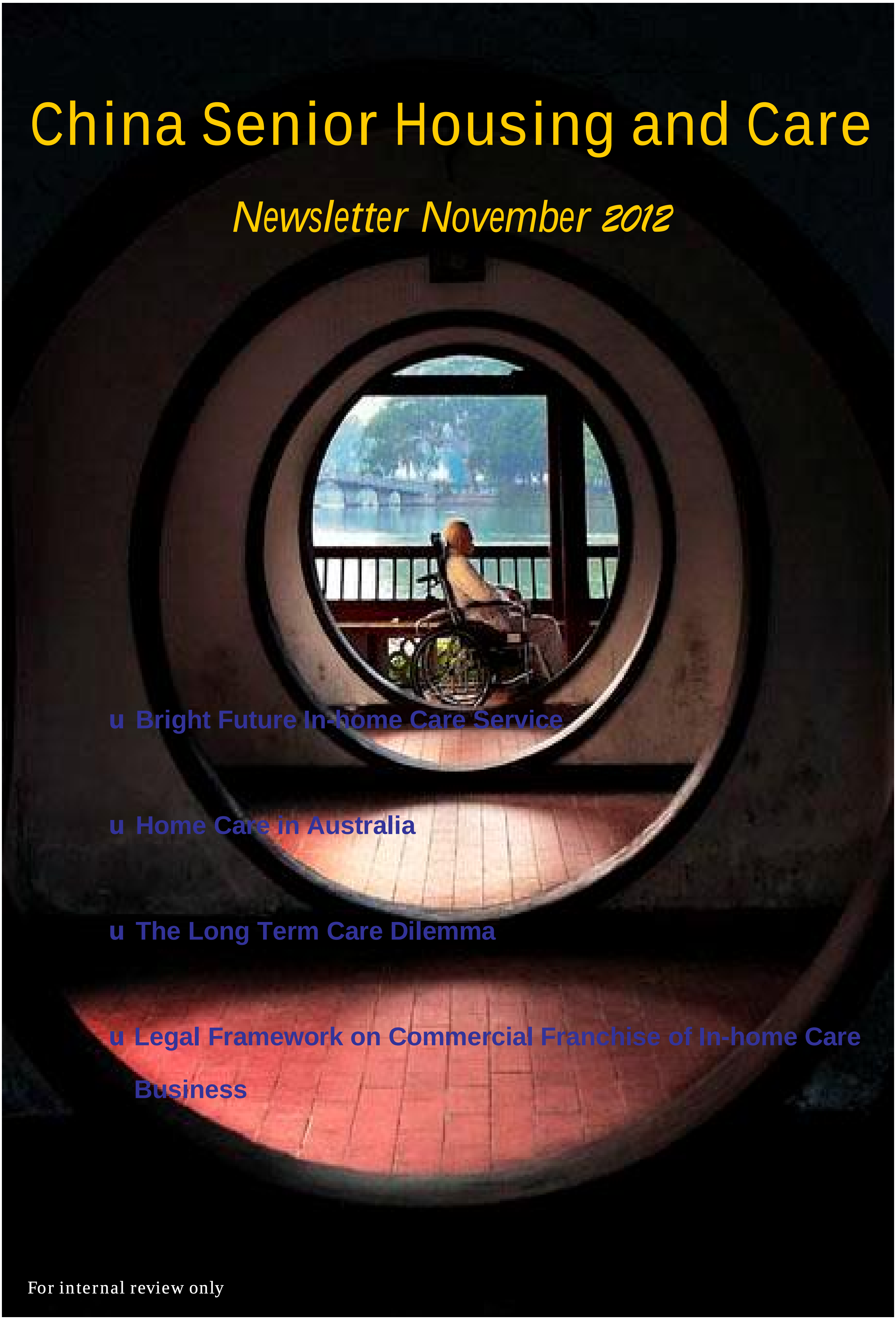
China Senior Housing and Care

Newsletter November 2012



- **Bright Future In-home Care Service**
- **Home Care in Australia**
- **The Long Term Care Dilemma**
- **Legal Framework on Commercial Franchise of In-home Care Business**

For internal review only

Editorial Notes

Where are the competitors?

I was attending senior living conferences during this October and November, meeting acquaintance and making new friends. I must admit a place with more domestic practitioners are more excited, as after all, this is a Chinese senior care market, and, many domestic players have already explored here in the industry for, maybe, more than 4~5 years. Some of them are maybe struggling with their unprofitability, some seeking new location for another facility, or, some maybe imaging a bigger picture in exploring nation-wide domination, the common position for them is they are still not yet facing real competitors. Some are expecting competition in the market, me too—definitely we will not keep waiting too long.

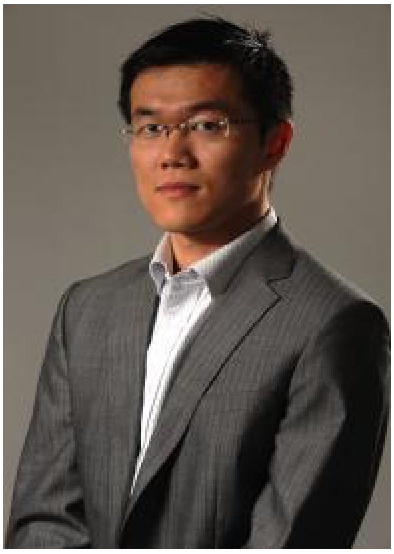
One segment of the senior care market will face more competition, although according to the national "9073" strategy, it may cover potentially 90% of the Chinese seniors. You know what I' m talking about—yes—it's in-home care service, which seems to have the lowest entry threshold in the senior care industry. We can see many brands have emerged in recent years, and there will be more. Therefore, it is necessary to take more time on the in-home care business model in this edition.

Also interesting thing is, thanks to the economic crises in many western countries, people tend to choose aging-in-place instead of moving to facilities. These countries may have introduced incentive policies and developed a full-fledged market and regulatory environment for decades, and their experiences are really worth learning.

In this edition, we invite our guest Paul Goldenberg, who has practiced in the US assisted living for 40 years, to tell about his journey in the senior care industry, in a series of stories from various angles. I like what he says, we may have different culture, regulation, or economic situation, but the story happens in every family is the same. Yes, emotion is universal. And, we are also happy to have my friend John Corcoron, who is a lawyer of RUSSELL KENNEDY PTY LTD, to introduce what happens in Australia in the in-home care segment with his colleagues.

See you early next year—we'll put more focus on CCRCs-type of senior living communities.

——*Michael Qu*



Michael Qu

Chief Editor
Attorney at Law

T: +86 (21) 8866151*152
F: +86 (21) 58871151
quqin@co-effort.com

Bright Future in In-home Care Service

Written by Michael Qu

In this Article we will see the current status and the future of China's in-home care service business, hoping to find where opportunity lies to…

- ***Aging-in-place is a global retirement living trend***
- ***Long ways to go in establishing a systematic regulatory environment***
- ***The government is to more suitably position itself***
- ***Urging for Long Term Care Insurance***
- ***A hybrid of senior care and medical treatment is under exploring***
- ***To tackle the workforce scarcity***
- ***Technology bringing about the breakthrough***
- ***Conclusion***

At the anniversary of China's implementation of 12th Five-year Plan on the Development of Senior Care industry, we focus again on the aging-in-place retirement model, which is encouraged by the government and has drawn much attention from foreign investors. From the investment cases, we can see several high-profile ones such as the first WOFE of its kind—Econ-SCA Health Management Co Ltd established in Shanghai at the end of last year, backed by Sweden and Singapore brands; and Right at Home International, Inc., a US franchisor of in-home senior care, signed off master franchise license agreement with an its Beijing Partner, etc. In fact, if taking housekeeping providers into account, who actually contribute much of the in-home care service in the marketplace, the market scale is by no means small. How to regulate and guide the in-home senior care industry in order to forge a health environment, remains to be a topic worthy of thoughts.

Aging-in-place is a global retirement living trend

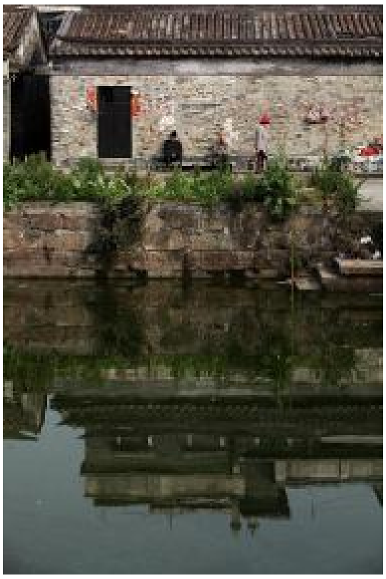
The most interesting thing is aging-in-place has in recent years become a global trend for senior living. Taking the US as an example, multigenerational households have surged back up to about 17% of the senior population from the bottom of 12% in 1980s, according to Pew Research studies. Apart from inevitably the main reason of economic recession, many has acknowledged cultural shifts—mean some groups are more comfortable having multiple generations living together—could be another big concern.

Observe from the development of senior care industry in these western countries, on one hand, countries like the US and Japan have all become aging society as of 1980s, and business models and regulatory environment has since long ago been established, experiences in in-home care service from these countries are really worth leaning; while on the other hand, countries like the US and Australia are also struggling on how to attract more people choosing aging-in-place. Therefore, it is a global rather than domestic topic for all of us to explore on how to invest a suitable in-home care solution that can benefit both the seniors and government.

Long ways to go in establishing a systematic regulatory environment

Currently, entrance threshold for in-home care service is low, and no effective administration and service guidance from government is put in place, whether it's for profitable or not-for-profit business. Although many cities are aiming at 100% qualified caregivers in the workplace and have increase investment in training nursing staff, given the fact standardized service protocols in the industry are still in lack, and many unqualified caregivers are employed by housekeeper providers to deliver care service to seniors, operational risks remain to be uncontrollable in many ways, either to the seniors or the providers themselves.

As for incentive policies to the industry, except for more funding from government in the area such as purchasing more private service, providing more seniors with various in-home care services, no more specific or active policy is found. As a matter of fact, experience from



Singapore or Japan can be referred to, such as the government to construct more "multi-generation" dwelling and attract families to live there with incentives of preferential price, arrangement or mortgage rate; or cutting some taxation for qualified children who live together with their elderly parents. While on the systematic construction, we think imminent priority shall be on the construction of accreditation standards for different levels of in-home care service, regulating and guiding fee charge mechanism and introducing industrial standards in order to unify the service standard for the whole industry.

The government is to more suitably position itself

In a poll conducted by the China Youth Daily, 86.4 percent of 8,476 respondents said they want more government investment in rehabilitation and care for senior citizens over the next decade. In the survey, more than half of respondents said high pressure in the workplace and living costs have made it difficult to take care of their own parents. About 39.7 percent of the people surveyed said it is not feasible for them to move their parents closer to home to look after them, while 36.4 percent said they believe nursing homes are not currently suitable for their parents. This survey shows aging-in-place, in many people's view, will be the best suitable in China, while the government will definitely take more responsibility in the process.

According to Shanghai Municipal Civil Affairs Bureau, mainly available in-home care services from the government include daily-care, in-home housekeeper, catering delivery, medical and bath aide, mental care, etc. Any qualified seniors can, in the future, enjoy different levels of governmental allowance according to the condition of their physical status, which are respectively RMB 300, 400, and 500 corresponding to three different levels from minor to mediate and high-level disability.

By far, there are only two types of seniors are entitled to enjoy the allowance. The first type is for indigent Shanghai local residents above 60 years old who are in need of care service. The other is for residents above 80 years old but are from “empty nest” family whose pension is less than the average standards, i.e. RMB 2,026 in Shanghai. After evaluation of such elderly’s needs in care service, government will cover 50% of the expense for his or her in-home care service.

Meanwhile, senior day care centers are expending very quickly in almost every cities recent years. We can see the determination and efforts from government to tackle the senior living difficulties from the very least community-level. Care centers are usually set up in communities to provide on-site dining, personal care, fitness training, recreation and escort service to partially disabled seniors on a daily bases. They are mostly funded and run by local government, and some are managed by private-run entities by government purchase arrangement. Given the very low service rate in the care center, most of the centers are hard to financially break even, even taking governmental allowance into consideration. Moreover, as most of these facilities are not-for-profit, private investors are barely interested in this business.

Good news is recently, we find a Notice from Qingdao regarding Strengthening the Construction and Operational Management of Exemplary Senior Day Care Center. The Notice clarifies many areas in the function, construction parameters, planning, equipment placement and operational management of day care centers, in order to eliminate the current problems of differentiated standard, simplified function or unqualified service, among others. Most important thing is, in the Notice, senior day care center can be operated by private investors for either for-profit or not-for-profit purpose. It is believed in the future more private investment will aim at this sector.

Urging for Long Term Care Insurance

Statistic shows by the end of 2010, the number of disabled or semi-disabled seniors in China has reached to about 33 million, and the number is expected to be 40 million by 2016. Many believe it is difficult to tackling with all the needs from these seniors, given no Long Term Care Insurance (LTCI) at present is available in China. Typically, LTCI can provide beneficiaries with coverage of care expense when he or she falls into sickness or disability and is in need of long term care service.

Insiders are suggesting to learning from countries like Germany, the United States or Japan to establish a LTCI system. It is suggested to have Ministry of Civil Affaires and Ministry of Health promulgated a regulation on care insurance, so to solve the funding problem by means of self-funding, public funding or mutual funding, etc. Some analysts also express the essence of a LTCI structural design is to make perfect match between the insurance and the actual needs from seniors, and hence the best solution might be a blend of both approaches of social security and commercial insurance, given the international practices and Chinese characteristics. That means the government is responsible to take care of the LTCI for low-income population by means of providing financial subsidiaries and tax preference as a part of social security; while the remaining citizens will take part in commercial LTCI program where employer and individual will together contribute the premium. As for the reimbursement method for long-term care expense, some suggests to referring to the international practice of both substance and cash reimbursement.

A hybrid of senior care and medical treatment is under exploring

Senior care and medical treatment always appear together, like two sides of a coin. How to make seamless match between the two is not an easy task. It is an imminent task for the whole industry to connect medical resource with senior care services.

A combination of senior and medical care, an emerging concept can be found in some under-planning or construction healthcare communities, is usually realized by means of setting up skilled nursing home, rehabilitation facility or geriatric hospital within the range of community. However, can such medical service be extended to home care service? Still no specific supportive policy is found. Moreover, threshold and barrier for most investors to establish geriatric hospital or rehabilitation facilities are too high. Therefore, many have focused on the “family doctor” system, which seems to be a feasible way out.

Shanghai took the lead in promoting the system since September 2010 when it introduced pilot scheme on licensed general practitioners, or GPs, at community health centers in several districts. According to statistics from Shanghai Municipal Ministry of Health released on this September 23, there are totally 769,800 families that have participated in the pilot scheme of “family doctor” rolling out in 10 districts in Shanghai. This allows residents to receive medical diagnose and therapy in or near their communities, easing the pressure on large, often overloaded hospitals. While the patient is deemed necessary to transfer to the designated hospital, the GPs will make the decision based on the patient’s condition. And establishment of medial expense reimbursement network in connection to this scheme is also under discussion.

By far, Shanghai allows qualified GPs to practice in different institutions, subject to approval from relevant authorities, and encourages experienced doctors to serve more to the community. However, systematic regulatory environment are still in lack, while an all-round implementation of “family doctor” will urge for support from different circles, such as network on medical expense payment, mechanism on compensation to medical institutions, and intensives to physicians, etc. What worth noting is, upon the success of Shanghai’s pilot scheme, the “family doctor” system has been introduced in different provinces like Jiangsu, Anhui and Fujian. It is believed, after several year’s improvement, it can become a very essential part in the solution on aging-in-place.

To tackle the workforce scarcity

Statistics show China will need 10 million caregivers by year 2015. However, there are only 300,000 in the marketplace right now, among which only 100,000 are licensed caregivers. Currently most of the senior caregivers are maids or housekeepers that come from rural areas or are temporary workforce from laid-off workers. They can only provide very simple aids to the seniors given their poor education and old age. With the increasing of aging population and improvement of welfare condition, seniors will ask for more advanced care service delivered by more technically improved nurses.

Reason for so few workforces in the senior care market can mostly attributed to the low income and social recognition to the caregivers. Although the Ministry of Civil Affaires has and will continue to invest huge amount of money in staff training, with a goal to realize 100% licensed nurses at work, it still seems hard to meet the current market demand in a short period.

On the other hand, it will adversely affect the maturation of the whole industry if we put only and too much stress on the workforce quantity instead of quality. To find a bottom-up approach, it’s better to start from preliminary education and training. For example, in Japan, caregivers should take two to three years’ of academic education in specialized college and then obtain professional qualification before he or she can be a licensed care worker. Catering to the Chinese situation, we should take more investment and effort in the academic education in college and provide more opportunities for graduates in professional practice. It was reported some colleges have aligned with hospitals, community health service centers and private-run senior care operators in order to train the workforce and provide more nursing staffs to the senior care industry. Some have also tried to enroll students from indigent families and provide them with subsidies or incentives. In that way, graduates are tailor-trained and then been employed by senior care providers. If it works, many will be attracted to follow this profession.

Meantime, Shanghai Senior Living Development Center (subsidiary to Shanghai Civil Affaires Bureau) has, start from this year, introduced a mutual care model—"old partners" scheme, which is to have lower aged seniors to take care of the higher seniors or live-alone ones. It will benefit 100,000 seniors who can have in-home care service thanks to such a plan. Distinguished from the current model of institutional senior care, in-home care or traditional family-support model, the plan is designed to strengthen people's connection within communities and families by means of mutual aid. In addition, to attract more senior citizen engaging into the similar scheme, some cities are exploring a "time deposit" scheme in order to switch the service time rendered by senior caregivers into the time they are entitled to enjoy care service in return.

Technology bringing about the breakthrough

The ever-changing advanced technology has brought about many business opportunities in the fields of "elderly-adapted" renovation. In the in-home care sector, it is important to prevent the live-alone seniors from being undiscovered when they have accidents and need emergent rescue or assistance. Many companies have therefore invented and produced all kinds of in-home care solutions by means of new technology. Telecare (or refer to as healthcare at a distance) is one these inventions. It can offer remote care of elderly and physically less able people, providing the care and reassurance needed to allow them to remain living in their own homes. The use of Internet and sensors integration can provide support for people with illnesses such as dementia, or people at risk of falling. When a sensor is activated it sends a radio signal to a central unit in the user's home, which then automatically calls a 24-hour monitoring center where trained operators can take appropriate action, whether it be contacting a local key holder, doctor or the emergency services. By such devices, residents can also achieve "remote diagnose" even they are at home. Technologies like this are uprising everyday that bring surprisingly convenience and innovation to the home care industry. While accessibility to Chinese citizens is still not that simultaneous, most needs are still on the "elderly-adapted" areas.

Shanghai municipal government is rolling out an "elderly-adapted" scheme within 10 districts. All costs are from welfare lottery revenue, and every family will have approximate RMB 20,000 subsidy for the purpose of house renovation. A seemingly small business of house renovation, if targeted at the huge potential costumer segment of senior citizens, the market opportunities are unmeasurable. Meantime, investors from environmental protection, information technology or video gaming sector, among others can also find numerous business opportunities in the in-home care industry.

Conclusion

To sum up, I've just seen a policy from Tianjin Municipal Civil Affairs Bureau on implementing a pilot scheme to extend the service parameter of institutional senior care facilities to the communities, or namely "virtual nursing home". The policy encourages the operators to walk out of their facilities and deliver care service to the seniors in the home. Moreover, the Tianjin government will provide incentive policies with regard to medical reimbursement, employment, risk management and subsidy of equipment purchase.

There will be a new trend in the industry that senior care facilities will have more chances to extend their service in the home care business. It is estimated by year 2020, total market revenue in the in-home care service segment will reach 500 billion. A long-term strategy for investors to find themselves a suitable place in this industry is therefore the most essential plan to consider for the time being. ■

Home Care in Australia

Article prepared by Russell Kennedy Principal John Corcoran and Solicitor Jessica Kinnear.

The Australian Government has done much to encourage home-based care in the last 20 years. The recent Aged Care Reform Package represents a further move towards home care that is consumer directed. However, with that comes new challenges for aged care providers.

On 20 April 2012, the Prime Minister, Julia Gillard, announced a comprehensive 10 year Aged Care Reform Package, "Living Longer. Living Better", recognising that older Australians want to stay at home for as long as possible and the need for reform of the aged care industry. It will provide $3.7 billion over 5 years to the aged care system, with $955.4 million going towards supporting people to live in their own home. It signifies the first national review of home support services since the 1980's.

One of the ways the Australian Government has assisted older Australians to remain living in their own homes is through funded Community Care Packages offering three levels of support based on an individual's needs. These are:

- Community Aged Care Packages providing a low level of care and offering an alternative to low-level residential care;
- Extended Aged Care at Home Packages providing high level care and offering an alternative to high-level residential care; and
- Extended Aged Care at Home Dementia Packages providing high level care to people with dementia.

Providers of aged care are able to take advantage of these packages by receiving daily subsidies per package allocated.

The "Living Longer. Living Better" comprehensive reform package gives priority to providing more support and care in the home with the proportion of home care packages to increase from nearly 40,000 to almost 100,000 by 2017.

Significantly, the reform package represents a profound shift in the direction of Consumer (or self) Directed Care (piloted since 2010), giving care recipients greater choice and control over the care they receive, engaging them in determining what and how their care needs are provided. The Government has trialled Consumer Directed Care through three levels of subsidised packages that broadly align with the Community Care Packages, and under the new reforms, all new home care packages will be offered on a Consumer Directed Care basis from 1 July 2013, with existing packages to be converted to this model by July 2015.

The message from the reform package for providers of aged care is that they will have an exciting opportunity to extend the services they provide by ensuring a more consumer focused approach to their businesses. However, with that comes increased accountability and responsibility, as providers will need to balance consumer choice with their duty of care to their customers, and consumer choice may not always be in the customers' best interests. This is an impending challenge for providers who will need to address how they will manage the process of customers directing care that may contradict the provider's assessment of their care needs. Increased funding will also result in the need for greater transparency that the funds are being appropriately spent on quality care services.

This initiative seeks to establish a nationally streamlined approach to home support but the challenge to aged care providers will be to ensure that the reforms are workable and sustainable for the long term. The reform package will be implemented in stages, with a major review to take place after 5 years, enabling consumers and providers alike to assess how the system has worked in practice and to propose any future reforms. ■

Russell Kennedy has a long and proud history of providing legal services to aged care and retirement village providers in Australia. We act for a number of not-for-profits, retirement villages, aged care providers, industry associations and government departments and agencies.

Our team comprises industry leaders who advise in medico-legal matters, property and facility development, employment and occupational health and safety standards, risk management and governance, commercial matters and in all issues relating to owning, operating and developing an aged care or retirement village facility.

We also advise our clients in relation to disciplinary hearings, administrative reviews, complaints handling issues, freedom of information, mental health, guardianship, coronial inquests, resident agreements and administrative matters.

John Corcoran
Principal

Tel: +61 3 9609 1624
Email:
jcorcoran@rk.com.au

Jessica Kinnear
Solicitor

Tel: +61 3 9609 1558
Email:
jkinnear@rk.com.au

The Long Term Care Dilemma

Written by Paul Goldenberg

"Does this path have a heart? If it does, the path is good; if it doesn't, it is of no use."—— Carlos Castaneda

We are visiting several homes and listening to discussions regarding difficult decisions about an elderly parent or spouse. The situations are different, but the ultimate question is the same. What do they do knowing that they cannot be there as their loved one ages and requires more care then they can provide?

It is truly sad as we watch the pain of having to conclude they no longer can be at home to manage the required support. The world around them has changed dramatically. There are fewer siblings to share the burden of care. Families often require two people to earn an income to support their current life style, or there is a single child who has not yet married and finds itself responsible for their parent.

Observing this discussion is even more troublesome as guilt and conflict fill the room. Culture tells them that they are responsible for their elderly parent. The weight often falls on the daughter or daughter-in-law who grew in a culture that values her role as a professional in the work force.

We have gone back in time to San Francisco, California in 1980. The struggles emanate from an aging population, smaller family units, people moving away from their parents for jobs, rising costs of care, not a lot of desirable options, and the feelings that that often get in the way of a rationale discussion.

I have heard that these are the same dilemmas people are discussing in the major cities of China, which is a country that has shown dramatic economic growth and lower birth rates in a culture the reveries the elderly, and is now facing these emotional and social crises thirty years later. There have been solutions in the United States and many of them not perfect with a series of missteps and various, often-imperfect solutions. Please join in a journey from 1980 until today, so we can look at some of these solutions. My professional experiences lead me to the conclusion that the culture and history of the United States is very different. I would presume this journey cannot always apply to answers that China is seeking, but the emotions are the same. The desire to provide quality care for the elderly is the same. As a proverb states:

"There are many paths to the top of the mountain, but the view is always the same."

My goal is to explore this path in the context of where the journey occurs, but the distention being the same. There cannot be long-term success if we do not understand where the journey is taking place. When I meet with families I talk about how important it is that they know their loved one is being cared for so they can "sleep at night" with comfort that the care being provided is safe. We also need to realize that no institution or caregiver can love their parent like they do. We must realize that placing someone in the care of others requires a level of faith that reduces the guilt and anxiety that could cause stress and anxiety.

Here is brief outline of the services offered in the United States with a brief description of each. Placing this in context requires an understanding that each of the Fifty Sates often have different regulations and different funding levels. There are also different regulations depending who is paying for the care. The Federal regulations are the most comprehensive. The federal regulations for Long Term care are second longest in the United States behind nuclear power plants. This is just a brief outline and each option requires even more discussion.

- Home care
  - Home health
    - Hours vary from weekly to daily and to having a live-in aid.
    - Nurses will visit

- Day Programs
  - Resembles day care for the elderly
    - Programs vary depending on the level of medical need.

- Independent living
  - Apartments with various levels of supervision, and the above survives can added as will

- Boarding homes
  - Rooms with continuous supervision
  - Communal dining
  - Continuous medical supervision is not provided.

- Assisted Living
  - Small apartments with continuous supervision and minimal daily nursing care

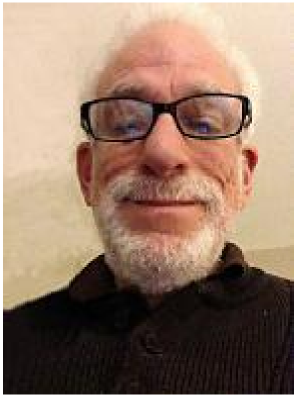
- Custodial Nursing Homes
  - Various programs and sizes with full supervision including trained and nurses. Therapy programs are available.

- Acute level nursing home
  - These facilities almost resemble hospital care with high levels of services and often look like a typical hospital ward, but at less cost. Highly trained aides, highly trained nurses with physician services available.

Each option needs to fit its community, so I am not presuming China should develop that same continuum of care. It is clear that it is difficult to have services that will meet everyone's needs.

Struggles that occurred in 1980 in California and often still occur are not different than what happens in the living rooms of many Shanghai apartments. The journey that takes place in China will take a different path. Ultimate outcomes depends on the knowledge that each path requires respect and recognition that it will not be same, but the Mountain that comprises excellent care is the ultimate destination. My hope is that we can share part of that journey and we learn from each other. This is a path that values our elders and creates values that connect all of us. ■

(To be continued…)



Paul Goldenberg

MSW, MBA, LNHA

Paul has been involved in carious aspects of human service management in for profit, government and non-profit agencies and organizations since 1974. He has graduate degrees from Philadelphia University and the University of Pennsylvania. His work in the long-term care industry began in 1989 when he joined Manor Care as a program director, which lead to a promotion as an administrator. Subsequently he has opened new facilitates, managed facilities as large as 300 beds, and pioneered the conversation and manage of post acute high acuity units. He also managed post-acute care and business development in a large metropolitan hospital environment. Paul currently consults for a long-term care management firm called Tobin Associates. In that roles he has opened a post acute unit for a large non-profit organization and he currently manageress nursing home that require a transitional processes into quality facilities. For the past eight years he has been an adjunction professor in the graduate program at Holy Family University in Philadelphia.

Contact the author: psgold@comcast.net

The Legal Framework on Commercial Franchise of In-home Care Business

Written by Michael Qu

Franchise offers a low cost and rapid growth model that provides easy access to the expanding consumer market and second and third-tier cities. Further, franchising enables faster brand recognition, drawing in consumers that see large brand name chains as being more reliable……especially in the in-home care service sector, many investors see huge potential opportunities in applying the franchise model, while some have already moved on.

Franchise has a history of more than one hundred years in foreign countries. Now it has developed to be a mature business mode, and it is widely used in food and beverage, apparel and hospitality sectors. In China, franchise has rapidly developed since 21 century and has fostered the biggest market in the world. As senior care industry grows, especially in the in-home care service sector, many investors see huge potential opportunities in applying the franchise model, while some have already moved on. Right at Home(R) International, Inc., a leading franchisor of in-home senior care and assistance, has since last year signed its first master franchise license agreement with an entrepreneurial group in Beijing, expanded into several cities. Seeing from the national strategy of helping majority elderly people to aging-in-place, we believe now it is just the very beginning.

Having advised investors in this sector since the industry's blooming, we found many are interested in franchise model—they all wish to bring successful business from their home country to China. Of cause, there are pros and cons, and profitability is to be tested given the scarcity of qualified caregivers in the market. However, enthusiasm never stops, thanks to not only the enduring charming of the franchise mechanism from itself, but a perfect match with senior care service as well.

To conclude a little bit on some of the most concerned questions from investors in the franchise regulatory environment, I will, in this article, introduce the legal system in China on commercial franchise, what are the solutions for in-home care service providers and what they should be aware of in the course of franchise business.

China's legal system on franchise

Generally speaking, commercial franchise is an arrangement whereby an enterprise (franchisor) through an agreement grants other operators (franchisees) the right to use its business operating resources, including registered trademarks, logos, patents, and proprietary technologies; whereby the franchisee conducts business under a uniform mode of operation; and whereby the franchisee pay franchise fees according to the agreement. Franchise offers a low cost and rapid growth model that provides easy access to the expanding consumer market and second and third-tier cities. Further, franchising enables faster brand recognition, drawing in consumers that see large brand name chains as being more reliable.

The main legislative provisions governing the commercial franchising in the PRC are: (a)the Measures on Administration of Commercial Franchises 《商业特许经营管理条例》(the "Franchise Measures") , took effect on May 1, 2007; (b) the Measures on Administrative Rules on Commercial Franchise filing 《商业特许经营备案管理办法》(the "Filing Rules ") , amended and took effect on February 1, 2012; and (c) the Measures for Administration of Disclosure of Commercial Franchise Information《商业特许经营信息披露管理办法》 (the "Disclosure Rules") , amended and took effect on April 1, 2012.

Apart from the above three, several regulations from local or departmental authorities are also indicative. On February 24, 2011, Beijing Municipal People's Higher Court issued the Guiding Opinions on Some Issues Concerning the Application of Laws in Hearing Cases of Commercial Franchise Contractual Disputes《北京市高级人民法院关于审理商业特许经营合同纠纷案件适用法律若干问题的指导意见》("the Guiding Opinions"), which represents the judicial attitude towards franchising in the city of Beijing. Moreover, Ministry of Commerce ("MOFCOM") issued Guiding Opinions of the Ministry of Commerce on Further Promoting the Healthy Development of Franchises during the 12th Five-Year Plan《商务部关于"十二五"期间促进商业特许经营健康发展的指导意见》 in January 2012 to further provide the policy trend in the regime.

Although the history of commercial franchise in China is short and unregulated market was found in early 90's, we have to admit right after the entry of WTO, a lot of progress was made and now these regulations are more catered to the international practice.

A, B, C steps and qualification for franchisors

Keeping one thing in mind is all franchising activities falls into the regulatory regime of MOFCOM, either MOFCOM itself or the local bureau of MOFCOM. To be qualified as a franchisor, the following requirements and conditions are to met:

Firstly, the franchisors shall be enterprises, excluding other economic organizations and individuals. The Franchise Measures clearly request that the franchisors shall operate at least 2 directly operated outlets, and the period of operation shall be more than 1 year (the "2+1" rule). If the outlets are outside China mainland and operated by foreign enterprises, franchisor shall provide proving documents, which have been notarized by local notary public and certified by Chinese embassy in the country. However, a foreign franchisor does not meet the "2+1" rule if using the domestic outlets operated by its affiliates in China. It is worth mention that, according to Beijing's Guiding Opinions, a franchise contract entered into failing to reach the "2+1" rule is not inevitably deemed invalid. That said, in a "Inter-company License" case where a foreign franchisor license trademarks or other resource to its China subsidiary will not be deemed as "franchising", rather, it will be deemed as "inter-company licensing" , which will not trigger the application of the "2+1" rule.

Secondly, to engage in franchising a franchisor shall have a mature business model, and shall be able to provide franchisees with continuous operational guidance, technical support, training and other services. Enterprises which copy the manuals, websites and enlisting documents of others, and have no service abilities for providing business guidance, technology support and training shall be excluded. The trademarks to be licensed to franchisees shall be registered trademarks. And, the logos, patents and proprietary technology of enterprises are included in the business sources to be licensed to others. Franchising activities involving trademark licenses or patent licenses shall file with relevant Chinese authorities.

Thirdly, archival filing procedures with MOFCOM should be conducted. According to the Filing Rules, where a franchisor engages in commercial franchise operations within the territorial scope of a province, autonomous region or municipality directly under the central government, the franchisor shall register with the Commerce Department of the respective province, autonomous region or municipality directly under the central government where it is located. Where a franchisor engages in commercial franchise operations across the territorial boundaries of a province, autonomous region or municipality under the central government, the franchisor shall register with MOFCOM or MOFCOM's delegated Commercial department. As a result, the general public may obtain the following information through the government website of the Ministry of Commerce: (a) The registered trademark(s), enterprise mark(s), patent(s), know-how and other business resources of the franchisor; (b) The franchisor's archival filing date; (c) The location of the legal business place, contact information and name of the legal representative of the franchisor; and (d) The location of the business place of the franchisee(s) within China. Moreover, foreign investment enterprises shall also submit <Approval Certificate of Establishment of Foreign Investment Enterprises>, which shall include "engage in business activities in the form of franchise" into its business scope.

What worth mentioning is that, the registration procedure with MOFCOM is only a filing procedure, not an approval one. Failure to file with the Chinese authority will be subject to penalties such as orders for rectification and fine, but not necessarily lead to the franchisor in question losing its legal capacity to sell franchise in China. And according to Beijing's Guiding Opinions, a franchise contract is usually deemed valid even though franchisor fails to complete with the filing procedure.

And fourthly, franchisor should meet the information disclosure requirements. Information disclosure system is the core system of franchising. The Disclosure Rules provides that the franchisors shall establish and implement a perfect information disclosure system, and provide the relevant information and franchising contracts in written form, at least thirty days before execution of franchising contracts. It also sets out the specific provisions on the information which shall be provided by franchisors, including the basic conditions and commercial reputation records of the franchisors and their legal representatives, business sources owned by franchisors, abilities of franchisors to provide service to franchisees and management and supervision on business of franchisees, franchisee fees and the payments, and budgets for investment in franchising shops. To the franchisors that violate these provisions, the authorities in charge of commerce will order them to rectify, charge penalties and make public statements. And if the franchisor fails to fully disclose the information accordingly, the franchisee is entitled to terminate franchise contract.

Common concerns from franchisors in senior care service providers

Choose between direct-ownership and franchise

Many international brands are struggling between the direct ownership (i.e. foreign direct investment with WOFE/JV) and franchise. Main reason to choose direct ownership over franchise might be the difficulty of finding good partners, lack of local management skills, local franchisees not following franchise standards (sacrificing brand image for short-term profits), lack of control over recruitment, intellectual property challenges or difficulties in acquiring locations. However, whilst direct-ownership gives investor control over business operations, it also constraints the business from rapid expansion. Franchise, on the other hand, provides investors with a simplest and cheapest way to get started and expand in China, but can result in a loss of control and supervision over the franchise. Therefore, a workable franchising mechanism is necessary to be established.

Protection of franchisor's intellectual property

Undoubtedly, core value of franchising is intellectual property. However, as a protective mechanism, franchisee is obliged to keep the franchisor's business secret confidential. According to the Disclosure Rules, if a franchisee knows business secrets of a franchisor as a result of their contractual relationship, the franchisee is required to keep such business secrets confidential even if no specific agreement has been made to this effect. After the franchise agreement is terminated, even though the franchisor and franchisee have not signed a non-disclosure agreement that regulates the confidential obligations afterwards, the franchisee still has an obligation to keep the franchisor's business secrets confidential. Failure to abide by the confidentiality obligation and causes damages to the franchisor and others, franchisee shall be liable for relevant liquidated damage. However, the most common cases are franchisee gets to know how to do the business and make a fresh start all by its own after expiry of franchise contract, which is very hard to control. What franchisor can do in advance is to set provisions on trade secrets and non-competition in the franchise agreement on the scope, protection measures and liability of breach of contract, and protect its legitimate right via legal action whenever any infringement is conducted by the franchisee.

How to manage operational risk

The Franchise Measures have provided in details administrative punishment for franchisor's illegal activities, and also touch on some criminal liabilities under certain circumstance. However, provisions on civil liabilities are very few, where, on the other hand, lies the biggest operational risks for senior care business. Generally speaking, as franchisees are independent legal entities who have separate capability to take their liabilities on their own, and therefore franchisor will not take responsibility to any third party that attributes to the franchisee. Only when the third party can prove franchisee is the deemed to have authorization from franchisor and franchisee is act on behalf of the franchisor, or in the event the business resources shared and licensed by the franchisor have some kind of defect and result in third party's damages, the franchisor is responsible to take liability to the third party.

In practice, accidents arising from negligence of caregivers occur very often in in-home senior care service industry, and therefore it is important to set provisions on liabilities that explicitly agreed on the liabilities between the franchisor and the franchisee if either of them breaches the contract or commits a tort against any third party. In addition, more important for the franchisor is put in place a supervision and control mechanism that explicitly agreed on supervision and control over the business location, business operation, quality of products and services and training for employees in order to prevent accidents from happening in daily operation.

Last but not the least important thing is to have the franchise contract well-drafted by your lawyers, and for foreign franchisors, whether they are already present in China or considering entering into the market, is advised to closely monitor the franchise regulatory developments and make sure that they are putting their best foot forward in terms of regulatory compliance. ■

If you want to know our publication, please click our official website: www.lawviewer.com
OR contact Michael Qu Attorney of Law
Email: quqin@co-effort.com Tel: 86-021-68866151*152 MP: 86-13817878607

Lawviewer.com is founded by lawyers and professionals from Co-effort Law Office--an international full legal service provider employs around two hundred lawyers and professionals that offer unique insight and experience to companies and investors in high-growth sectors. The firm's resources and services will span foreign investment and trade, M&A and finance, construction and real estate, as well as market-leading experience advising clients in corporate transaction, intellectual property and commercial litigation.

We understand that clients are looking for value beyond just legal expertise. For years, we work together with our clients to achieve business goals with our in-depth understanding of the industry, and have built a client roster that includes many of the world's most recognized and respected brands and a proven track record of unparalleled performance.