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Overview

1 What forms of business entities are relevant to the typical franchisor?

In Malaysia, a business may exist in a number of different forms, including sole proprietorships, partnerships (including a limited liability partnership) and companies or representative, regional or branch offices of foreign companies.

The principal form of business organisation that is most relevant and common to a typical franchisor would be a private limited company.

2 What laws and agencies govern the formation of business entities?

Where incorporation of a company is concerned, the relevant laws are the Companies Act 2016 and the Companies Regulations 2017 (2016 Act), which came into force on 31 January 2017 (save for certain provisions including corporate voluntary arrangements and judicial management), repealing the Companies Act 1965 (1965 Act). The relevant agency is the Companies Commission of Malaysia (SSM) (www.ssm.com.my).

3 Provide an overview of the requirements for forming and maintaining a business entity.

The 2016 Act has simplified the company incorporation and decision-making process by introducing Superform – a single, electronic incorporation template. All incorporation and registration procedures will be processed through SSM’s newly launched online portal, MyCoID 2016. A notice of registration will serve as conclusive evidence of incorporation. This is intended to reduce incorporation, maintenance and operational costs.

Briefly, the requirements for incorporating a company with the SSM and maintaining the company are as follows:

- the applicant must first apply to the SSM to confirm the availability of the proposed company name (section 27(1) of the 2016 Act);
- if the proposed name is available, the application will be approved and the name will be reserved for the applicant for a period of 30 days (instead of three months under the 1965 Act); and
- the applicant must then lodge an application containing the following particulars:
  - the name of the proposed company;
  - the status of whether the company is private or public;
  - the nature of business of the proposed company;
  - the proposed address of the registered office;
  - the name, identification, nationality and the ordinary place of residence of every person who will be a member of the company and where any of these persons is a body corporate, the corporate name, place of incorporation, registration number and the registered office of the body corporate;
  - the name, identification, nationality and the ordinary place of residence of every person who will be a director;
  - the name, identification, nationality and the ordinary place of residence of the secretary;
  - in the case of a company limited by shares, the details of class and number of shares to be taken by the member; and
  - any other information that the Registrar of Companies may require.

In short, the key changes of the 2016 Act include the following:

- companies are no longer required to state their authorised share capital;
- introduction of single member or single director company;
- additional memorandum and articles of association or constitution;
- abolition of the requirement for private companies to hold an annual general meeting;
- power of members to require circulation of statements;
- migration towards no par value regime;
- introduction of members’ right for management review;
- dividends can only be distributed out of profits and are only allowed if solvency test is met;
- abolition of the maximum age for directorship;
- statutory declaration by promoters or directors to be replaced with statement of compliance; and
- increased sanctions on directors and secretaries for breaches under the 2016 Act, which include heavier fines and longer terms of imprisonment.

4 What restrictions apply to foreign business entities and foreign investment?

Generally, a foreign company cannot carry on business in Malaysia unless it incorporates a company as its subsidiary, sets up a branch office or registers a representative office in Malaysia. In certain circumstances, a foreign company may wholly own a Malaysian company; for example, if the foreign company has been granted Multimedia Super Corridor status or has been granted the status of International Procurement Centre, Operational Headquarters or other special statuses which can be granted by various ministries.

As of 1 December 2004, all proposals for foreign involvement in distributive trade must obtain the approval of the Committee on Distributive Trade under the Ministry of Domestic Trade, Co-operatives and Consumerism (the Committee).

The Guidelines for Foreign Participation in the Distributive Trade Services (the Guidelines) include:

- opening of new branches;
- relocation or expansion of existing branches or outlets;
- buying or taking over of other operators’ outlets; and
- purchase of land, premises and assets prior to obtaining the approval or licence from the local authority to operate distributive trade activities.

Distributive traders include wholesalers, retailers, franchise practitioners, direct sellers, product manufacturers and suppliers who channel their goods in the domestic market and commission agents or other representatives, including those of international trading companies of all nationalities.

The Guidelines impose a general requirement that all proposals for foreign participation in distributive trade must obtain the approval of the Committee. In line with the national development policy, the Committee requires at least 30 per cent bumiputra participation for hypermarkets.

One of the said approvals is known to many as a wholesale and retail trade (WRT) licence, which must be obtained by all foreign-owned companies dealing in the wholesale, retail, trading, import or export, restaurant and franchise businesses before they can operate in...
Malaysia. In order for a foreign company to apply for a WRT licence, the company must have at least a minimum paid-up capital of 1 million ringgit and it will take around one to two months for the WRT licence to be processed.

It should be noted that the Guidelines provide that all franchise businesses with foreign equity must be registered locally under the 2016 Act.

5 Briefly describe the aspects of the tax system relevant to franchisors. How are foreign businesses and individuals taxed?

All of a company’s or individual’s income that is accrued in, derived from or remitted to Malaysia is liable to tax. Nevertheless, income derived from outside Malaysia and remitted to Malaysia by resident companies (except those involved in the banking, insurance, air and sea transportation business), non-resident companies and non-resident individuals are exempted from tax. A corporation is resident in Malaysia if its management and control are exercised in Malaysia.

The standard corporate tax rate is 24 per cent, while the rate for resident small and medium-sized companies (namely companies incorporated in Malaysia with paid-up capital of 2.5 million ringgit or less is 18 per cent on the first 500,000 ringgit with effect from year of assessment (YA) 2015, with the balance being taxed at the 24 per cent rate. For YA 2017 and YA 2018, companies will be eligible for a reduction of between 1 and 4 per cent on the standard tax rate for a portion of their income if there is an increase of 5 per cent or more in the company’s chargeable income, compared with the immediately preceding YA. Income tax is imposed at progressive rates up to 28 per cent for resident individuals. Non-residents are taxed at a flat rate of 28 per cent.

Apart from income tax, there are other direct taxes such as stamp duty and real property gains tax, and indirect taxes such as excise duty, import duty and export duty.

A withholding tax is charged to non-resident companies or individuals that derive income from a Malaysian source on payments for services rendered, technical fees or other payments including royalties and interest (at 10 and 15 per cent respectively).

The Goods and Services Tax (GST) under the Goods and Services Tax Act 2014 (GST Act) came into force on 1 April 2015 at the rate of 6 per cent, replacing the current sales and service tax regime. GST is a multistage broad-based consumption tax that is chargeable on all the taxable supplies of goods and services in Malaysia except those specifically exempted. GST is also charged on importation of goods and services into Malaysia. Only businesses registered under the GST Act can charge and collect GST.

6 Are there any relevant labour and employment considerations for typical franchise arrangements? 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?

The Employment Act 1955 governs all matters relating to employment. It applies to all employees whose wages do not exceed 2,000 ringgit and it will take around one to two months for the WRT licence to be processed.

It should be noted that the Guidelines provide that all franchise businesses with foreign equity must be registered locally under the 2016 Act.

The Franchise Act 1998 (FA) expressly provides for the protection of confidential information (see question 5).

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

Most franchised outlets are leased or tenanted properties rather than being owned by franchisees or franchisors. In Malaysia it is common for owners to enter into a tenancy agreement for a period not exceeding three years so as to avoid having to register the lease at the relevant land office. One has to fall back on general contract law – the Contracts Act 1950 – for much of the Malaysian law governing landlords and tenants.

Laws and agencies that regulate the offer and sale of franchises

9 What is the legal definition of a franchise?

Under section 4 of the FA (as amended by the Franchise (Amendment) Act 2012), the statutory definition of a franchise is a contract or an agreement, either expressed or implied and whether oral or written, between two or more persons, by which:

- the franchisor grants to the franchisee the right to operate a business according to the franchise system as determined by the franchisor during a term to be determined by the franchisor; and
- the franchisor grants to the franchisee the right to use a mark, or a trade secret, or any confidential information or intellectual property owned by the franchisor or relating to the franchisor, and includes a situation where the franchisor who is the registered user of, or is licensed by another person to use, any intellectual property grants such right that it possesses to permit the franchisee to use the intellectual property; and
- in return for the grant of rights, the franchisee may be required to pay a fee or other form of consideration.

In order to fall within the purview of the FA, the arrangement must consist of all of the above elements. This arrangement will then be regarded as a franchise, whether it is called a franchise or otherwise.
10 Which laws and government agencies regulate the offer and sale of franchises?
The FA, as amended by the Franchise (Amendment) Act 2012 came into force on 1 January 2013. The Franchise Development Division of the Ministry of Domestic Trade, Co-operatives and Consumerism (MDTCC) is the governmental agency that regulates the offer and sale of franchises and approval or registration of franchisors and franchisees in Malaysia.

11 Describe the relevant requirements of these laws and agencies.
The Malaysian government has long been aware that franchising is one of the fastest ways to create and increase the number of local entrepreneurs and promote growth in the franchise industry in Malaysia. Essentially enacted to facilitate and monitor the growth of the franchise industry, the FA applies throughout Malaysia and to the sale of any franchise in Malaysia. Pursuant to the FA, franchisors, master franchisees and foreign franchisees are required to seek approval from or register with (or both) the registrar of franchises before they can offer to sell or buy franchises in Malaysia.

Under the Franchise (Amendment) Act 2012, a franchisee of a foreign franchisor must register the franchise before commencing the franchise business. A franchisee of a local franchisor or a local master franchisee must register the franchise within 14 days from the date of signing the franchise agreement.

12 What are the exemptions and exclusions from any franchise laws and regulations?
If a person is able to demonstrate that its business model does not fall within the definition of a franchise, in that it does not satisfy all the ingredients in the definition of the franchise, such business would not be covered by the provisions and purview of the FA.

Under the Franchise (Exemption) Order 2004, any person who has sold a franchise in Malaysia or to any Malaysian citizen prior to the commencement of the FA (8 October 1999) would be exempted from complying with section 54, namely the requirement to submit an application to the registrar.

Pursuant to section 58 of the FA, the minister may, by order published in the Malaysian Gazette, exempt, subject to such conditions as he or she deems fit to impose, any person or class of persons or business or industry from any or all of the provisions of the FA. To date, the only industry that is exempted under this provision is the petroleum industry.

Under the Franchise (Exemption) Order 2001 (PU(A) 27/2001), the minister has exempted from the provisions of the FA the petroleum industry’s franchising:
• a petrol station business; and
• any other business operating together with the petrol station business referred to above, subject to the condition that the business operating together with such petrol station business:
  • is operated in the same premises as the petrol station; and
  • is franchised by the same petroleum industry franchising the petrol station business.

13 Does any law or regulation create a requirement that must be met before a franchisor may offer franchises?
One requirement that is highly unpopular among franchisors and local master franchisees is that they must operate their own outlets profitably for at least three years before they are permitted to appoint sub-franchisees. While this requirement is not expressly provided in the FA, or any of the regulations, the authorities have taken the view that it is one of the prescribed requirements under law due to section 18 of the Disclosure Document, which requires the franchisors or master franchisees to submit audited financial statements for the past three years.

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?
Although the FA does not expressly restrict the manner in which a franchisor recruits franchisees or selects its suppliers, the government does exercise some form of control and impose certain conditions (when granting its approval during the approval application or registration process). For instance, if the territorial area granted to a potential franchisee is considered to be too small or restrictive, the Registrar would request that the applicant to extend the territorial right to a larger area (usually by reference to a radius in kilometres). The Registrar of Franchises would also require the franchisor to submit a list of its suppliers in granting approvals. If the franchisor has not shown profitability or healthy growth in their financial statements for the franchise business, the Registrar is likely to refuse the approval application or registration on the basis that the franchisor is not ready to sell its franchise systems to franchisees in Malaysia.

15 What is the compliance procedure for making pre-contractual disclosure in your country? How often must the disclosures be updated?
In the case of a sub-franchising structure (namely where the foreign franchisor appoints a local master franchisee who will in turn appoint sub-franchisees in Malaysia), the local master franchisee is the one providing pre-sale disclosures to sub-franchisees. The local master franchisee must disclose the fact that it is a master franchisor, not the franchisor of the franchise in question, and that the trademarks belong to the foreign franchisor. As the foreign franchisor should have submitted an application for the franchise prior to the sale of the franchise to the master franchisee pursuant to section 54 of the FA, all relevant information pertaining to its operations and experiences would have been provided to the Registrar during such application. Section 16 of the FA (as amended by the Franchise (Amendment) Act 2012) provides that an updated disclosure document must be filed annually by the franchisor, within six months of the end of the financial year of the franchise business.

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?
A local franchisor must submit to a franchisee a copy of the franchise agreement, together with the disclosure documents, at least 10 days before the franchisee signs the franchise agreement with the franchisor. Basically, disclosure documents provide a full overview of the franchise business system that will be franchised to the franchisee. A franchisor’s failure to submit such documents is an offence under the FA. If there is any material change in the disclosure documents, they must be amended and filed with the Registrar of Franchises. The franchisor must submit an annual report with the Registrar of Franchises within six months of the end of the financial year of the franchise business, failing which is an offence. The report must contain updated disclosure documents.

17 What information must the disclosure document contain?
The disclosure documents contain a large amount of information, including, without limitation, the following:
• name, business address and type of business, including the franchisor’s business experience;
• details of the intellectual property rights granted to the franchisee;
• types and amount of fees imposed on franchisees;
• other financial obligations, including advertising, training or service fees payable;
• whether the franchisee is required to purchase equipment or products from the franchisor or from a source designated by the franchisor and, if so, to identify the source;
• the obligations of the franchisor, prior to operating or during operations, in determining the business site;
• the territorial rights granted to the franchisee and circumstances when the boundary of the territory may be altered;
• the franchise term, terms for renewal and termination of agreement by the franchisor or franchisee, and the parties’ obligations upon termination; and
• the franchisor is required to submit audited financial statements for the past three financial years and financial forecasts for five years. The requirement for financial forecasts for five years (instead of three years previously) were amended pursuant to the Franchise (Forms and Fees) (Amendment) Regulations 2007, which came into operation on 15 December 2007.
18 Is there any obligation for continuing disclosure?

Section 15 of the FA provides that a franchisor must submit to a franchisee a copy of the franchise agreement and disclosure documents at least 10 days before the franchisee signs the agreement with the franchisor. This seems to suggest that if the franchisees were to sign new franchise agreements (for the renewed terms) with the current franchisee, they would have to provide such disclosure documents.

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

It is a criminal offence under the FA to make false statements of material fact or to omit a material fact that renders the statement misleading in the disclosure documents. It is also a criminal offence if the franchisor fails to submit copies of the disclosure documents to the franchisee at least 10 days before the franchisee signs the franchise agreement. Failure to update the disclosure documents when submitting an annual report would also amount to an offence.

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? In the event of violations of disclosure requirements, the franchisees may lodge a complaint against the franchisor with the Registry of Franchises. A contract induced by misrepresentation is voidable at the choice of the innocent party. The innocent party may rescind the contract by giving notice to the other party and any party who has received any advantage under the contract is bound to restore it, or compensate the other party for it. The general rule governing the extent of damages payable is laid down in section 74 of the Contract Act 1950:

When a contract has been broken, the party who suffers by the breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from the breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it.

21 In the case of sub-franchising, 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?

Unless the franchisor is a party to the contract between the master franchisee and sub-franchisees, the franchisor will not be liable to the sub-franchisees as there is no privity of contract between them. Nevertheless, in most agreements between the franchisor and sub-franchisor, there would be an appropriately drafted warranty and indemnity clauses to address this issue. Individual officers, directors and employees of the franchisor or sub-franchisor, as the case may be, will not be liable unless they are personally party to the contract or if the other party is able to lift the corporate veil to impute liabilities to them personally.

22 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?

Apart from the FA, the provisions in the Contracts Act 1950 would be relevant and may affect the offer and sale of franchises.

23 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?

There is a requirement to provide the franchisee with the disclosure documents and the franchisee’s right of termination under section 18(5) of the FA during the cooling-off period, as well as a provision in section 37 of the FA that provides that a person who, whether directly or indirectly, makes any untrue statement of a material fact or omits to state a material fact that renders his or her statement to be misleading commits an offence. Apart from this, no other general obligations for pre-sale disclosure apply to franchise transactions.

24 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?

If the franchisor engages in any act, practice or course of business that operates or would operate as a fraud or deceit upon any person in relation to an offer to sell or a sale of a franchise, the franchisor commits a criminal offence under the FA that will entitle the franchisee to lodge a complaint against the franchisor with the Registry of Franchises. If convicted, the franchisor may be liable for a maximum fine of RM250,000 or to imprison for a term not exceeding five years. Further, the court may declare the franchise agreement null and void and may order the franchisor to refund any payments obtained from any franchisee or prohibit the franchisor from making any new franchise agreement or appointing any new franchisee.

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

25 Are there specific laws regulating the ongoing relationship between franchisor and franchisee after the franchise contract comes into effect?

The FA is the most specific and relevant law. The contractual relationship of the parties would also be governed by the contractual terms of the franchise agreement and accordingly the provisions of the Contracts Act 1950 would be relevant.

26 Do other laws affect the franchise relationship?

The Contracts Act 1950 also affects the franchise relationship. In addition, the provisions of the Competition Act 2010 should be taken into account.

27 Do other government or trade association policies affect the franchise relationship?

As well as the policies expounded by the Franchise Development Division of the Ministry of Domestic Trade, Cooperatives and Consumerism, other government policies such as the Distributive Trade Guidelines may have an impact on the franchise industry and franchise relationship. The Ministry of Domestic Trade, Cooperatives and Consumerism launched the National Franchise Development Blueprint 2012–2016 (NFDB), which is a long-term development plan to further develop the franchise industry. The NFDB has three objectives:

- to evaluate the franchise industry development based on main indicators (sales, employment and entrepreneur participation);
- to develop current policy, strategy and development programmes; and
- to determine the direction of the national franchise industry towards the goal of Malaysia being the franchise hub in South East Asia by 2020.

The Malaysian Franchise Association (MFA) was formed in 1994 to support the implementation of government programmes to promote entrepreneurship through franchising. The MFA serves as a resource centre for current and prospective franchisors and franchisees, as well as for the media and public. The MFA provides input and liaises with government departments and agencies on matters concerning franchising.
As well as setting guidelines and standards of ethical practice among its members, it serves as a forum through which expertise and experiences of members may be exchanged. The MFA also conducts seminars, exhibitions and educational programmes on franchising.

Perbadanan Nasional Berhad (PNS) is an agency under the MDTCC, with the mandate to lead the development of Malaysia's franchise industry. The PNS aims to develop the franchise industry while increasing the number of franchise entrepreneurs through its expertise in providing quality services and products. The PNS also offers various training and programmes for franchisees, including the Franchise Academy, which conducts various franchise-related training programmes.

28 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?

A franchisor may only terminate a franchise relationship under certain circumstances prescribed by the FA. For instance, section 31 of the FA provides that no franchisor shall terminate a franchise agreement before the expiration date, except for good cause.

'Good cause' includes:

- the franchisee's failure to comply with any terms of the franchise agreement; and
- the franchisee's failure to remedy the breach committed within the period stated in a written notice given by the franchisor, which shall not be less than 14 days, for the breach to be remedied.

Good cause also includes - without the requirement of notice and an opportunity to remedy the breach - instances in which:

- the franchisee voluntarily abandons the franchised business;
- the franchisee is convicted of a criminal offence which substantially impairs the goodwill associated with the franchisor's mark or other intellectual property; or
- the franchisee repeatedly fails to comply with the terms of the franchise agreement.

In addition, section 32 of the FA may restrict the franchisor's ability to terminate a franchise relationship in that a franchisor commits an offence if it refuses to renew a franchise agreement or extend a franchise term without compensating a franchisee either by a repurchase or by other means at a price to be agreed between the franchisor and the franchisee, after considering the diminution in the value of the franchised business caused by the expiration of the franchise where:

- the franchisee is barred by the franchise agreement, or by the refusal of the franchisor at least six months before the expiration date of the franchise agreement, to waive any portion of the franchise agreement which prohibits the franchisee from continuing to conduct substantially the same business under another mark in the same area subsequent to the expiration of the franchise agreement; or
- the franchisee has not been given written notice of the franchisor's intention not to renew the franchise agreement at least six months prior to the expiration date of the franchise agreement.

Notwithstanding these provisions of the FA, a franchise term may be terminated before the expiry of the minimum term of five years in the following circumstances:

- where both parties mutually agree to terminate the franchise agreement; or
- where the court has decided that there are certain conditions in the franchise agreement that merit the agreement being terminated earlier than the minimum term.

Nothing in the FA precludes the franchisor from taking over and operating the business formerly operated by the franchisee after the franchise agreement has been terminated or has expired.

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

Section 31 of the FA (as amended by the Franchise (Amendment) Act 2012) expressly provides for circumstances in which a franchisee may terminate a franchise relationship. It is now clear that the rights of the franchisee to terminate the relationship would be based on good causes as provided to the franchisor, as provided in 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?

The franchisor may refuse to renew the franchise agreement with a franchisee in the following circumstances:

- the franchisee has breached the terms of a previous franchise agreement; or
- the franchisee fails to give written notice to the franchisor to renew the term.

Unless the franchisor is able to establish either one of the above circumstances, it appears from section 34 of the FA that the franchisor must renew the franchise agreement to another period if the franchisee has applied for such renewal. It should also be noted that the franchise agreement for the renewed term must contain conditions which are similar or not less favourable than the conditions in the current franchise agreement. The term ‘another period’ in this provision seems to suggest that the renewed period for a franchise agreement based on similar or no less favourable terms is limited to one additional term from the initial term.

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

Yes, provided that such restrictions are contained in the franchise agreement.

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

Although there is no express provision in the FA or any other law affecting the nature, amount or payment of fees, there is a general provision in the FA that provides that a franchisor and a franchisee, in their dealings with one another, shall avoid the following conduct:

- substantial and unreasonable overvaluation of fees and prices;
- conduct that is unnecessary and unreasonable in relation to the risks to be incurred by one party; and
- conduct that is not reasonably necessary for the protection of the legitimate business interests of the franchisor, franchisee or franchise system.

In addition to the above general provision, if a franchisor requires the franchisee to make payment of the franchise fee before signing the franchise agreement, including a payment which is part of a franchise fee, the franchisor must state in writing the purpose of the payment and the conditions for use and refund of the monies. If the franchise agreement is terminated during the cooling-off period, the franchisor must refund all monies, including the initial fees paid by the franchisee, after deducting the reasonable expenses incurred to prepare the franchise agreement for the franchisee. The franchisor would commit a criminal offence if it fails to do so.

If the fees or other charges imposed by the franchisor are, in the Registrar's opinion, unreasonably or unjustifiably high, the Registrar may seek further information or explanations from the franchisor before the application or registration is approved or granted.

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

The amount of interest charged on overdue payments should not be excessively high or it may not be recoverable.
34 Are there laws or regulations restricting a franchisee's ability to make payments to a foreign franchisor in the franchisor's domestic currency?

There is no restriction on payments by a franchisee to a foreign franchisor in the franchisor's domestic currency (foreign currency).

35 Are confidentiality covenants in franchise agreements enforceable?

Yes, they are enforceable. In addition, section 26(1) of the FA provides that a franchisee must give a written guarantee to a franchisor that the franchisee, including its directors, the spouses and immediate family of the directors (as inserted by the Franchise (Amendment) Act 2012) and its employees may not disclose to any person any information contained in the operation manual or obtained while undergoing training organised by the franchisor during the franchise term and for two years after the expiration or earlier termination of the franchise agreement. Failure to provide such a written guarantee or to comply with the guarantee provided is an offence. Apart from being an offence under the FA, in the event of the franchisee breaching the confidentiality obligations, the franchisor may commence civil proceedings or proceedings regarding breach of the franchise agreement.

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?

Under the provisions of the FA, it is provided that a franchisor and a franchisee shall act in an honest and lawful manner and shall endeavour to pursue the best franchise business practice of the time and place. Nevertheless, failure to comply with such provisions is not an offence.

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

There is no law (including the Trade Descriptions Act 2011 and Consumer Protection Act 1999) that treats franchisees as consumers for the purposes of consumer protection.

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

Disclosure documents and franchise agreements may be in English. The Franchise Development Division expects a translated copy of the franchise agreement in Bahasa Malaysia to be submitted for approval by the local franchisors.

39 What restrictions are there on provisions in franchise contracts?

Pursuant to the FA, there are various restrictions in relation to such provisions in the franchise contracts. They include, without limitation, the following:
- the duration of the franchise agreement must be at least five years;
- the franchisee must give a written guarantee that it and its employees will not carry on any other business similar to the franchise business during the franchise term and for two years after the expiry of the franchise agreement; and
- the franchisee must not unreasonably and materially discriminate between franchisees where charges are offered or made for franchise fees, royalties, goods, services, equipment, rentals or advertising services, if such discrimination will cause competitive harm to the franchisees.

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

The Malaysian Competition Act 2010 (CA) came into force on 1 January 2012. The Malaysia Competition Commission (MyCC) is an independent body established under the Competition Commission Act 2010 to enforce the CA. MyCC issued numerous guidelines that came into force in 2012, including the Guidelines on Anti-Competitive Agreements and Market Definition that set out a non-exhaustive list of factors and circumstances that MyCC may consider in deciding whether certain agreements are anticompetitive. These guidelines are non-exhaustive and not a substitute for the CA or any regulations made thereunder and may be revised should the need arise. In applying these guidelines, the facts and circumstances of each case will be considered. MyCC has indicated that it has plans to issue specific guidelines dealing with franchise agreements but no specific timeline has been given.

The CA prohibits two broad categories of anticompetitive activities: 'anti-competitive agreements' and 'abuse of a dominant position'. A franchise agreement, which is a vertical agreement, would be prohibited by the CA if it has the object or effect of significantly preventing, restricting or distorting competition in any market for goods or services (section 4(1) of the CA). Towards this end, MyCC will not just examine the common intentions of the parties to an agreement but will also assess the aims pursued by the agreement in the light of the economic context of the agreement. If the object of an agreement is highly likely to have a significant anticompetitive impact, then MyCC may find the agreement to have an anticompetitive object. If an anticompetitive object is not found, the agreement may still breach the CA if there is an anticompetitive effect. In general and as a starting point, MyCC will adopt the following basis for assessing whether an anticompetitive effect is 'significant'. Anticompetitive agreements will not be considered significant if (paragraph 3.4 of the Guidelines on Anti-Competitive Agreements):
- the combined market share of the parties to the agreement is less than 20 per cent of the relevant market; and
- the parties to the agreement are not competitors and their individual market share in any relevant market is not more than 25 per cent.

It should be noted that the CA does not apply to agreements that comply with legislative requirements. Thus, if certain provisions in the franchise agreements are inserted to comply with the FA (for example, the provision against the franchisee in conducting a similar business during the franchise term and for two years thereafter), arguments could be made that they are not anticompetitive. Apart from these guidelines, and given that the CA came into force in 2012, there are no decisions that would be instructive as to how MyCC or the Malaysian courts would consider various contractual restrictions in franchise agreements. In applying these guidelines, the facts and circumstances of each case will be considered.

41 Describe the court system. What types of dispute resolution procedures are available relevant to franchising?

The Malaysian legal system is based substantially on the English legal system and the principles of common law. English judicial decisions and other Commonwealth judicial decisions are considered by the Malaysian courts, but only as a persuasive rather than conclusive authority. Although Malaysia is federally constituted, its judicial system is a single-structured system consisting of superior and subordinate courts. The superior courts are the High Court of Malaya, the High Court of Sabah and Sarawak and the Court of Appeal. The subordinate courts are the magistrates' courts and the sessions courts. The Federal Court is the highest judicial authority in Malaysia and is the final court of appeal.

The law offers equal protection for foreigners and foreign-owned companies. Commercial disputes may be resolved by arbitration. Malaysian law gives effect to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Unlike arbitration, which enjoys statutory recognition (the Arbitration Act 2005 came into force on 15 March 2006 and repealed the Arbitration Act 1952 and the Convention on the Recognition and Enforcement of Foreign Arbitral Awards Act 1985), there is no statute providing for dispute resolution by way of mediation, as is found in some other jurisdictions. Nevertheless, in recent times mediation has been increasingly encouraged as an alternative mechanism for dispute resolution.

The Registrar of Franchises has recently adopted a practice that would require franchise agreements to incorporate a mediation clause.

42 Describe the principal advantages and disadvantages of arbitration for foreign franchisors considering doing business in your jurisdiction.

Arbitration is often promoted and considered as better and more efficient than litigation when resolving franchise disputes, saving both money and time. Arbitration's rules of evidence and procedures are more relaxed and simple, which usually means it takes less time and less money to bring a franchise dispute to resolution.
It is particularly attractive for foreign franchisors, as the proceedings and documents can be conducted in English. As well as flexibility regarding the choice of arbitration location, hearing dates can be scheduled around the needs and availability of the parties involved – unlike trial dates, which are fixed by the courts and beyond the control of those involved. Arbitration proceedings are generally held in private, and parties keep the proceedings and terms of the final resolution confidential.

Despite its many benefits, arbitration may not always be the best option. In certain circumstances, it may have various drawbacks and shortcomings that do not exist in litigation. The costs may be higher than anticipated, as the arbitrators’ fees, administrative fees and other expenses to be borne by the parties are higher than those incurred in litigation. The arbitrator’s decision-making power is a more discretionary and flexible decision-making power than a judge’s and the hearing is private, meaning the ramifications of choosing the wrong or unskilled arbitrator could be more serious. The less well-defined rules and fewer procedural safeguards adopted in arbitration may sometimes result in mistakes. Owing to the arbitrator’s final and binding decision being generally unappealable (except in special circumstances), the decision can result in serious and unfortunate repercussions for one of the parties involved.

In what respects, if at all, are foreign franchisors treated differently from domestic franchisors?

Although the requirements for registration under the Franchise Act 1998 differ between foreign and local franchisors, the recent trends seem to show that the MDTCC has adopted a more stringent approach where foreign franchisors are concerned. Under the section 54 approval application, a foreign franchisor is now required to provide as much information and data as a local franchisor before it is approved to appoint franchisees in Malaysia, in order to create a level playing field for these players. Such information and documents include, without limitation, its detailed profile, extent of experience and knowledge in the franchised business, the total number of franchise outlets globally, initial franchise investment costs and certified true copies of audited accounts for the past three years. A foreign franchisor does not have to submit a disclosure document as yet though it does appear that the information and documents submitted are similarly extensive.
Acquisition Finance
Advertising & Marketing
Agribusiness
Air Transport
Anti-Corruption Regulation
Anti-Money Laundering
Arbitration
Asset Recovery
Automotive
Aviation Finance & Leasing
Banking Regulation
Cartel Regulation
Class Actions
Commercial Contracts
Construction
Copyright
Corporate Governance
Corporate Immigration
Cybersecurity
Data Protection & Privacy
Debt Capital Markets
Dispute Resolution
Distribution & Agency
Domains & Domain Names
Dominance
e-Commerce
Electricity Regulation
Energy Disputes
Enforcement of Foreign Judgments
Environment & Climate Regulation
Equity Derivatives
Executive Compensation & Employee Benefits
Financial Services Litigation
Fintech
Foreign Investment Review
Franchise
Fund Management
Gas Regulation
Government Investigations
Healthcare Enforcement & Litigation
High-Yield Debt
Initial Public Offerings
Insurance & Reinsurance
Insurance Litigation
Intellectual Property & Antitrust
Investment Treaty Arbitration
Islamic Finance & Markets
Labour & Employment
Legal Privilege & Professional Secrecy
Licensing
Life Sciences
Loans & Secured Financing
Mediation
Merger Control
Mergers & Acquisitions
Mining
Oil Regulation
Outsourcing
Patents
Pensions & Retirement Plans
Pharmaceutical Antitrust
Ports & Terminals
Private Antitrust Litigation
Private Banking & Wealth Management
Private Client
Private Equity
Product Liability
Product Recall
Project Finance
Public-Private Partnerships
Public Procurement
Real Estate
Restructuring & Insolvency
Right of Publicity
Securities Finance
Securities Litigation
Shareholder Activism & Engagement
Ship Finance
Shipbuilding
Shipping
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Tax Controversy
Tax on Inbound Investment
Telecoms & Media
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