or contractor offered, promised, provided, authorized, directed, solicited, or accepted a bribe, kickback, or any other improper payment, advantage, favor, or thing of value to or from any person?

26. Does the Company maintain petty cash funds?

a. What petty cash controls and policies exist?

b. Are Company employees permitted to use petty cash in relation to gifts, meals, hospitalities, entertainment, or other benefits provided to employees, officials, or agents of Government Agencies, PIO’s, or ISO’s?
c. Does the Company expressly prohibit its employees from using petty cash in relation to gifts, meals, hospitalities, entertainment, or other benefits provided to employees, officials, or agents of Government Agencies, PIO’s, or ISO’s?

27. Does any Company entity, employee, agent, or contractor maintain any off-the-books account or side funds?

28. Please provide copies of the Company’s most current code of conduct, FCPA/anti-corruption policy, conflicts-of-interest policy, gifts and travel policy, petty cash policy, and whistleblower policy if any.
   a. What extra compliance measures if any does the Company observe when engaging in business in countries that have a reputation for corruption?

29. Does the Company train its employees and contractors on anti-corruption compliance?
   a. How frequently does such training occur?
   b. Is there a formal training schedule?
   c. Which vendor, if any, provides the training?
   d. Is training conducted on an in-person basis or via webinar?
   e. Does the Company require Intermediaries to undergo anti-corruption training?

30. Does the Company collect anti-corruption compliance certificates from its employees and contractors?

31. Does the Company maintain a telephone hotline, central e-mail address, or similar mechanism that can be used by employees and contractors for reporting anti-corruption violations and other compliance issues?
   a. Are these reporting mechanisms administered by a Company employee or a vendor?
   b. How frequently are these reporting mechanisms tested to ensure that they work and are being monitored by responsible Company employees?
   c. What efforts does the Company make to ensure that Company employees, contractors, and vendors are made aware of these reporting mechanisms? (For example, do policies and/or training slides contain information on these reporting mechanisms?)

32. Who is the Company’s official or de facto compliance officer?
   a. Does that individual have a direct reporting line to the Company’s board?
   b. Does that individual receive sufficient funding and resources from the Company to support his/her compliance role? (How has this assessment been made?)
c. Does that individual have any deputies that assist with compliance matters in other countries where the Company does business?

33. What incentives does the Company have in place to ensure that Company employees and contractors adhere to the Company's anti-corruption compliance policy? (For example, do evaluations of Company employees/contractors account for their adherence to such policy?)

34. Do you think there are other officers, managers, and employees of the Company that may have additional information relevant to the above inquiries?

This FCPA Risk Assessment Questionnaire was completed by

Name: __________________
Title: __________________
Date: _________________
Appendix 3

Sample Contractual Clauses

1.1 Training.

The Franchised Business will at all times be managed by personnel who have satisfactorily completed Franchisor’s mandatory training programs as provided in the Standards. Franchisor may offer optional training programs related to operating the Franchised Business. Franchisee will pay all Training Costs for mandatory programs and optional programs in which Franchisee participates. Franchisee will provide training required by Franchisor for personnel working at the Franchised Business.

1.2 Translations

Most written materials relating to the Franchised Business and the System, including the Agreements, the Standards, the Software, and advertising materials provided by Franchisor will be in the English language. Franchisee may, at its cost, translate such materials into another language. Franchisee will obtain Franchisor’s approval before using any translation. Franchisor will own all translated materials, and any related copyrights will be assigned to Franchisor on Franchisor’s request. Franchisee will obtain any agreements necessary from third parties to convey such rights. The English version of all translated materials will control.

1.3 Modifications to System.

Franchisee has no Ownership Interest, and will not obtain any, in any part of the System (including any modifications, derivatives or additions made by or on behalf of Franchisee or its Affiliates). Franchisee assigns, and will cause each of its employees or independent contractors who contributed to System modifications to assign, to Franchisor, in perpetuity throughout the world, all rights, title and interest (including the entire copyright and all renewals, reversions and extensions of such copyright) in and to such System modifications. Except to the extent prohibited by Legal Requirements, Franchisee waives, and will cause each of its employees or independent contractors who contributed to System modifications to waive, all rights of “droit moral” or “moral rights of authors” or any similar rights in such System modifications.

1.4 Local Advertising.

Franchisee will undertake local advertising, marketing, promotional, sales and public relations programs and activities for the Franchised Business, including preparing and using any Marketing Materials, in accordance with the Standards. Franchisee will only use signs and other Marketing Materials and the Proprietary Marks in the places, combination, arrangement and manner approved or required by Franchisor and in accordance with the Standards and Legal Requirements. Franchisee will deliver samples of Marketing Materials not provided by Franchisor and obtain prior approval from Franchisor before any use. Franchisor may withdraw its approval but will take into consideration any contracts Franchisee has related to the use of such Marketing Materials and the amount of Franchisee’s existing supply of such Marketing Materials in determining when such use will stop. If Franchisor withdraws its approval, Franchisee will stop using such Marketing Materials in accordance with Franchisor’s notice. Any Marketing Materials developed by Franchisee may be used or modified by other Franchised Businesses without compensation to Franchisee.
1.5 Inspection Rights.

Franchisee will permit Franchisor’s representatives to enter and inspect the Franchised Business at all reasonable times to confirm that Franchisee is complying with the terms of this Agreement and the Standards, and to test the equipment, food products, and supplies at the Franchised Business. In conducting such inspections, Franchisor will not unduly interfere with the operation of the Franchised Business. Franchisee will pay any costs related to such inspections, including under the Quality Assurance Program and the on-site costs of third party inspectors.

1.6 Inspection of Accounting and Records

Franchisor or its representatives (including independent auditors, attorneys or agents) shall have the right at all reasonable times to examine and copy (and to remove and return the materials to be copied from the premises on which they are located), at Franchisor’s expense, the books, records and tax returns of Franchisee. Franchisee will cooperate fully and will ensure that its employees working in relation with the Franchised Location cooperate fully with Franchisor’s representatives and any independent accountants hired by Franchisor to conduct any such inspection or audit.

1.7 Compliance with laws

Franchisee and Franchisee’s Principals agree to comply at their sole expense with all laws and regulations applicable to this Agreement and the operation of the Franchised Location. Copies of all inspection reports, warnings, certificates and ratings, issued by any governmental entity during the Term in connection with the conduct of the Franchised Location which indicate Franchisee’s failure to meet or maintain the highest governmental standards (such as, without limitation, a Grade A sanitation rating or its equivalent) or less than full compliance by Franchisee with any applicable law, rule or regulation, shall be forwarded to Franchisor by Franchisee within 5 days of Franchisee’s receipt thereof.

1.8 Compliance with anti-terrorism laws

Franchisee and Franchisee’s Principals represent, covenant and warrant to Franchisor that, to the best of their knowledge, neither Franchisee nor any of Franchisee Principals or managerial employees thereof is identified, either by name or an alias, pseudonym or nickname, on the lists of “Specially Designated Nationals” or “Blocked Persons” maintained by the US Treasury Department’s Office of Foreign Assets Control (texts currently available at www.treas.gov/offices/enforcement/ofac/). Further, Franchisee and Franchisee’s Principals represent, covenant and warrant that, to the best of their knowledge, they have not violated and agree that they will not violate any law (in effect now or which may become effective in the future) prohibiting corrupt business practices, money laundering or the aid or support of persons or entities who conspire to commit acts of terror against any person or government, including acts prohibited by the US Patriot Act, Public Law No. 107-56 (text currently available at Error! Hyperlink reference not valid.), US Executive Order 13244, or similar law. The foregoing constitute continuing representations and warranties, and Franchisee shall notify Franchisor immediately in writing of the occurrence of any event or the development of any circumstance that might render the foregoing representation and warranty false, inaccurate or misleading.
1.9 Compliance with anti-corruption laws

Franchisee agrees to, and shall cause all of its employees, consultants, contractors, subcontractors and all other persons under its supervision to, conduct all activities under this Agreement and in connection with the development, ownership, and operation of the Franchised Location in compliance with the US Foreign Corrupt Practices Act (a copy of which can be found at http://www.usdoj.gov/criminal/fraud/fcpa/), and all other comparable Anti-Corruption Laws (as defined below) or regulations in the jurisdiction where the Site is located, as well as any international conventions that outlaw bribery and corrupt practices (including for example the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions), and all Franchisor policies relating to anti-corruption.

Franchisee represents, warrants, and covenants to Franchisor that:

(a) Franchisee has not, and will not, in connection with its performance under this Agreement, or in connection with any other business transactions involving Franchisor, make, offer, give, or promise to make, offer, or give, directly or indirectly, any payment (in currency, property, or other thing of value): (i) to any Government Official (as defined below) or to an intermediary for payment to any Government Official; or (ii) to any political party if that payment or transfer would violate any applicable law. It is the intent of the parties that no payments or transfers of value be made that have the purpose or effect of public or commercial bribery, or acceptance of or acquiescence in extortion, kickbacks, or other unlawful or improper means of obtaining business. This does not, however, prohibit normal and customary business entertainment or the giving of business mementos of nominal value in connection with Franchisee’s performance under this Agreement, provided the entertainment or giving of the memento is otherwise legal under local law and does not violate or exceed Franchisor’s or the recipient’s rules, policies, or other ethical standards.

(b) If Franchisee learns or has reason to know of: (i) any payment, offer, or agreement to make a payment to a Government Official or political party for the purpose of obtaining or retaining business or securing any improper advantage for Franchisor under this Agreement or otherwise, or (ii) any other development during the Term that in any way makes inaccurate or incomplete Franchisee’s anti-corruption related representations, warranties, or certifications at any time during the Term, Franchisee will immediately advise Franchisor in writing of the knowledge or suspicion and the basis therefor.

(c) Franchisee understands that Franchisor has the right to monitor compliance with its policies, including to verify compliance with the representations in this Section. Franchisor’s right to monitor includes the right to conduct, or have its designee conduct, unannounced inspections of Franchisee’s facilities and records. Franchisee will cooperate fully with any investigation, the scope, method, nature, and duration of which is determined at the sole reasonable discretion of Franchisor.

(d) None of Franchisee’s Personnel and none of Franchisee’s Personnel’s Family Members are Government Officials. If any of Franchisee’s Personnel or their Family Members become a Government Official, Franchisee shall immediately notify Franchisor in writing.

Franchisee hereby acknowledges and agrees to these representations and agrees that at any time during the Term when requested by Franchisor, and at least annually, Franchisee will provide to Franchisor a certification in the form attached hereto as Attachment A.
If Franchisor believes, in good faith, that Franchisee has acted in any way that may subject Franchisor to liability under any Anti-Corruption Law, or has otherwise failed to comply with the terms of this Section, Franchisor may terminate this Agreement immediately upon notice to Franchisee.

Franchisee agrees that Franchisor may make full disclosure of information relating to any possible violation of any Anti-Corruption Law or any related offenses to the US government and its agencies, and to any other public or private person or entity that Franchisor determines has a legitimate need to know.
Ximena Couret

Associate
Baker McKenzie LLP
Dallas, Texas

Ximena Couret has a broad-based practice with an emphasis in international cross-border transactions. She has experience with complex global contract matters. Ximena assists clients in realizing their corporate transactional goals through the development of strategies, structuring, negotiating and implementing all types of business matters. Ximena’s practice focuses on corporate and commercial law including cross-border joint venture transactions, international mergers and acquisition, multijurisdictional corporate reorganizations, and international franchising and distribution matters involving public and private companies.
Mr. Forseth is responsible for responding to legal issues involving the development and operation of franchised hotels and regulatory compliance in both domestic and international markets for the company’s multiple lodging brands. Mr. Forseth is currently working out of Marriott’s London, England office and charged with the development and structuring of the legal processes for Marriott’s European franchise development and operations. Before joining Marriott, Mr. Forseth was in private practice, focusing on representation of franchise and other licensing and distribution companies in both domestic and international markets, and related business structuring, regulatory and relationship issues. Prior to that, Mr. Forseth was the Senior Franchise Examiner for the Maryland Division of Securities, responsible for enforcement of the Maryland Franchise Registration and Disclosure Law. Mr. Forseth is currently the Chair of the International Franchise Association Legal Legislative Committee. He is a recognized speaker on the topic of franchising and related legal issues and has published numerous papers and articles on the subject.
Tao Xu

Partner
DLA Piper LLP (US)
Reston, Virginia

Tao Xu devotes his practice to franchising and distribution matters, especially international franchising, licensing and distribution transactions. Tao counsels a broad range of clients in their international expansions, including master franchising, multi-unit licensing, area development, single-unit licensing and direct investment (both joint venture and wholly owned). Tao is particularly active in food and beverage, hospitality and leisure, and retail industries, having acted for a number of high profile US brands in their international expansion efforts. Tao is deeply involved in franchising activities in China, having both acted for a number of clients in entering the Chinese market and lobbied on behalf of the International Franchise Association in connection with the Chinese government's franchise regulations and their implementation rules.