Introducing the New Multi-Level Marketing Governing Act

By Max Wang

Background

Taiwan had approximately 369 multi-level marketing (MLM) companies and a total of 3.09 million MLM participants as of December 31, 2012. Adjusting for people who participate in more than one MLM company, almost 12% of Taiwan’s total population participates in at least one MLM business.

Although Taiwan’s MLM industry is robust and thriving, Taiwan until recently did not have any law specifically aimed at regulating this business. Instead, the MLM industry was regulated by certain provisions of Taiwan’s Fair Trade Act (FTA) and a set of regulations issued under the FTA, the Supervisory Regulations Governing Multi-Level Marketing (MLM Supervisory Regulations).

Recently, the Fair Trade Commission (FTC) successfully promoted a new legislative regulation scheme - the Multi-Level Marketing Governing Act (MLM Act), which was passed by Taiwan’s Legislative Yuan and became effective on January 29, 2014. The MLM Act supersedes the FTA as it formerly applied to the MLM industry.

The MLM Act has introduced critical changes to Taiwan’s MLM industry, including those described below.

Change of the Definition of 'Multi-Level Marketing'

The FTA previously defined MLM as a “promotion or sales plan or organization pursuant to which the participants pay a certain consideration to obtain the right to promote or sell goods or services and the right to introduce other persons to participate in the plan or organization, thereby receiving a commission, bonus, or other economic benefit.”

The MLM Act has changed this definition to “a way of marketing by which [a company] acts through its distributors (MLM participants) to introduce others to participate in the business and create a multi-level organization so as to promote or sell certain goods or services”.

Under this broader definition, it no longer matters whether a participant pays an MLM company for the right to participate. If a company recruits new participants through existing participants and establishes a multi-level organization, it is governed by the MLM Act. However, we expect a clearer definition of ‘multi-level organizations’ to be established through court decisions and rulings under the MLM Act.

Impact of Expanded Coverage of the MLM Act

Requirement of FTC Registration

The MLM Supervisory Regulations required MLM companies governed by the FTA to register with the FTC before they began to transact business. With the expansion of the definition of ‘multi-level organizations’, the MLM Act requires an MLM company not
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previously covered by the FTA to register with the FTC as an MLM company within three months of the effective date of the MLM Act. Because the registration requirements under the MLM Act are different from the requirements under the MLM Supervisory Regulations, the MLM Act also requires those MLM companies that have already registered with the FTC to make an additional registration with the FTC in accordance with the MLM Act within two months of the effective date of the MLM Act.

Requirement of Written Participation Agreements with Compulsory Provisions

The MLM Supervisory Regulations required MLM companies to enter into written participation agreements with their participants incorporating certain mandatory provisions, and required that such agreements not be made electronically. The MLM Act now requires those MLM companies not covered by the FTA definition to enter into written participation agreements within six months of the effective date of the MLM Act.

Furthermore, the MLM Act grants MLM participants of such MLM company the option to rescind or terminate their participation agreements within 30 days from the date that a written participation agreement is entered into.

Expansion of the Compulsory Provisions in the Participation Agreement

As mentioned above, the MLM Supervisory Regulations set compulsory provisions to be included in MLM participation agreements. In addition to keeping the compulsory provisions under the MLM Supervisory Regulations, the MLM Act requires MLM participation agreements to contain the additional terms as follows:

- operation plans
- qualifications to become a participant
- the formula, standards and reasons for an MLM company to estimate the depreciation of the goods or services returned by a participant after the cooling-off period
- the events of default by participants and the procedure to be followed
- the method for dealing with a participant’s request to return goods or services in the event that termination or rescission of the participation agreement is attributed to the participant’s breach of contract or regulations
- conditions and methods for the renewal of participant agreements.

The MLM Act requires those MLM companies subject to the FTA to revise their existing participation agreements within three months of the effective date of the MLM Act, to notify existing participants in writing, and to make a copy of the revisions available on the MLM company’s business premises. If the participants do not express disagreement within a certain period, they are deemed to have agreed to the revision.

Broadening of Forbidden Conduct

Similar to the MLM Supervisory Regulations, the MLM Act also specifies conduct in which MLM companies are forbidden to engage. In general, the types of forbidden conduct are:

- requiring participants to pay fees for training, seminars, social activities, etc. that are obviously not equivalent to the real costs
- requiring participants to pay an improper guarantee, default payment, or other fee
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- requiring participants to purchase goods in a quantity that is obviously impossible for an average person to sell in a short period, unless it is agreed that the price shall be paid to MLM companies only after the goods are re-sold
- giving specific persons preferential treatment in a manner contrary to the multi-level sales organization or plan, such that the commissions, bonuses, or other economic benefits that should be available to other participants are diminished
- improperly soliciting participants to purchase or to possess two or more participation rights to promote the MLM organization
- requesting that participants bear other obviously unfair obligations.

It is noteworthy that the MLM Supervisory Regulations did not prohibit the sale of multiple participation rights, but the MLM Act now prohibits the “improper solicitation” of such a sale.

Foundation of a Protection Institute Funded by MLM Companies

The MLM Act requires the FTC to establish an MLM Protection Institute to protect both MLM companies and their participants and to resolve disputes between them.

According to the MLM Act, the FTC may designate certain registered MLM companies to fund the establishment of the Protection Institute. The MLM Act also empowers the FTC to authorize the Protection Institute to collect funds and annual fees from both MLM companies and participants. Only those companies and individuals who have paid funds and annual fees may seek protection from the Protection Institute.

According to a press release, the FTC aims to establish the Protection Institute before the end of 2014. Therefore, when the FTC enacts rules or guidelines for the Protection Institute, details of the function and operations of such Institute will become clear.

Extended Cooling-Off Period

The FTA granted every MLM participant a 14 day cooling-off period starting from the date that he/she entered into an MLM participation agreement with an MLM company. Within this period, a participant was able to rescind the participation agreement by giving written notice to the MLM company.

The MLM Act has increased this cooling-off period to 30 days, during which an MLM participant has the option to choose whether to 'rescind' or 'terminate' the participation agreement. Under Taiwan law, upon 'rescission' of an agreement, the agreement is deemed not to have been made, and therefore each party must restore the other party to its status quo ante (the way things were before the agreement was signed). Upon 'termination', the agreement is deemed valid until terminated, and the parties therefore are still obliged to perform their respective obligations arising from the agreement prior to termination.

The MLM Act requires MLM companies to accept a request to return goods or services (if applicable) made by an ex-participant within 30 days of termination or rescission, and to refund 100% of the original purchase price, plus all other payments made by the ex-participant, excluding depreciation that may be attributed to the participant and any bonus/incentives that have already been paid to the participant. This requirement seems intended to protect MLM participants; however it blurs the distinction between the existing legal consequences of termination and rescission.
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New Six-Month Limit on Buy Back of Goods Upon Termination of Participation Agreement

Under the FTA, an MLM participant was entitled to terminate the participation agreement at any time after the cooling-off period and the MLM company was obliged to buy back all the goods and services (if applicable) in the participant’s possession. The buy back consideration was required to be 90% of the original purchase price (as opposed to the 100% of the original purchase price that applied during the cooling-off period), excluding depreciation (regardless whether such depreciation was attributed to the participant) and any bonus and/or incentives that had already been paid to the participant.

The MLM Act maintains an MLM participant’s termination right and the right to compel the MLM company to buy back goods and services; however, under the MLM Act, an MLM company has no obligation to buy back goods that have been available for the participant to pick up for over six months. The buy back price remains the same. However, the six month limit only applies to goods, not services. In addition, in the event that the goods or services are provided by a third party, the MLM Act still requires the MLM company to buy them back. Furthermore, MLM companies must pay any and all damages or default penalties incurred by participants arising from rescission or termination.

Implications

The MLM Act affects different companies in different ways, depending on whether they were subject to the former MLM regulations.

Some companies not previously subject to the MLM Supervisory Regulations (because they didn’t charge a participation fee) are now subject to the MLM Act. These companies need to register with the FTC and ensure their participation agreements comply with all of the compulsory requirements of the MLM Act.

Companies entering the Taiwan market for the first time may consider whether they are able to adopt a single-level rather than multi-level business model. By doing so, they may avoid being covered by the MLM Act.

Companies that were previously subject to the MLM Supervisory Regulations and are now subject to the MLM Act will be required to:

- revise their existing participation agreements within three months of the effective date of the MLM Act
- deliver original copies of the revised participation agreements to existing participants and display a public announcement of the revision on their business premises
- update their filings with the FTC to comply with the new filing requirements within two months of the effective date of the MLM Act.

Because the MLM Act provides tight timeframes for MLM companies to comply, to avoid being fined for late revision or registration we recommend that all MLM companies initiate necessary compliance actions now. We also encourage MLM companies to take into account the potential increase in their operational costs caused by the MLM Act during their annual pricing review.
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