

# Franchising in South Korea

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## I. Introduction

South Korea has a population of about 51.78 million people. Its gross domestic product (GDP) reached USD 1.64 trillion in 2020,<sup>1</sup> making it the world's tenth largest economy and one of the fastest-growing since the 1980s.<sup>2,3</sup> The country's rapid economic growth



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and innovation make it a top location for foreign investment and franchising. In 2020, South Korea posted a record-high 12.5% growth in the number of franchise brands registered with the Korean Fair Trade Commission (KFTC)—6,847—of which approximately eighty percent are in the food industry.<sup>4</sup> The KFTC expects the number of registered franchises to increase as more Koreans in their twenties and thirties turn to franchise ownership in response to worsening employment conditions during the COVID-19 pandemic.<sup>5</sup> South Korea's franchising regulations, which address unfair franchising practices and promote the protection of franchisees, create an environment conducive to franchising.

1. *South Korea*, GOV.UK FOREIGN, COMMONWEALTH & DEV. OFFICE (Oct. 2021), [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/1036623/South\\_Korea\\_economic\\_factsheet\\_2021.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1036623/South_Korea_economic_factsheet_2021.pdf) (last visited Jan. 1, 2022).

2. *GDP (current USD - Korea, Rep.)*, WORLD BANK, <https://data.worldbank.org/indicator/NY.GDP.MKTP.CD?locations=KR> (last visited July 27, 2022).

3. *Gross Domestic Product 2020*, WORLD BANK (July 1, 2022), <https://databank.worldbank.org/data/download/GDP.pdf>.

4. *Korean Youth Turn to Franchising to Beat Unemployment, Behind Half of 2021 Openings*, PULSE KOREA, (Oct 18, 2021), <https://pulsenews.co.kr/view.php?sc=30800028&year=2021&no=986380>.

5. *Id.* As of October 18, 2021, an additional 280 franchises were opened during 2021 by persons in their twenties and thirties. The sector also recorded annual sales of USD 102.7 billion as of end-June 2021.

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This article discusses the current rules in South Korea governing the sale of franchises, delves into the trademark requirements and considerations in the country, and provides an overview of the franchise relationship laws.

## II. Regulations Covering Offers and Sales of Franchises

### A. Franchise Sales Laws

In Korea, a franchisor may be a foreign or domestic entity, and, historically, there have not been any pre-offering requirements imposed on the franchisor. However, the Fair Transactions in Franchise Business Act (Franchise Act) was recently amended, effective as of November 19, 2021, such that only franchisors with experience operating at least one or more directly managed stores may offer a franchised business to others.<sup>6</sup> Thus, the franchisor is now required to have operated at least some company-owned units (either inside or outside of Korea) to offer franchises. This threshold requirement, in addition to the preparation and registration of a franchise disclosure document (FDD), is needed to engage in the sale of franchises in Korea.

The Franchise Act is a pre-sale disclosure and registration law, and the primary law governing the franchisor-franchisee relationship in Korea. This statute requires a franchisor to register an FDD and provide it to its prospective franchisees, master franchisees, and area developers.<sup>7</sup> The FDD must disclose the following broad categories of information:

1. Description of the franchisor's general status;
2. Description of the current status of the franchisor's franchise (e.g., the total number of company-owned and franchised units in operation as of the most recent fiscal year's end);
3. Description of any legal violations of the franchisor and/or its executives;
4. Description of the franchisee's obligations;
5. Description of the conditions of, and restrictions on, the franchised business operations;
6. Detailed description of the procedure and period required to commence the franchised business;
7. Description of the franchisor's support, education, and training regarding the management and operation of the franchised business; and
8. Description of the franchisor's directly managed stores.<sup>8</sup>

The Franchise Act prohibits the franchisor from accepting any franchise fees or executing the franchise agreement unless and until the franchisor

6. Fair Transactions in Franchise Business Act, Act No. 6704, May 13, 2002, *amended by* Act No. 18113, Apr. 20, 2021 (S. Kor.) [hereinafter Franchise Act].

7. *Id.* art. 7(1).

8. *Id.* art. 2(10)(a)–(h).

has provided to the prospective franchisee the registered FDD and allowed fourteen days (seven days if the prospective franchisee is advised by a franchise counsel or broker) for the prospective franchisee to review the contents of the FDD.<sup>9</sup>

The franchisor may deliver the FDD to the prospective franchisee by providing:

1. the FDD (hard copy) directly or sending it by content-certified mail to the prospective franchisee;
2. the FDD via access to the Internet; or
3. the FDD in an electronic file to the prospective franchisee by email that is capable of a “read-receipt” confirmation.<sup>10</sup>

The franchisor is also required to obtain proof of delivery from the prospective franchisee by one of the following four methods: a handwritten receipt, a certified-read receipt, an email read receipt, or website access log evidencing access by the franchisee.<sup>11</sup>

In addition to delivering the FDD, the franchisor must also prepare two additional documents to satisfy its pre-contractual disclosure obligations under the Franchise Act. First, the Franchise Act requires the franchisor to provide certain information about the ten franchised units closest to the prospective franchisee’s contemplated franchised unit.<sup>12</sup> This “Information on the Proximate Franchised Unit” disclosure must include the name of the franchisees, their addresses, and their contact information.<sup>13</sup> The franchisor must provide this information concurrently with delivery of the FDD.<sup>14</sup> Second, the Franchise Act mandates that the franchisor calculate the minimum and maximum sales revenue projections for the first year of operations of the prospective franchisee’s franchised unit, unless an exception applies.<sup>15</sup> In this “Information on the Sales Revenue Projections” disclosure, the franchisor must lay out, among other information, the methodology used to calculate the minimum/maximum sales revenue projections.<sup>16</sup> Moreover, the maximum sales projection may not be more than 1.7 times the minimum sales projection.<sup>17</sup>

The franchisor may deliver the “Information on the Sales Revenue Projections” to the prospective franchisee at any time before executing the franchise agreement.<sup>18</sup> Thus, it is possible to deliver this document separately

9. *Id.* art. 7(3).

10. *Id.* art. 7(a); Enforcement Decree of the Fair Transactions in Franchise Business Act, Presidential Decree No. 32133, art. 6(1) (Nov. 19, 2021) (S. Kor.) [hereinafter Enforcement Decree of Franchise Act].

11. *Id.*

12. *Id.* art. 7(2).

13. *Id.*

14. *Id.*

15. *Id.* art. 9(5).

16. *Id.* art. 9(3).

17. *Id.*

18. *Id.* art. 9(5).

from the FDD and the “Information on the Proximate Franchised Unit.” In practice, however, the franchisor often delivers this document to the prospective franchisee concurrently with the FDD and the “Information on the Proximate Franchised Unit.”

In 2021, the Korea Fair Trade Commission (KFTC) spearheaded several amendments to the Franchise Act and its subordinate statute—the Enforcement Decree—that further shifted the bargaining power in favor of franchisees. The most pertinent changes are discussed below.

### B. Significant Changes to the Enforcement Decree of the Franchise Act

Recently the number of franchisors selling products online or through directly managed stores has increased, and concern has arisen that this trend may lead to a decrease in the sales of franchisees. To address this concern, the Enforcement Decree of the Franchise Act was amended in 2021. The amendments require franchisors to disclose detailed information about product sales through online channels (i.e., proportion of online sales and offline sales as to the franchisor’s total domestic sales, and the proportion of online exclusive and offline exclusive products as to the total products sold by the franchisor) and directly managed stores (i.e., its name and location, average operation period, and average annual sales).<sup>19</sup> These new disclosure requirements took effect on November 19, 2021, and, as a result, any new FDD registrations and updates to registered FDDs filed after this date must include the new disclosures.

### C. Significant Recent Amendments to the Franchise Act

Several amendments to the Franchise Act itself came into force in 2021. The majority of these amendments implement the proposed measures announced by the KFTC in November 2021 and aim to address the unfair franchising practices of franchisors and promote the protection of franchisees’ interests.

Under the previous Franchise Act, it was possible for franchisors without business experience to participate in the franchised business. So, as it stood, franchisors who had not been verified by the market could offer franchises to franchisees. To address this problem, a set of amendments that came into force on November 19, 2021, requires franchisors to have at least one year of experience in operating directly managed stores (either inside or outside of Korea) before participating in the franchised business.<sup>20</sup>

However, this amendment provides exceptions for (1) franchisors who operate franchised business with permission or license under other laws and regulations; (2) franchisors who have at least one year of experience in operating a business in the same industry as the franchised business inside or outside of Korea; and (3) franchisors whose businesses have been verified by KFTC even if they have no experience in operating directly managed stores.<sup>21</sup>

19. *Id.* arts. 4(1), (10).

20. Franchise Act, *supra* note 6, art. 6-3 (1).

21. Enforcement Decree of Franchise Act, *supra* note 10, art. 5-5(2), subpara. 1-3.

#### D. Government Agency Regulation

All franchisors, foreign and domestic, must register their FDD with KFTC before signing a franchise agreement or receiving any franchise fees from the franchisee.<sup>22</sup> Besides this requirement, there are no other approvals or registrations that the franchisor must obtain in Korea to offer its franchised business to Korean franchisees.

As part of the registration process, the KFTC requires the franchisor to submit the following broad categories of information:

1. Information regarding the general status of the franchisor;
2. Information regarding the current status of the franchisor's franchises (e.g., the total number of company-owned and franchised units in operation as of the of most recent fiscal year end);
2. Information regarding any legal violation committed by the franchisor and its executives;
3. Information regarding the obligations of the franchisee;
4. Information regarding conditions of and restrictions on the business activities of the franchisee;
5. Information regarding detailed procedures and the period required in respect of the commencement of the franchised business; and
6. Information regarding support for business activities and education and training programs (and it must be specified if no plan exists for education and training); and
7. Description of the franchisor's directly managed stores.<sup>23</sup>

In support of this disclosure, the franchisor must also submit the following documents during the process of registering the FDD:

1. Certificate of good standing (or equivalent) of the franchisor;
2. Financial statements of the franchisor for the last three years;
3. Data regarding the sales revenue of the franchisor that is attributable to the franchised business (in case the franchisor has multiple lines of businesses);
4. Trademark license agreements (in case the franchisor is not the trademark owner but a licensee); and
5. Template form franchise agreement.<sup>24</sup>

As to the form that the FDD must take, the KFTC issues a standard FDD template.<sup>25</sup> All franchisors are obligated to prepare their FDDs in accordance with this prescribed template.<sup>26</sup> And, while no express provision

22. *Id.* art. 7-3.

23. *Id.* art. 2(10)(a)–(h).

24. *Id.* art. 5-2(2), (3).

25. Franchise Act, *supra* note 6, art. 7(4).

26. *Id.*

in the Franchise Act requires the franchisor to draft the FDD in a certain language, the general practice of the KFTC is to only accept Korean-language versions of the FDD for registration. Thus, the franchisor must prepare the FDD in Korean and translate all ancillary documents into Korean when filing for registration.

A franchisor that fails to register their FDD may face liability under the Franchise Act. First, the franchisor must refund any franchise fees collected if the franchisee makes a request for refund within *four months* from the date of executing the franchise agreement. If a refund is due, the franchisor must make the refund within one month from the date of the franchisee's request.<sup>27</sup> Second, the KFTC may order a corrective measure, which would include ordering the franchisor to register or carry out the disclosure of the FDD. The four possible corrective measures include the following: 1) administrative warning; 2) recommendation to correct; 3) corrective order; and 4) administrative fine. The administrative warning is the least severe corrective measure, and the administrative fine is the most severe.<sup>28</sup>

With respect to the administrative fine, the KFTC may impose a fine of up to two percent of the total sales of the franchisor to the specific franchisee in Korea for the duration in which the franchisor was not in compliance.<sup>29</sup> In determining the amount of the administrative fine, the Franchise Act stipulates that the KFTC should consider the nature, severity, duration, and frequency of the infraction, as well as the profits that the franchisor derived as a result of its non-compliance.<sup>30</sup> Alternatively, in case the franchisor's total sales during the period of non-compliance is difficult to calculate, the Franchise Act provides that an administrative fine of up to KRW 500 million (approx. USD 480,000) may be imposed.<sup>31</sup>

Failure to comply with any of these three provisions does not lead to automatic rescission or cancellation of the franchise agreement. However, the franchisee may bring a lawsuit for damages and cancel or rescind the franchise agreement under general principles of tort or contract law in accordance with the Korean Civil Code.<sup>32</sup> If the franchisee is not adequately compensated through cancelling or rescinding the franchise agreement, the franchisee may be entitled to additional damages.<sup>33</sup>

The KFTC may investigate a violation of the Franchise Act for up to three years from the termination of a transaction.<sup>34</sup> However, if any person reports a violation within that three year period, the KFTC may investigate the matter even if the three-year period has elapsed after such termination.<sup>35</sup> Further, if the KFTC commenced its investigation upon a person's

27. *Id.* art. 10.

28. *Id.* arts. 33(1), 34(1), 35(1).

29. *Id.* art. 35(1); Enforcement Decree of Franchise Act, *supra* note 10, art. 34 (1).

30. Franchise Act, *supra* note 6, art. 35(2).

31. *Id.* art. 35 (1), (2); Enforcement Decree of Franchise Act, *supra* note 10, art. (34).

32. Civil Act art. 109-110, *amended by* Act No. 17503, Oct. 20, 2020 (S. Kor).

33. Franchise Act art. 37(2); Civil Act art. 741, 750 (S. Kor.).

34. Franchise Act, *supra* note 6, art. 32(1).

35. *Id.* arts. 32(1), 32-3(1).

report of a violation, the KFTC may impose punishment up to three years after the date of such report.<sup>36</sup> When commencing investigation without any report filing, the KFTC may impose punishment up to three years after its investigation.<sup>37</sup>

The Franchise Act also includes penal provisions that provide for imprisonment of no more than two years or a criminal fine not exceeding KRW 50 million (approx. USD 47,000) for failure to provide a registered FDD.<sup>38</sup>

### III. Foreign Exchange Controls

#### A. *Limits on Currency Conversion*

Korea does regulate foreign exchange. However, Korea has liberalized its foreign exchange controls, and thus, generally no currency control restrictions limit the flow of funds into or out of Korea. To that end, a franchisee is not required to make any filings with any government agencies, including the Bank of Korea, before making remitting payments to the foreign franchisor.

However, under exigent circumstances, foreign exchange transactions could be temporarily suspended or restricted if such measures are deemed necessary on account of natural calamities, war, grave and sudden changes in domestic and foreign economic conditions, or other similar situations.<sup>39</sup>

#### B. *Government Filing Requirements*

Besides those discussed earlier, no other franchise filing requirements in Korea must be satisfied before the franchisee is permitted to make payments to a foreign franchisor.

### IV. Taxes

#### A. *Royalties*

Under the applicable tax treaty between South Korea and the United States, the remittance of franchise fees and royalties by a Korean company is subject to a fifteen percent withholding tax and a ten percent surcharge on the withholding tax amount, bringing the total effective rate of these taxes to 16.5%.<sup>40</sup> There are no alternative fee structures in common use that would reduce or eliminate withholding taxes on payments from South Korea to the United States.

The current minimum withholding tax rates based on the Korea–U.S. treaty are ten or fifteen percent for dividends; twelve percent for interest;

36. *Id.* art. 32(2).

37. *Id.*

38. *Id.* art. 41(3).

39. Foreign Exchange Transactions Act, Act No. 6277, Oct. 23, 2000, *amended by* Act No.14525, Jan. 17, 2017 (S. Kor.) [hereinafter Foreign Exchange Act].

40. Tax Convention with The Republic of Korea, Aug. 14, 1976, Korea–U.S. Tax Treaty, art. 14(1).

and fifteen percent for royalties (ten percent for copyright royalties). In addition, a ten percent surcharge will apply to the withholding tax rates.<sup>41</sup>

### B. Service Fees

No stamp tax must be paid to execute the franchise agreement (or any other types of agreement) in Korea.

### C. Double Taxation Treaties

Corporate income tax is progressive and can be broken down as follows:<sup>42</sup>

Taxable Income	Tax Rate (Including Local Surtax)
~ KRW 200 Million (approx. USD 180,000)	11%
KRW 200 Million ~ KRW 20 Billion (approx. USD 180,000 ~ USD 18,000,000)	22%
KRW 20 Billion ~ KRW 300 Billion (approx. USD 18,000,000 ~ USD 270,000,000)	24.2%
KRW 300 Billion or Higher (approx. USD 270,000,00 or higher)	27.5%

Corporations that are residents for tax purposes are taxed on their worldwide income.<sup>43</sup> Non-resident corporations with a permanent establishment in Korea are only taxed on their Korea-sourced income.<sup>44</sup> Non-resident corporations without a permanent establishment in Korea are generally taxed through a withholding tax on each separate item of income that is subject to withholding.<sup>45</sup>

Thus, a non-resident franchisor without a local presence—that is, a franchisor that has or is deemed to have no “permanent establishment” in Korea—is only subject to the withholding tax described earlier.

## V. Franchise Relationship Laws

### A. Defaults, Termination, and Nonrenewal

The Franchise Act regulates not only pre-sale disclosure, but also the relationship between the franchisor and the franchisee. In addition to the registration and disclosure requirements described in Section II.A previously, there are a number of other key requirements.

41. *Id.* arts. 12, 14(1), (2); *see also id.* art. 1(1).

42. Corporate Tax Act, Act No. 5581, art. 55(1), Dec. 28, 1998, *amended by* Act No. 16833, Dec. 31, 2019 (S. Kor.) [hereinafter Corporate Tax Act].

43. *Id.* arts. 4, 14, 15, 19.

44. *Id.* arts. 91, 97.

45. *Id.* art. 98.



First, The Franchise Act regulates termination and non-renewal of franchise agreements. Under the Franchise Act, if a franchisee requests to renew a franchise agreement during the 90 to 180 day period before expiration of such agreement, a franchisor may not deny such request unless the franchisee has been in breach of a payment obligation or if the franchisee rejects common obligations and duties accepted by other franchisees.<sup>46</sup> However, the franchisee's right to request renewal of the franchise agreement exists for a period of ten years, which includes both the initial term and any renewal terms thereafter of the franchise agreement.<sup>47</sup>

Second, franchisors are prohibited from forcing franchisees to remodel without just cause. If a franchisor either recommends or demands remodeling, the franchisor may be required to bear up to twenty percent of the remodeling costs and up to forty percent of the remodeling costs if the franchisee is required to relocate or expand.<sup>48</sup>

Third, franchisors are prohibited from unfairly restricting franchisees' business hours.<sup>49</sup> Franchisors will also be prohibited from requiring franchisees to engage in late-night operations (1:00 am to 6:00 am) if the revenue from such operations—for the three-month period immediately preceding the month in which a franchisee requests a reduction in the opening hours—is significantly lower than the cost of operating in the extended hours.<sup>50</sup>

Finally, franchisors must explicitly state the franchise territory in their franchise agreements and are prohibited from establishing the "same type of business" as the franchisees within such protected franchise territory.<sup>51</sup> Specifically, during the term of the franchise agreement, a franchisor cannot establish a company-owned (including affiliate-owned) franchise of the "same type of business" within the protected franchise territory.<sup>52</sup> The "same type of business" is determined case-by-case, taking into account, for instance, the target class, territorial boundary, population boundary, types of products sold, and business manner and method.<sup>53</sup>

Further, in Korea, the Commercial Act governs commercial agency, and the Fair Agency Transactions Act is the principal statute regulating distribution relationships.<sup>54</sup> Neither of these two statutes specially governs franchise arrangements directly. However, the Commercial Act may be relevant to franchise relationships. Under the Commercial Act, if an agency agreement terminates or expires, the agent may seek compensation from the principal under certain limited circumstances.<sup>55</sup> Specifically, Article 92-2 of the

46. Franchise Act, *supra* note 6, art. 13(1).

47. *Id.* art. 13(2).

48. *Id.* art. 12-2.

49. *Id.* art. 12-3(1).

50. *Id.* art. 12-3(2), subpara. 1; Enforcement Decree of Franchise Act, *supra* note 11, art. 13(3).

51. Franchise Act, *supra* note 6, art. 12-4.

52. *Id.* art. 12-4(3).

53. *Id.*

54. Commerce Act, art. 92-3, *amended by* Act No.19362, June 6, 2020 (S. Kor.) [hereinafter Commercial Act]; Fair Agency Transactions Act, *amended by* Act No. 18570, Dec. 7, 2021.

55. Commercial Act, *supra* note 54, art. 92-2.

Commercial Act provides that an agent may claim “reasonable” compensation from the principal if the principal (i) obtains new customers or (ii) its business transactions increased substantially through the agent’s activities during the term of the agency agreement, and thereby, the principal gains profits even after the agency agreement comes to an end.<sup>56</sup>

The right of an agent to seek compensation only exists if the agency agreement is terminated through no fault attributable to the agent.<sup>57</sup> If the agency agreement naturally expires (or terminates without any breach by the agent), then the agent may have a right to claim compensation. However, the agent must make the claim for compensation within six months from the date of termination/expiration of the agency agreement.<sup>58</sup> In the event that any compensation is due, the compensation amount may not exceed the average annual remuneration of the agent for a period of five years before the end of the agency agreement.<sup>59</sup>

In general, Article 92-2 is interpreted as a mandatory provision. Therefore, an agent’s waiver of this right (or the agreement to waive this right between the parties) before termination or expiry of the agreement is invalid. But, according to Korean court precedents, if the governing law of the agreement is foreign law under which such waiver is permissible, then such waiver is enforceable in Korea, and, thus, the agent cannot seek compensation from the principal.<sup>60</sup>

So far, no case precedents (or KFTC rulings) exist in which the Korean courts have expanded the application of Article 92-2 to a franchise arrangement. Given that some legal commentators are arguing for its application to franchising, however, it is important to flag this issue so that appropriate measures may be taken to preclude the application of Article 92-2 of the Commercial Act and, thus, avoid having to compensate the franchisee upon expiration or earlier termination of the franchise agreement.<sup>61</sup>

### B. *Laws Regulating Unfair Contract Terms*

The Franchise Act is a *lex specialis* for franchising and is derived from the Korean unfair trade law, the Monopoly Regulation and Fair Trade Act (MRFTA). The Franchise Act outlines certain franchisor conduct that could be deemed an “unfair trade practice.” Such practices are prohibited because it would undermine the fair trade in carrying out the franchised business. The prohibited conduct is as follows:

1. “Unfair” refusal to deal:
  - (A) Refusal to provide support (e.g., products, services, etc.);

56. *Id.*

57. *Id.* art. 92-2(1).

58. *Id.* art. 92-2 (2).

59. *Id.*

60. See Seoul High Court [Seoul High Ct.], 2004Na14040, Jan. 14, 2005 (S. Kor.).

61. Young Hong Choi, *A Characteristics of Commercial Agent’s Entitlement of Indemnity*, 36 ANAM L. REV. 575 (2019).

- (B) Refusal to renew the franchise agreement without just cause; or
  - (C) Unjust termination of the franchise agreement.
2. “Unfair” restraint or restriction:
- (A) Restrictions on pricing;
  - (B) Restrictions on the parties with whom the franchisee may commercially transact;
  - (C) Restrictions on the sale of products or services by the franchisee;
  - (D) Coercion of observance of business territory; or
  - (E) Other “unfair” restrictions on business activities.
3. Abuse of bargaining power:
- (A) Requiring the franchisee to purchase products, services, or other goods in excess of what is necessary to engage in the franchised business;
  - (B) Unfairly demanding that the franchisee provide economic profit or placing a burden on the franchisee for certain expenses;
  - (C) Establishing or amending provisions of the franchise agreement having the effect of placing the franchisee in an “unfair” position;
  - (D) Interfering with the management of the franchisee’s operations;
  - (E) Establishing mandatory sales targets; or
  - (F) Imposing other similar disadvantages on the franchisee.
4. “Unfair” imposition of compensation for damages:
- (A) Imposing or stipulating an excessive amount of liquidated damages; or
  - (B) Transferring to the franchisee the franchisor’s liability to the customers.
5. Any other activity which may seem to obstruct fair trade, such as causing harm to the franchisee by unfairly inducing the franchisee of a competing franchisor to transact with the franchisor.<sup>62</sup>

Any contract term that would result in any of the above conduct would be deemed “unfair.” However, the determination of whether a practice is deemed “unfair” will be determined based on a rule of reason and, thus, would be heavily fact-dependent.

Meanwhile, as to the matters not specifically regulated by the Franchise Act, the general provisions of the MRFTA would apply to regulate the franchise arrangement.

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62. Franchise Act, *supra* note 6, art. 12; Enforcement Decree of Franchise Act, *supra* note 10, art. 13(1), Ex. 2.

## VI. Trademark Requirements and Licensing Considerations

### A. Trademark Registration

Korea is a “first-to-file” jurisdiction.<sup>63</sup> Any of the following marks can be registered as a trademark when used on goods or services related to the business of a person who conducts business activities, such as producing, processing, distributing, certifying or selling such goods, to distinguish them from the goods of others:

1. a sign, character, figure, sound, smell, three-dimensional shape, color, hologram, motion, emblem, or any combination of these; or
2. things that can be visually recognized other than the above-mentioned things.<sup>64</sup>

A trademark, collective mark, business emblem, or geographical indication and certification mark can be registered and protected in Korea as well.<sup>65</sup> However, a trademark cannot be registered if it is deemed to be identical or confusingly similar to a national flag, titles or marks of well-known international organizations, such as the International Olympic Committee.<sup>66</sup>

In addition, when filing a trademark application, the trademark applicant is required to designate goods or services according to the NICE Classification (thirty-four classes of goods and eleven classes of services under the Eleventh Edition of the NICE Classification).<sup>67</sup>

In principle, the Trademark Act does not protect unregistered marks.<sup>68</sup> So it is advisable for franchisors to register their trademarks when seeking to enter into franchise arrangements in Korea.

### B. Trademark License Registration

It is not mandatory for the trademark license to be registered (i.e., recorded) with the Korean trademark office—the Korean Intellectual Property Office (KIPO).<sup>69</sup> However, if recorded, the trademark license becomes effective against any third party who subsequently acquires the trademark right or an exclusive license.<sup>70</sup>

63. Trademark Act, Act No. 14033, Feb. 29, 2016, *amended by* Act No. 17728, Dec. 22, 2020 (S. Kor.) [hereinafter Trademark Act], art. 35(1).

64. *Id.* art. 2(1).

65. *Id.* arts. 2 (1), (3), (8), (9); *id.* art. 3.

66. *Id.* art. 34(1).

67. *Id.* art. 36(1), subpara. 4. The NICE Agreement establishes a classification of goods and services for the purposes of registering trademarks and service marks (the NICE Classification). The trademark offices of Contracting States must indicate, in official documents and publications in connection with each registration, the numbers of the classes of the Classification to which the goods or services for which the mark is registered belong. The Republic of Korea is one of Contracting States and thus needs to be compliant with the above requirements.

68. See KOREAN INTELLECTUAL PROP. OFF., TRADEMARKS (June 15, 2022), [https://www.kipo.go.kr/en/HtmlApp?c=30103&catmenu=ek04\\_02\\_01](https://www.kipo.go.kr/en/HtmlApp?c=30103&catmenu=ek04_02_01).

69. *Id.*

70. *Id.* art. 100.

To record the license (exclusive or non-exclusive), the trademark licensee must prepare a short-form license agreement in the format prescribed by KIPO that requires the following information:

1. Geographic scope of the trademark license;
2. Duration of the trademark license; and
3. Scope of the trademark license (e.g., license to make, use, transfer, lease, offer for sale).<sup>71</sup>

It is not necessary (and usually not advisable) for the exclusive licensee to submit the actual license agreement to KIPO for purposes of recordation.

## VII. Competition Laws

The MRFTA is the primary competition (antitrust) statute in Korea, and it applies to franchise relationships.<sup>72</sup>

Post-term covenants against competition are enforceable in Korea. If challenged, however, the Korean courts employ a totality of the circumstances approach to determine the reasonableness of such post-term covenants. In this analysis, the Korean courts consider various factors: (1) whether there is legitimate business interest to protect; (2) whether there is consideration exchanged for the non-competition obligations; (3) whether the scope of competing business is narrowly tailored; and (4) whether the geographic and temporal scope is reasonable given the underlying facts. Based upon these factors, the Korean courts may enforce, modify, or invalidate the non-compete agreements (or covenants within agreements).<sup>73</sup>

It is common practice for franchisors in Korea to include post-term covenants against competition that covers a period of one year following termination/expiration of the franchise relationship.

## VIII. Employment Laws

Some scholars argue that the joint employer doctrine might be applied to the franchise business in Korea as it sometimes is in the United States.<sup>74</sup> However, there has been no case to date involving workers in the franchisees' units in Korea where a franchisor has been deemed as a "joint employer" with its franchisees. Therefore, at this time, it is safe to say that franchisors are not seen as "joint employers" of the franchisees' workers.

71. See KOREAN INTELLECTUAL PROP. OFF., *supra* note 68.

72. Franchise Act, *supra* note 6, art. 38.

73. See Seoul District Court [Seoul Dist. Ct.], 2010Kahap1692, Dec. 2, 2010 (S. Kor.).

74. Hyunhee Park, *United States Joint Employer Doctrine and What Are the Implications for Korea Labor Law*, 23 SOC'Y OF LABOR LAW THEORY & PROF. LABOR LAW F. \_\_\_\_ (2018).

## IX. Privacy Laws

### A. Applicable Privacy Laws

While no industry-specific privacy laws specific to the franchise relationship exist, the general law of privacy—the Personal Information Protection Act (PIPA)—impacts franchising in South Korea.<sup>75</sup>

### B. Effect on Franchising

Under PIPA, information that is categorized as “personal information” is regulated. “Personal information” is any information that is related to a living person, including information that can be used to identify the living person by itself or through combination with other information, notwithstanding that such other information may not be “personal information.”<sup>76</sup>

In principle, PIPA requires individuals to receive certain information regarding the data collector and processor (e.g., information regarding the franchisor or franchisee and the purpose of acquisition/collection/use of “personal information”) and provide their consent.<sup>77</sup> In the case of a franchisee collecting data in a franchise system, the franchisee will be the data collector and processor of the “personal information,” and, thus, the franchisee must comply with the data privacy requirements under PIPA. Moreover, to transmit the “personal information” to the franchisor, who is considered as a third party, the franchisee must obtain a separate consent from the customers.<sup>78</sup>

## X. Governing Law and Dispute Resolution

### A. Governing Law

There is no requirement for franchise documents to be governed by local laws. In fact, Korean courts readily enforce foreign governing laws. However, some compulsory provisions of Korean law apply irrespective of the governing law as agreed by the parties in their contract.<sup>79</sup> Although not explicitly provided under the Supreme Court’s decisions on whether the provisions of the Franchise Act constitute compulsory provisions, many scholars view certain provisions of the Franchise Act as compulsory, and, thus, even if the franchise documents are governed by foreign laws, these documents must comply with the compulsory provisions of the Franchise Act. These compulsory provisions relate to requirements on renewal, termination, cost-contribution to remodeling or renovation, and business territory.

75. Personal Information Protection Act, Act No. 11690, Mar. 23, 2013, *amended by* No. 16930, Feb. 4, 2020 (S. Kor.) [hereinafter PIPA].

76. *Id.* art. 2(1).

77. *Id.* art. 15.

78. *Id.* arts. 15, 17.

79. Act on Private International Law, Article 7 *amended by* Act No. 13759, Jan. 19, 2016.

### B. *Injunctive Relief*

The law provides for preliminary injunctive relief upon showing of (a) an actual or threatened harm or dispute, (b) a likelihood of success, and (c) a possibility of significant damages if the injunctive remedy were not granted.<sup>80</sup> Here, the grounds for seeking such preliminary injunctive relief would include, among others, the need to protect the brand from damage or to prevent the misuse of critical confidential information. The franchisor must also be prepared to post bond to enforce a preliminary injunction order, if granted by the Korean courts.<sup>81</sup>

### C. *Foreign Judgment*

Foreign judgments are not automatically enforceable in Korea. A foreign judgment will be acknowledged as valid and enforceable in Korea if it satisfies the requirements discussed below.

First, the foreign court that rendered the judgment, of which recognition and enforcement is sought, had proper jurisdiction over the case according to the principle of international jurisdiction under the Korean Civil Procedure Act or international treaties.<sup>82</sup> Next, the party against whom the foreign judgment is sought has received, pursuant to a lawful method, a service of summons with sufficient time to defend the lawsuit or, alternatively, has responded to the lawsuit voluntarily.<sup>83</sup> Third, the foreign judgment is final and conclusive.<sup>84</sup> Fourth, the recognition and enforcement of the foreign judgment is not contrary to the public policy of Korea.<sup>85</sup> Finally, the foreign country from which recognition and enforcement of the judgment is sought reciprocally recognizes and enforces Korean courts' judgments in the equivalent manner as Korean courts.<sup>86</sup>

It is worth noting that Korean law recognizes only final and conclusive foreign judgments.<sup>87</sup> Accordingly, interim relief obtained in a foreign court will not be enforceable in Korea.<sup>88</sup>

### D. *Arbitration*

The Arbitration Act and its subordinate statutes govern arbitration in Korea.<sup>89</sup> Moreover, the Korean Commercial Arbitration Board (KCAB) is the principal arbitration forum for arbitrating disputes (located in Seoul and Busan).

80. Civil Execution Act, Act No. 7358, art. 300, Jan. 27, 2005, *amended by* No.13952, Feb. 3, 2016 (S. Kor.).

81. *Id.* art. 280; Civil Procedure Act, art. 301, Act No. 6626, Jan. 26, 2002, *amended by* No. 17689, Dec. 22, 2020.

82. Civil Procedure Act, art. 217(1), *amended by* No. 17689, Dec. 22, 2020.

83. *Id.* art. 217(1), subpara. 2.

84. *Id.* art. 217(1).

85. *Id.* art. 217(1), subpara. 3.

86. *Id.* art. 217(1), subpara. 4.

87. *Id.* art. 217(1).

88. *Id.*

89. Arbitration Act, art. 21, Act No. 6465, Apr. 7, 2001, *amended by* No. 16918, Feb. 4, 2020.

Parties can refer their disputes to arbitration at a venue situated outside the country, and the Korean courts readily enforce foreign arbitral awards.<sup>90</sup> Further, enforcement of foreign arbitral awards is not difficult. Korea is a signatory to the New York Convention, subject to two reservations. First, Korea will apply the Convention only to recognition and enforcement of awards made in the territory of another contracting State.<sup>91</sup> Second, Korea will apply the Convention only to differences arising out of legal relationships, whether contractual or not, that are considered commercial under the national law.<sup>92</sup>

In contrast to a foreign judgment, foreign arbitral awards coming from a member state of the New York Convention, and satisfying the reservation requirements, are recognized and enforced by Korean courts without further review.<sup>93</sup>

## XI. South Korea Case Law

Few cases in South Korea have involved franchises and interpretation of the Franchise Act. However, in 2020, the Supreme Court considered a franchise case.<sup>94</sup>

In the case, a franchisor refused to renew a franchise agreement with a franchisee who had operated a franchised restaurant for twelve years. The franchisor refused because the franchisee used slightly different cooking methods, and thus failed to follow faithfully the franchisor's operational manual. Ultimately, the Supreme Court held in favor of the franchisee. Under the Franchise Act, a franchisee's right to request renewal of a franchise agreement may be exercised only when the total period of the franchise agreement, including its initial period, does not exceed ten years. Therefore, in principle, if a franchise agreement exceeds ten years, the franchisor can, at its discretion, freely decide whether to accept the franchisee's renewal request. Nonetheless, the court found that the franchisor unfairly abused its superior position in this transaction by refusing the renewal, contrary to the principles of good faith. The Court considered various factors such as the background and purpose of entering into the franchise agreement, the progress of the contractual relationship, and the unique nature of the franchise agreement in general.

This case is noteworthy because it demonstrates that, notwithstanding the renewal provision of Franchise Act above, a franchisor can be barred from refusing a franchisee's right to request a renewal when there is an abuse of bargaining power.

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90. *Id.*

91. UN Conference on International Commercial Arbitration, Convention on the Recognition and Enforcement of Foreign Arbitral Awards, art. I, June 7, 1959, No. 4739.

92. *Id.* art. 1(3).

93. *Id.* art. 39.

94. See Supreme Court, 2019Da289495, July 23, 2020 (S. Kor.).



## **XII. Conclusion**

South Korea remains a prime market for foreign investment, especially franchising. However, as noted, any prospective franchisor must consider important legal and business considerations before entering the market. Given the constantly evolving forces affecting franchising (from regulatory requirements from the KFTC, to privacy laws, to franchise-specific legislation), a great deal of initial (and continued) diligence about the legal framework in South Korea that affects franchising must be conducted.

