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| | DLA Piper LLP (US) |
Overview

1. What forms of business entities are relevant to the typical franchisor?
The typical franchisor would usually take the form of a limited liability company whose capital is divided into shares.

2. What laws and agencies govern the formation of business entities?
The formation of limited liability companies in Indonesia is governed by the Companies Law (Law No. 40 of 2007) and administered by the Ministry of Law and Human Rights (MOLHR).

3. Provide an overview of the requirements for forming and maintaining a business entity.
In general, a limited liability company must be formed by at least two parties by executing a deed of establishment containing its articles of association before a notary public. The notary then submits the deed of establishment and articles of association to the MOLHR for its approval. Upon obtaining the MOLHR's approval, the company attains legal status and the shareholders' liability is determined according to the percentage of issued shares to which they have subscribed. The MOLHR then arranges for the publication of the deed of establishment and articles of association in the Supplement to the Indonesian State Gazette.

The company must then be registered with the Companies Registry maintained by the local office of the Ministry of Trade (MOT). The MOT then issues a company registration certificate valid for five years (renewable). Another division of the MOT (assuming the company is a 100 per cent locally owned company, ie, it has no foreign shareholders) then issues the company an operating business licence that is valid for as long as the company remains in operation. Depending on its business activities, the company may also be required to apply for a technical business licence from the relevant authority. All companies must convene the annual general meeting of shareholders to discuss and approve, among other things, the annual report and financial statements prepared by the board of directors. Extraordinary general meetings of shareholders may also be held when required.

4. What restrictions apply to foreign business entities and foreign investment?
Foreign business entities may establish a foreign investment company (PMA Company) in Indonesia to engage in business activities that are open for foreign investment. A PMA Company falls under the auspices of the Indonesian Investment Coordinating Board (BKPM). Foreign investors should check the investment negative list to see whether there is any share ownership prohibition or restriction for foreign investors in the business field and discuss with the BKPM or other relevant authorities whether they must satisfy any other requirements when BKPM issues its approval for the investors’ application form (eg, if a manufacturing venture, where the factory must be located, and so forth).

Every Indonesian company must have authorised capital of at least 50 million rupiah and at least 25 per cent of the authorised capital must be issued and fully paid up by the shareholders. Specifically for a PMA Company, the Indonesian government requires a much higher minimum investment for one business activity, as detailed below:

- the minimum total investment, which may consist of loans and (paid-up) capital with an allowed ratio generally of 2:1 (excluding the value of its land and buildings): more than 10 billion rupiah;
- issued and paid-up capital: at least 2.5 billion rupiah; and
- capital participation of each shareholder: at least 10 million rupiah, and the percentage share ownership is based on the nominal value of the shares.

A PMA Company may not engage in retail business, except on a large scale. Foreign investment in the financial sector is regulated by the Ministry of Finance. There is no foreign exchange control. However, any movement of foreign currency worth US$100,000 or more must be reported to the Indonesian Central Bank by the facilitating bank in Indonesia. In addition, the bank must obtain the supporting documents for the transaction underlying the outgoing transfer in foreign currency from its customer or the foreign party if they wish to purchase foreign currency against the Indonesian rupiah, if the total amount exceeds US$100,000 (or its equivalent in other currencies) per month per customer.

5. Briefly describe the aspects of the tax system relevant to franchisors. How are foreign businesses and individuals taxed?
Foreign businesses and individual residents of Indonesia must pay income tax. Some of the taxes that need to be considered include VAT, withholding tax and permanent establishment tax.

VAT
VAT is levied on supplies of goods and services within the Indonesian customs area and those imported into the customs area. VAT also applies to services performed abroad but consumed in Indonesia. Therefore, VAT is payable on the provision of services by the franchisor to the franchisee, regardless of the place of performance. The general rate of VAT is 10 per cent. VAT on luxury goods is between 10 per cent and 75 per cent.

Withholding tax
Tax on the importation of goods and the use of foreign services is paid by the importer or user. Under Indonesian tax law, as a non-resident taxpayer, a foreign franchisor does not have to withhold taxes.

Permanent establishment
Foreign companies with no permanent establishment in Indonesia are only subject to a final withholding tax on certain types of income derived from Indonesian sources. A permanent establishment of a foreign corporation is liable for regular Indonesian corporate tax on profits directly or indirectly attributable to its permanent establishment in Indonesia. In addition, a 20 per cent ‘branch profit’ tax (reduced by tax treaty; 10 per cent in the case of the United States) is imposed. With respect to services and contracts to be performed in Indonesia, a foreign corporation from a tax-treaty country (such as the United States) is considered to have a permanent establishment if its employees are present in Indonesia for business purposes for more than 183 days in a 12-month period (in some cases a 90-day or 120-day limit applies, depending on the tax treaty with the relevant country). If the franchisor plans to send any staff to Indonesia, it should seek tax advice related to

Norma Mutalib, Richard Cornwallis and Reagan Roy Teguh
Makarim & Taira S
6 Are there any relevant labour and employment considerations for typical franchisors? What is the risk that a franchisee or employees of a franchisee could be deemed employees of the franchisor? What can be done to reduce this risk?

In general, the Manpower Law does not apply to foreign franchisors domiciled overseas, unless they employ Indonesian nationals or expatriates to work in Indonesia. To minimise the risk of a franchisee’s employee being deemed an employee of the franchise, the franchisor must make sure that the relationship with the franchisee is that of an independent contractor and expressly provide for this in the franchise agreement. If the franchisee requires assistance from the franchisee’s employees on a more permanent basis, the employees should be employed by the franchisee.

7 How are trademarks and know-how protected?

Foreign and domestic franchisors may protect their trademarks and know-how under the prevailing intellectual property laws. Trademarks are registered with the Indonesian Trademark Office of the Directorate General of Intellectual Property Rights (the Directorate), and know-how may be protected under the patent or relevant IP laws (industrial designs, copyrights, trade secrets). There is no obligation to register a copyright, but it is recommended.

Trade secrets are also protected under the Indonesian Trade Secrets Law (Law No. 30 of 2000) and the Anti-Monopoly and Unfair Business Competition Law (Law No. 5 of 1999 – the Anti-Monopoly Law). Under the Trade Secrets Law, an agreement containing the granting of rights to use trade secrets must be registered with the Directorate. The agreement will then be published in the Official Trade Secrets Gazette. One consequence of not registering an agreement is that it will not bind third parties. Unfortunately, no further details on this binding effect are provided in the law. However, it is expected that registration will provide the trade secret holder the right to enforce its IP rights against infringers, as well as to preserve its rights against third parties. Without registration, it is also arguable that as long as the agreement is entered into in good faith and satisfies the requirements under the Indonesian Civil Code (ICC) (articles 138 and 1320), and it has been signed by the authorised representatives of the contracting parties, the agreement should reasonably bind a third party. According to the Trade Secrets Law, the procedures for registration will be provided in a government regulation, but no such regulation has been issued yet. Therefore, the Directorate cannot formally process the registration of such an agreement and, in practice, not many parties register their agreements. This may also be because of the confidentiality issues (ie, to what extent the Directorate will maintain the confidentiality of the agreements submitted to it).

8 What are the relevant aspects of the real estate market and real estate law?

The franchisee will have to purchase or lease the real estate for its premises from the property owner. Under the ICC, a lessee has the right to enjoy leased property until the expiry of the lease term. If the property is transferred to a third party, the new owner cannot terminate the lease without the consent of the lessee. Care should be taken that the property is located in an area designated (zoned) for commercial purposes (as opposed to residential purposes). In general, non-resident foreign franchisors cannot purchase real estate. Resident foreigners may purchase property under a specific title – a right to use title – and under certain conditions (ie, their presence must be ‘of benefit to national development’ and their ‘ownership’ is limited to one property.

9 What is the legal definition of a franchise?

A franchise is described as a special right that is owned by an individual or an entity over the unique characteristics of a business system that has been successful in the promotion of goods or services, and can be used by another party pursuant to a franchise agreement.

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

Government Regulation No. 42 of 2007 on Franchising (Regulation No. 42) and its implementing regulations:

- Decree of the Director General of Domestic Trade No. 138/PDN/KEP/10/2008 on the Technical Guidelines for the Implementation of Franchising (Decree No. 138);
- Business Competition Supervisory Commission Regulation No. 6 of 2009 on Guidelines on the Exemption from the Implementation of Law No. 5/1999 (the Anti-Monopoly Law) for Franchise Related Agreements (Commission Guidelines);
- Regulation of the Minister of Trade No. 53/M-DAG/PER/8/2012 on the Implementation of Franchising (Regulation No. 53) as amended by Regulation of the Minister of Trade No. 57/M-DAG/PER/9/2014; and
- Decree of the Director General of Domestic Trade No. 16/PDN/KEP/3/2014 on the Technical Guidelines for the Implementation of Franchising (Decree No. 16).

Also, specific related regulations have been issued by the Minister of Trade:

- Modern Store Franchising (Regulation No. 68/M-DAG/PER/10/2012 – Regulation 68);
- the Development of Partnerships in Franchising for Food and Beverages Services Business Activities (Regulation Number 07/M-DAG/PER/5/2013 – Regulation 07 as further amended by Regulation No. 58/M-DAG/PER/9/2014); and
- the Obligation to Use the Franchise Logo (Regulation No. 60/M-DAG/PER/9/2013).

11 Describe the relevant requirements of these laws and agencies.

A franchise must meet the following criteria:

- have a specific business characteristic;
- be a proven successful business, which refers to the franchisor having business experience of approximately five years;
- have a written standard operating procedure to enable the franchisee to conduct its business according to the franchisor’s business system;
- be easy to learn and apply;
- provide continuous support to the franchisee; and
- have a registered intellectual property right.

Before entering into a franchise agreement, a franchisor must provide a prospectus disclosing its business data or information to a franchisee at least two weeks before the execution of the franchise agreement.

Certain restrictions apply to franchises in general, as well as specific restrictions on modern store and food and beverages businesses. See question 14.

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

In theory, franchisors and franchisees must use domestically produced goods and services for at least 80 per cent of their raw materials, business equipment and sales. Further, a statement confirming this must be attached to the prospectus and franchise agreement registration form. Compliance with the rule is disclosed in the annual report submitted by every franchisor and franchisee. If the parties believe that this threshold is not possible, they can apply to the MOT for an exemption and it will be evaluated by the assessment team.

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

Ideally, the franchisor should be registered before it offers franchises. However, owing to the cumbersome registration process, which is not efficient from a business point of view because of various commercial issues, some franchisors and franchisees go ahead and sign the franchise agreement first and deal with registration of the prospectus later, followed by registration of the signed franchise agreement. In practice, this approach seems to be acceptable provided that the parties then comply with the registration requirements and obtain a franchise registration certificate under each of their names.
A franchisee that has been granted the right to sub-franchise must have at least one company-owned operation before it can offer franchises to third parties.

14 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. According to Decree No. 16, this control relationship may be a blood relationship, an employment relationship or a shareholding relationship. This means that a franchisor cannot appoint one of its subsidiaries or affiliates as its franchisee in Indonesia. Regulation 53 also requires franchisees to cooperate with local small and medium-sized businesses as franchisees or suppliers, if they can satisfy the franchisor's requirements.

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 franchise regulations do not set a minimum or maximum number of outlets to be developed within a specified period. This is normally decided by agreement among the parties. However, Regulations 68 and 67 impose limitations on the number of outlets managed or owned by a franchisor and a franchisee. Regulation 68 allows franchisors and franchisees engaged in a modern store business to operate up to 150 company-owned outlets. Thereafter, they must appoint independent sub-franchisees. Meanwhile, Regulation 07 limits the number of self-managed or company-owned outlets for franchisors and franchisees in the food and beverage businesses (restaurants, bars and cafés) to up to 250 outlets. Any additional outlets must either be franchised or operated by way of cooperation with capital participation.

15 What is the compliance procedure for making pre-contractual disclosure in your country? How often must the disclosures be updated?

The disclosure document must be registered with the MOT for franchisees originating from both within Indonesia and outside Indonesia, following which, the franchisor or sub-franchisor will receive a franchise registration certificate (the STPW). The franchisor must provide the disclosure document at least two weeks before the execution of the franchise agreement to prospective franchisees. Although the regulations do not obliged franchisors to update their disclosure document, it is recommended to continuously send updates to the disclosure document to each prospective franchisee and the MOT. Regulation No. 53 requires a prospectus to be registered with the MOT from overseas to be notarised first by a notary public in the jurisdiction of the franchisor, and if possible, to then be processed by the Indonesian consulate or embassy in the home country of the franchisor. The franchisor must also obtain a reference letter from the relevant trade attaché or Indonesian consulate or embassy in the home country of the franchisor. This statement is a one-page letter confirming the details of the franchisor, such as its name and address, legal form or status, date of establishment, the trademark under franchise and the name and address of the prospective Indonesian franchisee. A certified Indonesian translation of a foreign-language disclosure document and its attachments must also be prepared.

16 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 sub-franchisor?

The franchise regulations are silent on this matter. However, before it enters the Indonesian market and appoints Indonesian parties to be its sub-franchisees, a master franchisee must be registered with the MOT. The master franchisee will then be deemed a sub-franchisor and therefore the provisions that apply to a franchisor will also apply to this master franchisee. For example, it must have its own disclosure document and obtain an STPW under its own name. See questions 15 and 17.

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

17 What information must the disclosure document contain? At least the following information must be provided in the disclosure document:

- the identity of the franchisor, including the information provided on the identity cards or passports of the shareholders, commissioners and directors (if the franchisor is a business entity);
- the legal business status of the franchisor, including information about the franchisor's business licence;
- the business history of the franchisor, including information regarding the establishment of the franchisor, its business activities and the development of the franchisor's business;
- the organisational structure of the franchisor, including the management hierarchy, from the commissioners, shareholders and management structure to the operating division;
- the audited balance sheet for the past two years;
- the number of franchise businesses, including the number of outlets owned by the franchisor;
- the list of franchisees; and
- the rights and obligations of:
  - the franchisor, such as the right to receive royalties and the obligation to provide continuous assistance to the franchisee; and
  - the franchisee, such as the right to use the franchisor's intellectual property rights or business characteristics and the obligation to maintain their confidentiality.

18 Is there any obligation for continuing disclosure?

As explained in question 15, the disclosure document does not have to be updated, but it is recommended to do so.

19 How do the relevant government agencies enforce the disclosure requirements?

There are no regulations regarding enforcement of the disclosure requirements, except for the registration of the disclosure document. The administrative sanction that will be imposed on the franchisor or franchisee, or both, for not complying with the disclosure document and franchise agreement registration requirements is initially a written warning. The written warning will be served up to three times and 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 comply with the registration requirement within two weeks of the third warning letter's expiry date.

In practice, a warning letter is sent to the franchise operation stating that the authorities consider it to be a franchise and that it should register as such; no meaningful sanctions are imposed for non-registration. It is very common for the authorities to write letters to those who may be seen or thought to be in breach of the regulations, but not, for example, to revoke their licences directly. In other areas, the authorities have often refused to provide approval or a licence until a certain action is taken or requirement satisfied.

20 What actions can franchisees take to obtain relief for violations of disclosure requirements? What are the legal remedies for such violations? How are damages calculated?

If the franchisee can cancel or rescind the franchise contract, is the franchisee also entitled to reimbursement or damages?

Franchise regulations provide no remedy for the franchisee. Any remedy it wishes to have should be provided in the franchise agreement. Article 1338 of the ICC allows parties to a commercial contract to contract freely as long as the contract is made in good faith and satisfies the requirements under article 1320 of the ICC. Therefore, the parties can fashion their own remedies in the contract, subject to limitations in the law. Basically, article 1320 of the ICC states that certain elements of a contract must be satisfied to establish a contractual arrangement in Indonesia, namely a mutual agreement between the parties, the legal capacity of the parties to enter into the contract, specific subject matter and a lawful purpose.

In the absence of contractual provisions to the contrary, general remedies available to a contracting party in the event of a breach of contract can arise from claims under articles 1256, 1243 and 1267 of the ICC.
Article 1236 requires the obligor to reimburse costs, losses and interest to the creditor if it has put itself in a situation in which it is unable to deliver the goods or if it is unable to properly maintain the goods.

Article 1245 explains that compensation for costs, losses and interest due to non-performance of an agreement is only due if the obligor, after being declared in default, continues to fail to perform, or if it has to deliver or make the goods and their delivery or performance is performed after the agreed to time limit.

Article 1267 states that the party against whom an agreement is breached can choose whether to force the defaulting party to comply with its obligations (if this is still possible) or to request the termination of the agreement, accompanied by compensation for costs, losses and interest.

To avoid difficulties in calculating or proving damages, the franchise agreement may state a certain fixed amount of money (ie, liquidated damages) to be paid to the non-defaulting party (article 1249 of the ICC). This means that the amount of compensation is agreed to before any actual losses are incurred. The consequence of such an agreement is that the agreed to amount must be paid in the event of non-performance, regardless of the actual losses and in fact, no evidence is required to prove the losses. Under article 1249, the creditor can claim either performance of the obligation or compensation, but not both.

However, under article 1209 of the ICC, judges may reduce the amount of the agreed to compensation if the contract has been performed in part. Jurisprudence shows that judges have reduced the amount of the agreed to compensation (even without any performance at all) on the grounds of decency and good faith.

The law limits what can be claimed in compensation. Compensation for default or non-performance is limited to losses that can be predicted and are directly caused by the default or non-performance (articles 1247 and 1248). Another limitation is with regard to a moratorium interest. Moratorium interest is interest that must be paid (as a sanction) because the obligor is in default. Article 1250 of the ICC states that in agreements that solely relate to the payment of money, the compensation for costs, losses and interest caused merely by a delay in payment may only consist of payment of the interest determined by law, without prejudice to any specific regulation. Furthermore, under article 1250, compensation for costs, losses and interest only needs to be paid from the day the claim is filed in the court until the day one which it is paid, unless determined otherwise by law.

The remedies specified in a contract are not the only or exclusive remedies to which a party is entitled in the event of a breach. Under article 1267 of the ICC on tort, a party can claim losses suffered outside any contractual relationship.

In practice, few cases brought under article 1265 have been successful. In most cases, the court either rejects or only accepts the claim in part (ie, it agrees that tort has been committed but the amount of compensation claimed cannot be fully justified). Also, claims under article 1265 cannot be combined with a remedy under the contract.

Statutory liability for negligence is recognised in Indonesia under both the Criminal Code and the ICC. The Criminal Code separates crimes resulting from an intended action and those resulting from negligence. Under article 1266 of the ICC, a person may be held liable, not only for losses caused by his or her action, but also for any losses caused by his or her negligence or carelessness.

In a franchise arrangement, how is liability for disclosure violations shared between franchisor and sub-franchisor? Are individual officers, directors and employees of the franchisor or the sub-franchisor exposed to liability? If so, what liability? There is no regulation on the sharing of liability. This should be agreed to between the franchisor and the sub-franchisor. Individual officers, directors and employees of the franchisor or the sub-franchisor should not be exposed to liability unless there is negligence or fault on their part. However, in legal proceedings, they are usually named as co-defendants.

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?

Other than franchise-specific rules on what disclosures a franchisor should make to a potential franchisee or a franchisee should make to a sub-franchisee regarding predecessors, litigation, trademarks, fees, etc, are there any general rules on pre-sale disclosure that might apply to such transactions?

What actions may franchisees take if a franchisor engages in fraudulent or deceptive practices in connection with the offer and sale of franchises? How does this protection differ from the protection provided under franchise sales disclosure laws?

Legal restrictions on the terms of franchise contracts and the relationship between parties in a franchise relationship

Are there specific laws regulating the ongoing relationship between franchisor and franchisee after the franchise contract comes into effect? The parties will have to comply with the franchise regulations and other laws or regulations related to the business, as well as the terms and conditions that have been agreed to under the franchise agreement. The signed agreement will bind the parties concerned and must be implemented in good faith.

Do other laws affect the franchise relationship? Franchises are exempt from the Anti-Monopoly Law (article 50B of the Anti-Monopoly Law). According to the Commission Guidelines under this law, the law does not apply to licence or franchise relationships. However, the commission has issued further guidelines under which the exclusion of franchise related agreements does not always apply, as they could contain provisions that would lead to monopolistic practices or unfair business competition.

Other laws or regulations may affect the franchise relationship. For example, regulations on import activities, food and drink-related regulations such as food registration and halal certification, consumer protection laws, zoning rules, advertising restrictions, etc.

Do other government or trade association policies affect the franchise relationship? The MOT’s policies and the Commission Guidelines should be taken into account when preparing a franchise arrangement.

In what circumstances may a franchisor terminate a franchise relationship? What are the specific legal restrictions on a franchisor’s ability to terminate a franchise relationship? In general, the parties should state in the franchise agreement the circumstances that may give rise to termination of the franchise agreement.
relationship. Under article 1266 of the ICC, a party may not unilaterally terminate an agreement without a ruling of the court with jurisdiction. If an agreement waives this article and contains a clause allowing unilateral termination, by reason of either breach or default or any other reason, one of the parties to the agreement may unilaterally terminate it. Consequently, it is advisable to include a waiver of article 1266. The franchise agreement may also be terminated by agreement between the parties.

29 In what circumstances may a franchisee terminate a franchise relationship?

See question 28.

30 May a franchisor refuse to renew the franchise agreement with a franchisee? If yes, in what circumstances may a franchisor refuse to renew?

Yes, the franchisor may refuse to renew the franchise agreement with the franchisee. As with termination, the parties should agree to the franchise renewal rights and their terms and conditions, and they should be stated in the franchise agreement. It is prudent to state in the agreement that the agreement will expire on a certain date, and either party may convey a written request for its renewal to the other party at least three or six months before the expiry of the agreement. Automatic renewal is not recommended as it makes it too easy to miss the expiry date of the current term, which may mean that the agreement will continue under the same terms and conditions. The franchisor should state that it may, at its sole discretion, refuse to renew the franchise. In the event of its renewal, the parties will sign a renewal agreement with the terms and conditions agreed to between them. However, it is recommended that the discontinuation of the franchise relationship (either by termination or non-renewal, or otherwise) be made amicably in order to secure a clean-break agreement or letter from the franchisee. This will allow the franchisor to appoint a new franchisee, if required, fairly easily.

31 May a franchisor restrict a franchisee’s ability to transfer its franchise or restrict transfers of ownership interests in a franchisee entity?

Yes, this restriction should be stated in the franchise agreement. The franchisor usually has these rights. The franchise agreement usually only allows the franchisee to transfer its franchise or undertake a transfer of ownership in the franchisee entity with the prior written approval of the franchisor. The aim of this restriction is to ensure the continued operation of the franchisee despite the transfer of the franchisor or transfer of ownership in the franchisee entity.

32 Are there laws or regulations affecting the nature, amount or payment of fees?

There are no specific laws or regulations affecting the nature, amount or payment of fees. See question 34.

33 Are there restrictions on the amount of interest that can be charged on overdue payments?

The parties may specify in the agreement the amount of interest to be charged on overdue payments. The underlying principle is the good faith of the parties. The aggrieved party can seek a reduction in the interest charged on overdue payments. The underlying principle is the good faith of the parties. The aggrieved party can seek a reduction in the interest charged on overdue payments. It should be remembered that Indonesia operates a civil law system. Unlike in the common law system, courts do not have to follow precedent. Each case is decided according to the presiding court’s interpretation of the law and determination of the facts. It is therefore difficult to predict how the courts will decide on specific matters.

34 Are there laws or regulations restricting a franchisee’s ability to make payments to a foreign franchisor in the franchisor’s domestic currency?

No, there is no law or regulation restricting a franchisee’s ability to make payments to a foreign franchisor in the franchisor’s domestic currency. However, note the requirements related to the purchase of foreign currency against the rupiah discussed in question 4.

Law No. 7 of 2011 regarding currency requires the rupiah to be used for any payments, financial transactions or the settlement of obligations in the territory of the Republic of Indonesia, except for:

- certain transactions for the implementation of the state budget;
- grants from or to Indonesia;
- international trade transactions, which include exports and imports of goods out of or into the Indonesian customs area, and the cross-border provision of services through cross-border supply and overseas consumption (such as an Indonesian citizen who is studying abroad);
- deposits in foreign currencies with Indonesian banks; or
- international financing.

Given the above, any transaction between two Indonesian entities in Indonesia is subject to the Currency Law, and therefore any payment must be made in rupiah. Meanwhile, any transaction between Indonesian entities and overseas entities such as a franchise agreement or technical services agreement can be categorised as an international trade transaction since the services are provided from overseas and may be classified as cross-border supply and therefore the fee chargeable may be in US dollars or any other foreign currency.

The sanction for a violation of this requirement is imprisonment for up to one year and a fine of up to 200 million rupiah. In addition, any recipient who refuses to accept payment in rupiah for the settlement of financial transactions in Indonesia is liable to up to one year in prison and a fine of up to 200 million rupiah, unless:

- it is in doubt about the genuineness of the money received;
- it has been agreed to in writing with the other parties to the agreement that payment will be made in foreign currency; or
- the payment is for one of the transactions specified in the previous paragraph.

35 Are confidentiality covenants in franchise agreements enforceable?

Yes, they are generally enforceable. The franchise agreement should state that the franchisor will be entitled to certain damages or to pursue certain sanctions in the event of a violation of the confidentiality covenants.

36 Is there a general legal obligation on parties to deal with each other in good faith? If so, how does it affect franchise relationships?

Yes, the ICC requires all agreements to be entered into in good faith. Article 338 of the ICC states that all agreements validly entered into shall serve as law for the parties to them. Agreements cannot be cancelled except by mutual agreement between the parties, or for reasons determined by law. All agreements must be implemented in good faith.

37 Does any law treat franchisees as consumers for the purposes of consumer protection or other legislation?

The Consumer Protection Law (Law No. 8 of 1999) defines consumers as users of goods and services for their own, their family members', or other persons' or other living creatures' purposes, not for trading. The law explains that consumers are end-users of the products and services. As franchisees are business agents, not end-users, they are not treated as consumers for the purposes of consumer protection.

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38 Must disclosure documents and franchise agreements be in the language of your country?

The disclosure document and the franchise agreement may be in a foreign language, but its Indonesian translation must be provided. Ideally, both the foreign and the Indonesian versions must be signed by the franchisor and franchisee.

In addition, Law No. 24 of 2009 on the National Flag, Language, Emblem and Anthem (the Language Law) requires the Indonesian language to be used in, among other things, agreements entered into by Indonesian parties. If the agreement involves foreign parties (such as a foreign franchisor and an Indonesian franchisee), the agreement can be executed in a dual language format (eg, Indonesian and the foreign language side-by-side), which will be treated the same as the original.

The Language Law does not provide any sanctions for a violation of the obligation to use the Indonesian language or any further explanations of what is meant by all versions being the same as the original (in the case of a dual-language agreement).

The Language Law was issued in 2009, and in theory, an implementing regulation should have been issued within two years. However, so far, it has not been issued. Pending this enabling regulation, it is still unclear what the legal consequence of having an agreement executed only in English will be or the choice of a foreign language in the event of any conflict between the Indonesian and the English versions, for example. Therefore, it is advisable to include a clause clearly confirming the parties’ agreement on this matter in the agreement. It can also be argued that an agreement that has been entered into binds the contracting parties as a law which should be implemented in good faith. In addition, the Indonesian translation of a foreign language franchise agreement is expected to be prepared by a sworn translator.

A precedent is provided by a court ruling on a civil case handed down in June 2012 based on the Language Law, under which a contract governed by Indonesian law but executed only in the English language was declared null and void. An appeal against this ruling was rejected by the Jakarta High Court and Supreme Court. Although Indonesia does not have a system of precedent as exists in certain common law jurisdictions and other Indonesian courts reviewing similar cases are not required to follow this ruling, the contracting parties should be aware of this possibility.

39 What restrictions are there on provisions in franchise contracts?

See question 40.

Governing law

An Indonesian franchise agreement must be governed by Indonesian law.

Business areas

Except in provincial capitals, a franchise business may not be conducted unless the municipality or area has been 'opened' specifically for franchise activities by the Ministry. Again, this is to protect smaller enterprises. The precise location of franchise activities (whether in a traditional market or in a modern shopping mall) is also regulated, as is the ability to appoint franchisees for the same products or services in adjacent sites in a particular location. A convenience store may be subject to the zoning restrictions depending on the size of the store, for example, a mini-market must be located at least 0.5 km away from the local market and on the side of the road.

Training programmes

A franchisor must provide its franchisees training in the form of operational management assistance, marketing, research and sustainable development. The following are the types of training that the franchisor should provide to its franchisees:

- education and training in the franchise management system, to help the franchisees to operate the franchise in good order and to make a profit;
- routine operational management assistance, so any operational errors can be remedied immediately;
- market development assistance through promotions using advertisements, leaflets, catalogues, brochures or participating in exhibitions; and
- market research and the development of products to be promoted, so that the products meet market needs and are accepted by the market.

The authorised agency will revoke the franchisor’s certificate if the franchisor fails to provide the above after receiving three consecutive warning letters, although it appears that this has never been tested in practice.

40 Describe the aspects of competition law in your country that are relevant to the typical franchisor. How are they enforced?

The Commission Guidelines indicate areas of concern to be taken into account when drafting franchise agreements. These areas include resale price maintenance, the procurement of goods or services from the franchisor or its appointees, the purchase of other goods or services from the franchisor, area restrictions and undertaking competitive business after the expiry of a franchise arrangement. In general, these are not prohibited, but the parties must make sure that the franchise arrangement does not create or result in monopolistic practices or unfair business competition. The Commission Guidelines cover the following.

Resale price maintenance

A franchisor may not fix the sales prices to be charged to customers by its franchisees. From the anti-monopoly perspective, fixing sales prices can lead to price uniformity among franchisees, and customers then have no choice. A franchise agreement containing a fixed sales price therefore violates the Anti-Monopoly Law. However, to maintain the economic value of the franchise business, the franchisor is allowed to recommend sales prices to its franchisee so long as the recommendation is not binding.

Procurement of goods or services from the franchisor or its appointees

A franchisor cannot require the franchisee to only procure goods or services from the franchisor or its appointees. An exemption from the Anti-Monopoly Law may apply if the purpose of the restrictions is to protect the franchisor’s reputation and to maintain the franchise. However, the franchisor cannot prevent the franchisee from purchasing similar goods or services from other sources if they meet the quality standards set by the franchisor.

Purchasing other goods and services

A franchise agreement that obliges the franchisee to purchase goods and services that are not related to the franchise from the franchisor is not exempt from the Anti-Monopoly Law.

Area restrictions

The purpose of an area restriction under a franchise agreement is usually to establish a franchise networking system and to determine the permitted activities of the franchisor and franchisee in the particular area. However, this restriction violates the Anti-Monopoly Law if the intention is to limit customers’ access to the franchised goods or services if the customers are domiciled outside the determined franchise area, or to establish market boundaries or assign a share of the market.
Non-compete provisions
Following the termination or expiry of a franchise agreement, a franchisor may prohibit the franchisee from engaging in the same business as the franchisor. This restriction is acceptable under the Anti-Monopoly Law as long as the purpose is to protect the intellectual property rights of the franchisor or to maintain the reputation of the franchise, in particular, if the franchisor has transferred its know-how. Several factors will be considered by the commission in deciding whether a non-compete period is acceptable, such as the technology that has been transferred and the total investment made. Under the Commission Guidelines, if the technology has entered the public domain and the investment so far has not been significant, the non-compete period would normally be one year.

Describe the court system. What types of dispute resolution procedures are available relevant to franchising?
The 1945 Constitution and relevant laws governing Indonesia’s judicial system (for example, Law No. 48 of 2009 on the Jurisdiction of the Courts of Justice) divide judicial authority between the Supreme Court and the Constitutional Court. The Supreme Court has jurisdiction over appeals against rulings of the general courts, religious courts, military courts and the State Administrative Court. Unlike other courts, the Constitutional Court is not supervised by the Supreme Court.

Indonesia also recognises several specialised courts: commercial courts, which rule on bankruptcy petitions and trademark infringements; children’s courts; human rights courts; industrial relations courts; fisheries courts, which operate under the general courts; and tax courts, which operate under the state administrative courts.

Commonly, a lawsuit is initiated by a plaintiff submitting a complaint to the chairman of the district court with jurisdiction over the defendant’s domicile. The plaintiff is then required to register the lawsuit with the Deputy Registrar of the district court. The losing party at district court level can appeal to the High Court. It may take a year or more for the High Court to issue its ruling. The losing party under a High Court decision may appeal against it to the Supreme Court. It can take three years or more for a final decision to be issued. Unless stated otherwise in the relevant law, a panel of judges consisting of at least three judges, one of whom acts as the presiding judge, will examine the lawsuit. The judgment must be delivered in open public court.

As well as through the courts, the parties may also settle their dispute by arbitration or an alternative dispute resolution method if they agree to do so. The law defines an alternative dispute resolution method as through an institution for the settlement of disputes or divergent views through an out-of-court procedure agreed to by the parties (ie, consultation, negotiation, mediation, conciliation or evaluation by experts). Foreign arbitral awards are enforceable in Indonesia. The enforcement of an arbitral award, whether domestic or foreign, requires an execution order to be issued by the relevant court.

Describe the principal advantages and disadvantages of arbitration for foreign franchisors considering doing business in your jurisdiction.
Theoretically, the principal advantages of arbitration for foreign franchisors are the following:
• the confidentiality of the dispute between the parties is guaranteed;
• procedural and administrative delays can be avoided;
• the parties can appoint an arbitrator who in their view has proper knowledge, experience and background in the matter in dispute;
• the parties can determine the choice of law for settlement of any dispute, as well as the arbitration process and venue (except in certain commercial transactions, such as franchise arrangements to which Indonesian law applies); and
• the decision resulting from arbitration can be implemented through a supposedly simple procedure.

However, there are certain disadvantages to arbitration over normal litigation, for example:
• while Indonesian arbitration law attempts to reduce the potential for delays in the enforcement of arbitral awards, there is a distinct danger that the tight procedural time limit for courts to hear appeals or for the disputing parties to prepare and make filings may result in hasty decisions and rushed drafting; and
• some uncertainty is caused by some of the provisions of the Arbitration Law (eg, the parties must try to resolve the dispute within 14 days before proceeding to an alternative dispute resolution method, but when the 14-day period commences or whether it can be extended is not stated).

Another example is where a party wants urgent injunctive relief in the event of default by the defaulting party. Some contracts provide for one or both parties to seek urgent relief from the courts. This has the obvious disadvantage that once a matter is before the court, it is very difficult to halt the action and the party bringing the action will have to face counterclaims, etc. Finally, in practice, it is often difficult to prevent another party taking a dispute to the courts even though the parties have chosen arbitration as the exclusive dispute resolution mechanism.

In what respects, if at all, are foreign franchisors treated differently from domestic franchisors?
Indonesian franchise regulations apply equally to foreign and domestic franchisors. Administrative requirements may differ, but in general foreign and Indonesian franchisors are not treated differently.
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