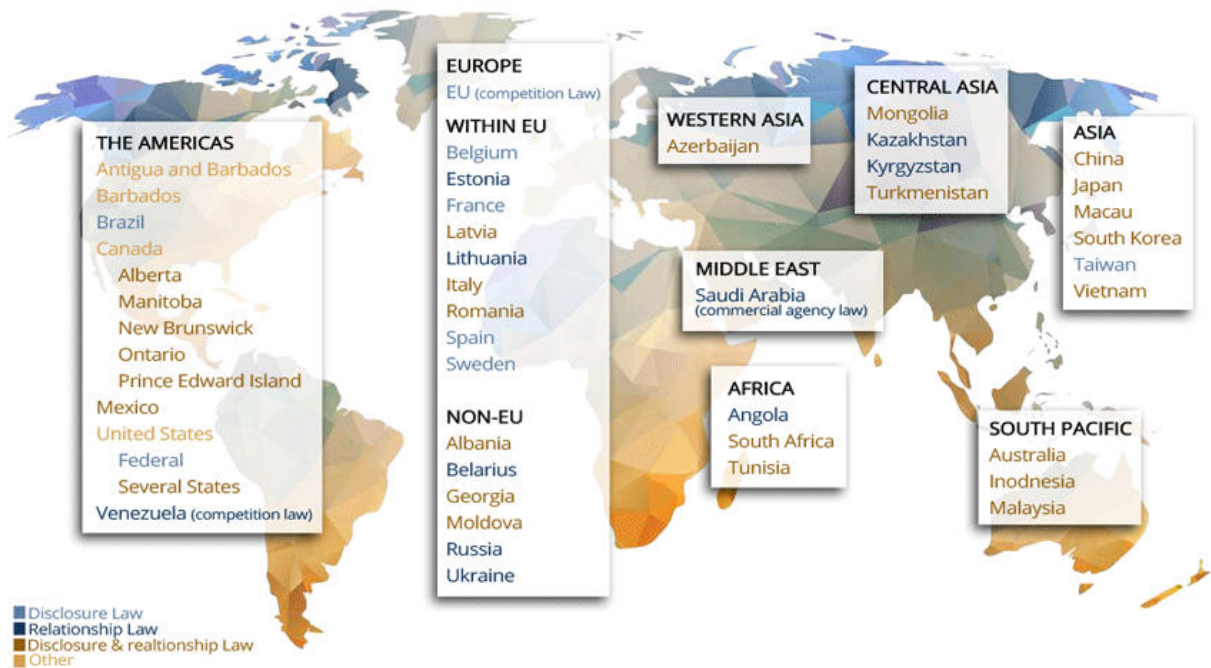




INTERNATIONAL RESOURCES ABSTRACT

Laws and agencies that regulate the offer and sale of franchises



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Which laws and government agencies regulate the offer and sale of franchises?

Government Regulation No. 42 of 2007 dated 23 July 2007 on Franchising (Regulation No. 42) and its implementing regulation, Regulation of the Minister of Trade No. 53/M-DAG/PER/8/2012 dated 24 August 2012 on Implementation of Franchising (Regulation No. 53), and Decree of the Director General of Domestic Trade No. 138/PDN/KEP/10/2008 dated 31 October 2008 on the Technical Guidelines for the Implementation of Franchising (Decree No. 138).

Also, specific regulations have recently been issued by the Minister of Trade on, respectively, Modern Store Franchising (Regulation Number 68/M-DAG/PER/10/2012 – Regulation 68) and The Development of Partnerships in Franchising for Food and Beverages Services Business Activities (Regulation Number 07/M-DAG/PER/2/2013 – Regulation 07).

What are the exemptions and exclusions from any franchise laws and regulations?

In general, there are no exemptions. However, we were informed that in certain cases, at the recommendation of the franchise assessment team, the relevant ministry may issue a permit to use less than 80 per cent of domestically produced products and services. In addition, there are no clear guidelines as to how this recommendation will be issued.

Does any law or regulation create a requirement that must be met before a franchisor may offer franchises?

The Franchise Law stipulates that the franchisor must have been in business for five years. Its franchise business must still be in operation and must be profitable. A franchisee that has been granted the right to sub-franchise must have at least one company-owned operation.

Are there any laws, regulations or government policies that restrict the manner in which a franchisor recruits franchisees or selects its or its franchisees' suppliers?

Under Regulation 53 a franchisor may not appoint a franchisee with which it has a direct or indirect control relationship. Such measures mean that this would be a relationship with common shareholders rather than a management relationship. Hence, a franchisor cannot appoint a subsidiary or affiliate as its franchisee. Further, both franchisor and franchisee can only operate in business activities specified in their business licences, ie the franchise business should be the line of business specified in their corporate documents (articles of association or bylaws) and the technical licences issued by the relevant technical ministry. Regulation 53 also requires franchisors to cooperate with local small and medium businesses (SMEs) as franchisees or suppliers, if they can satisfy the franchisor's requirements.

Franchisors and franchisees must use domestically produced goods or services for at least 80 per cent, consisting of raw materials, business equipment and merchandise which will be measured by number of items (not by value). The minister of trade may exempt a franchise from this requirement in certain cases, based on the recommendation of an assessment team. In certain cases, the franchise business may also sell up to 10 per cent supplementary goods out of their total offered items. However, there



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are no further guidelines on how the cooperation with SMEs is to be implemented, or how the recommendation will be issued or what may be considered 'certain cases'. The satisfaction of those requirements by the parties to a franchise arrangement should be provided in the annual report submitted by the franchisor and franchisee to the Ministry of Trade.

In the event of unilateral termination by the franchisor, a clean break letter or alternatively a final and binding court ruling is now required before the franchisor can appoint a new franchisee for the same territory.

The total number of outlets to be managed by the franchisee must be stated in the franchise agreement. However, specific franchise regulations (ie, Regulation 68 and Regulation 07, now impose limitations on the number of outlets managed or owned by a franchisor and a franchisee). Regulation 68 stipulates that franchisors and franchisees engaged in a modern store business may operate up to 150 company-owned outlets. Thereafter, they must appoint independent sub-franchisees. This requirement applies to mini markets with an area of 400 square metres or less, supermarkets of 1200 square metres or less and department stores of 2000 square metres or less. Exemption to this requirement may be applied in certain circumstances. Regulation 07 limits the number of self-managed or owned outlets for franchisors and franchisees in the food and beverage businesses (restaurants, bars, and cafés) up to 250 outlets. Any additional outlets must either be franchised or operated by way of cooperation with capital participation.

In the case of a sub-franchising structure, who must make pre-sale disclosures to sub-franchisees? If the sub-franchisor must provide disclosure, what must be disclosed concerning the franchisor and the contractual or other relationship between the franchisor and the subfranchisor?

The law does not explicitly regulate this. A master franchisee will act as a franchisor in a sub-franchising arrangement, therefore the provisions applicable to a franchisor will also apply to a master franchisee.

The sub-franchisor must provide disclosure of its proposed sub-franchising. The scope of disclosure will be similar to that which must be disclosed by the franchisor.

In addition, in a sub-franchising arrangement, the master franchisee is required to own and manage by itself at least one of the businesses that it is permitted to sub-franchise.

Is there any obligation for continuing disclosure?

As advised above, the law does not require the disclosure document to be updated. However, we understand that in practice, it is advisable to continuously send updates for the disclosure document to each prospective franchisee and the MOT.



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How do the relevant government agencies enforce the disclosure requirements?

There are no regulations regarding enforcement of the disclosure requirements, except the enforcement of the disclosure registration itself. An administrative sanction in the form of a written warning will be imposed on the franchisor or franchisee, or both, that does not comply with the prospectus and franchise agreement registration requirements. The written warning will be served a maximum of three times: each warning will be served two weeks after the date of the previous warning letter.

A fine of up to 100 million rupiah will be charged if the franchisor or franchisee, or both, fail to respond to the registration requirements within two weeks of the third warning letter's expiry date.

In addition to any laws or government agencies that specifically regulate offering and selling franchises, what are the general principles of law that affect the offer and sale of franchises? What other regulations or government agencies or industry codes of conduct may affect the offer and sale of franchises?

The Indonesian Supervisory Commission on Business Competition (KPPU) Regulation No. 6 of 2009 on Guidelines for Exemptions from the Implementation of the Anti-monopoly Practices and Unfair Business Competition Law for Agreements Related to Franchises and the ICC.

Do other laws affect the franchise relationship?

Franchises are exempt from the provisions of Indonesia's Antitrust and Unfair Business Competition Law (article 50B of Law No. 5 of 1999 on the Prohibition against Monopolistic Practices and Unfair Business Competition). The Indonesian Supervisory Commission on Business Competition (the Commission) has formulated franchise guidelines (Regulation No. 6 of 2009 on Guidelines for Exemptions from the Implementation of the Anti-Monopoly Practices and Unfair Business Competition Law for Agreements Related to Franchises (Guidelines)). The Guidelines serve as a clarification of article 50B that deals with matters relating to agreements for intellectual property such as franchising, licensing, patent, trademark, copyright, industrial designs, integrated circuits and trade secrets.

Franchise agreements must not contain provisions that may result in monopolistic and unfair business practices. Other laws may affect the franchise relationship. If the franchise involves the importing of goods, import and export regulations are relevant. Trademark laws and other intellectual property laws may affect the franchise relationship.

Other specific laws that may affect the franchise relationship may include regulations on food registration and 'halal' certificates, regulations on modern markets (applicable to mini-markets, supermarket franchisees, hypermarkets and traditional markets), regulations on advertising, and Indonesian consumer law. The ICC will apply regarding the parties' general contractual obligations or when said obligations are not specifically regulated in the franchise agreement.