



India: Legal and Regulatory Aspects of Doing Business in the Franchising Industry

Manjushree Phookan
July 09

Summary

The franchising industry is in its early stage of development in India though it is increasingly becoming a popular business model. India as yet does not have a specific legislation regulating franchise arrangements. As a result, franchising in India is governed by a number of different statutes and regulations rather than a single comprehensive law. There are various laws in India which impact the relationship between the franchisors and franchisees. Some of these laws include intellectual property laws, taxation, labor regulations, competition laws, property, exchange control, and consumer protection. A clear understanding of the laws related to the business of franchising in India is vital for a U.S. franchisor planning to enter the Indian market.

Market Demand

India's nascent franchising sector continues to boom at an impressive rate of 30 percent and is considered India's second fastest-growing industry. Though the current economic downturn could slow-down the growth temporarily, the avid interest in franchises in India is expected to increase over the next two to three years. With an investment of \$1.1 billion and sales turnover of \$2.7 billion, over 70 international franchise operations are successfully operating in India. Franchising in India is fast becoming the business model of choice, most noticeably in the food & beverage, education, and professional services sectors. Franchising currently accounts for three percent of India's total organized retail market. The top prospects for U.S. firms include specialized food and restaurant services, education & training, garments and apparel, stationery and gift shops, entertainment, professional services, fitness/health and wellness.

Market Data

Since there are no specific laws governing franchising in India, a franchise agreement is governed by several different laws and regulations. A franchise agreement is primarily a contract between the franchisor and the franchisee. The first applicable law is the [Indian Contract Act of 1872](#), which governs contracts in India. The Indian Contract Act, 1872 and the [Specific Relief Act of 1963](#), which provides for both specific enforcement of agreements in a contract and remedies in the form of damages for breach of contract, will govern a franchise agreement. Other laws that also impact franchising in India include:

Competition law: In India, laws to prevent monopolistic, restrictive and unfair trade practices that adversely affect free competition in the market are covered by Part A of the [MRTP Act of 1969](#).

Consumer protection law: The remedies available to Indian consumers for loss and injury suffered as a result of sub standard products and deception are covered by the [Consumer Protection Act of 1986](#) and Part B of the MRTP Act, 1969.

Intellectual Property laws: Indian laws offer adequate protection to trademarks or brand names as well as copyright and designs of a foreign franchisor. However, weak enforcement is an issue in India. Large-scale copyright piracy, especially in the software, optical media, and publishing industries continues to be a major problem. Adequate laws do not, due to ineffective or nonexistent enforcement, entail good IPR practices in India. [The Trademarks Act, 1999](#), which came into force after the amendment of the Trademarks and Merchandise Act of 1958 provides for the registration and protection of trademarks and for the prevention of the use of fraudulent marks on merchandise. The [Designs Act, 2000](#) protects the owners of novel or original designs and for enforcing those rights against infringers. This helps the franchisor to protect his designs and maintenance of his image and goodwill, which forms the basis of the franchising system. [The Copyrights Act](#)

[of 1957](#) provides protection to a franchisor against piracy of the franchisor's know-how and products and services.

An important step taken by India is the recognition and protection extended to service marks in India enabling a foreign franchisor to license its mark to a franchisee in order to extend the services synonymous with the franchisor to consumers in India.

Insolvency Laws: Insolvency becomes an issue if either the franchisor or a franchisee is unable to pay its debts as and when they are due. The [Companies Act, 1956](#) and the Provincial Insolvency Act of 1920 govern insolvency laws in India.

Taxation Laws: Taxation including sales tax, property tax, [service tax](#), [income tax](#), withholding tax are issues, which also deserves to be carefully considered. All taxes are subject to Double Taxation Avoidance Agreements (DTAA) entered into by India with any foreign country. India has entered into DTAA with 65 countries including the United States. In case of countries with which India has Double tax Avoidance Agreement, the tax rates are determined by such agreements. Section 90 of the [Income Tax Act](#) recognizes this, and this agreement takes precedence over the terms of the Income Tax Act.

Labor laws: India has numerous [labor laws](#) addressing various issues such as resolution of industrial disputes, working conditions, labor compensation, insurance, and equal remuneration. Some of the main laws that govern labor regulations in India are: the [Apprentices Act, 1961](#); the [Contract Labor \(Regulation & Abolition\) Act, 1970](#); [Employees Provident Funds and Miscellaneous Provisions Act, 1952](#); [Employees State Insurance Act, 1948](#); [Equal Remuneration Act, 1976](#); [Factories Act, 1948](#); [Industrial Disputes Act, 1947](#); [Minimum Wages Act, 1948](#); [Payment of Bonus Act, 1965](#); [Workers Compensation Act, 1923](#); [Payment of Gratuity Act, 1972](#); and [Payment of Wages, Act of 1936](#).

Additionally, laws and regulations applying to specific sectors of goods and services will also apply depending on the franchise operation.

Market Entry

Key factors to successfully entering the franchising market in India include finding the right partners who have knowledge of the local market and procedural issues, good planning, and aggressive due diligence and follow up. It is vital to conduct a thorough financial and legal due diligence on potential partners to ascertain their ability to invest and expand the business. The U.S. Commercial Service in India offers customized solutions to help your business enter and succeed in the Indian market. To identify franchisees in India, U.S. franchisors can take advantage of the [Gold Key Service](#) program offered by the U.S. Commercial Service through its seven offices in India. To conduct a background check on potential franchisees, U.S. companies can take advantage of the Commercial Service's [International Company Profile](#) service.

The [Focus Franchising Promotion - India](#) is an exclusive program to introduce U.S. concepts/brands into the Indian franchise market. The U.S. Commercial Service's Franchise Team in India has designed this unique cost-effective program to offer U.S. franchisors the opportunity to present their franchise concepts/brands to a customized target audience of potential investors seeking master licenses of U.S. brands in India. It offers an in-depth first-hand experience for U.S. franchisors to understand the Indian market and to establish new and profitable commercial relations with Indian companies. Immediately after the promotion, U.S. participants will receive a list of pre-screened potential franchisees from all over India. The "Focus Franchising" promotions will prominently promote industry specific U.S. brands product brochures/literature at Commercial Service offices' for two months. The program will feature U.S. food franchise concepts during August/September 2009; wellness and healthcare services during October/November 2009; and professional cleaning services during December/January 2010. For more information and to contact us with your interests, please visit: <http://www.buyusa.gov/india/en/focusfranchising.pdf>

<http://www.buyusa.gov/india/en/ff.html>

Market Issues & Obstacles

Unlike the United States and other countries with a developed franchising system, the absence of specific regulations or a comprehensive franchising law, coupled with the applicability of several laws poses a number of challenges for foreign as well as domestic franchisors and franchisees in India. The applicability of multiple laws to a franchise transaction poses problems of complexities and ambiguities in agreements and is also time consuming. However, the present ambiguity also offers scope for flexibility and variation to a franchisor's strategy and approach.

The royalty cap in India continues to adversely affect the pace of growth of the franchising industry in India since it restricts the master franchisee from paying the royalty charged to the franchisor. India permits foreign franchisors to charge royalties up to 1 percent for domestic sales and 2 percent on exports for use of the foreign franchisor's brand name or trade mark, without transfer of technology. This implies that by just lending their brand name or trademark to an Indian company, a foreign company can receive royalties. The laws in India also permit lump sum and royalty payments to be made by Indian franchisees to their foreign counterparts for use of foreign technology, which includes manuals, and systems. Lump sum payments up to \$ 2 million are permitted and royalties of 5 percent on domestic sales and 8 percent on exports can be paid to the foreign franchisor. A foreign company must seek the approval of the Reserve Bank of India, India's central bank and regulatory authority for royalties exceeding these prescribed limits.

Despite these market impediments or constraints, India remains a "sizzling" market place for American Franchisers. Demand for U.S. brands remains strong and American franchises thrive in India with strong prospects in various sectors like food, education & training, health & fitness, beauty salons & supplies, professional services, and apparel. India is a story of growth and opportunity. India's sustained growth of 9 percent in fiscal year 2006-2007 and 2007-2008, and with a 6.7 percent growth during the last fiscal year, 2008-2009 despite a worldwide slowdown makes it one of the fastest growing economies in the world and offers diverse business prospects for U.S. franchisors.

Since economic liberalization in 1991, India has witnessed a huge growth in entrepreneurs. As a business model, franchising is ideally suited for Indian entrepreneurs. India has a vast pool of entrepreneurial energy and talent, and a pressing need for increasing self and other employment opportunities. Franchising meets all these needs. According to a study conducted by the management-consulting firm A.T. Kearney, India tops the list of the 30 most attractive emerging markets for investment opportunities by mass merchants and food retailers. Franchising retail outlets is emerging as a popular model for reaching the Indian consumer, and has grown in popularity. Though current investment regulations of the Indian government restrict foreign investment in the retail sector, many international companies have chosen the franchising route to grab a share of the enormous market that India offers.

Trade Events

[Focus Franchising, August to September, 2009](#) – Ahmedabad, Bangalore, Chennai, Hyderabad, Kolkata, Mumbai, and New Delhi

The Franchising Association of India in association with Franchise Plus – India's leading magazine on franchise opportunities organizes the Indian Franchising Summit, in conjunction with the Indian Franchising Exhibition every year. Please check the Franchise Plus web link below for next years venue and event dates.

Resources & Contacts

[Franchising Association of India](#)
[Franchise India](#)
[Info Franchise](#)
[Franchise Plus](#)
[Franchise Business](#)

[Reserve Bank of India](#)
[Ministry of Finance, Government of India](#)
[Ministry of Law & Justice, Government of India](#)

For More Information

The U.S. Commercial Service in Bangalore, India can be contacted via e-mail at:
Manjushree.Phookan@mail.doc.gov ; Phone: 91-80-2220 6404; Fax: 91-80-2220 6405; or visit our website:
www.buyusa.gov/india

The U.S. Commercial Service — Your Global Business Partner

With its network of offices across the United States and in more than 80 countries, the U.S. Commercial Service of the U.S. Department of Commerce utilizes its global presence and international marketing expertise to help U.S. companies sell their products and services worldwide. Locate the U.S. Commercial Service trade specialist in the U.S. nearest you by visiting <http://www.export.gov/eac>.

Comments and Suggestions: We welcome your comments and suggestions regarding this market research. You can e-mail us your comments/suggestions to: Customer.Care@mail.doc.gov. Please include the name of the applicable market research in your e-mail. We greatly appreciate your feedback.

Disclaimer: The information provided in this report is intended to be of assistance to U.S. exporters. While we make every effort to ensure its accuracy, neither the United States government nor any of its employees make any representation as to the accuracy or completeness of information in this or any other United States government document. Readers are advised to independently verify any information prior to reliance thereon. The information provided in this report does not constitute legal advice. The Commercial Service reference to or inclusion of material by a non-U.S. Government entity in this document is for informational purposes only and does not constitute an endorsement by the Commercial Service of the entity, its materials, or its products or services

International copyright, U.S. Department of Commerce, 2007. All rights reserved outside of the United States.