

GETTING THE
DEAL THROUGH 

Franchise 2016

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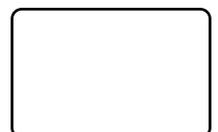


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South Africa

Eugene Honey

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Overview

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

The most common business entity, subsequent to 1 May 2011, is a company. Incorporation proceedings are relatively straightforward with regard to this type of entity. A private limited liability company may have between one and 50 shareholders. External companies can also be registered.

The new Companies Act (Companies Act No. 71 of 2008) that came into effect on 1 May 2011, establishes two categories of business entities, namely profit companies and non-profit companies. The two most common business entities relevant to the typical franchisor are public companies and private companies – both categorised as profit companies under the new Companies Act. Incorporation proceedings are relatively straightforward with regard to both of these types of entities. There is no limit on the number of shareholders that either of these companies are obliged to have. However, a private company is prohibited from offering any of its securities to the public and the transferability of its securities is restricted. External companies can also be registered. The Companies Act provides that external companies must be registered within 20 business days after they first begin to conduct business within the republic.

Previously, it was possible to register a close corporation in terms of the Close Corporations Act. A close corporation was obliged to have at least 10 members, all of whom were natural persons. The Close Corporations Act has been amended so that no new close corporations have been registered since 1 May 2011.

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

The Commissioner of Companies deals with the registration of companies at the South African Companies Intellectual Properties Commission. The relevant act that governs companies is the Companies Act. The Companies Act also establishes a Companies Tribunal, whose function is to adjudicate any application made to it. The Companies Tribunal also serves as a forum for the voluntary resolution of disputes.

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

Incorporation proceedings in South Africa for public and private companies are relatively straightforward. A private company is designated by the term 'Proprietary Limited' or '(Pty) Ltd' and a public company is designated by the term 'Ltd' or 'Limited'. There is no restriction on local or foreign shareholding levels imposed on private or public companies. Share certificates in respect of shares purchased by foreigners should be endorsed non-resident for exchange control purposes. There is no minimum capital requirement.

One or more persons may incorporate a profit company (namely, a private company or a public company). Each incorporator of a company is a first director of the company and serves until sufficient directors are first appointed or first elected to satisfy the minimum requirements of the Companies Act or the company's memorandum of incorporation. For each new company, a memorandum of incorporation must be submitted to the commissioner of companies, together with a notice of incorporation.

In the ordinary course of events, incorporation takes approximately four to six weeks from a name being reserved. On registration, the Commissioner of Companies will assign to the company a unique registration number, enter the prescribed information concerning the company in

the companies register, endorse the notice of incorporation, and issue and deliver a registration certificate to the company. Only when the latter certificate has been issued may the company commence business. Nevertheless, it is possible for pre-incorporation contracts to be concluded by persons acting as trustees for the company to be formed. Any such contract must be in writing, entered into before the company comes into existence and ratified or rejected (completely, partially or conditionally) by the board of the company within three months after the date on which the company was incorporated. Pre-incorporation contracts need not be filed at the Companies Commission, nor is it required that they be certified by a notary.

There is no requirement that directors be South African citizens or residents. The company is, however, obliged to file a statutory form containing the personal details of directors with the Companies Commission. All companies have to file an annual return for each financial year. Only public companies are obliged to appoint an auditor, an audit committee, a company secretary and have their annual financial statements audited. Private companies are only obliged to appoint an auditor if required by the Companies Act or the Companies Regulations to have their annual financial statements audited each year; or if the company's memorandum of incorporation requires their annual financial statements to be audited.

In terms of the Income Tax Act, both public and private companies are obliged to appoint a public officer who is a natural person resident in South Africa. The public officer of a company is the representative taxpayer in respect of the income of the company. Public officers are responsible and answerable for doing all things necessary under the Income Tax Act and every notice, process or proceeding that under the Income Tax Act may be given to, served upon or taken against a company, may be given to, served upon or taken against its public officer.

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

There are a number of ways in which investments may be made by a foreigner or foreign-owned company in South Africa, such as:

- forming a company in South Africa, which is the most common procedure. This may be wholly owned or held jointly with other local or foreign shareholders. The formed company can then become engaged in business by setting up a 'greenfield' operation, buying an existing business or setting up in partnership or joint venture with a South African person or company;
- the investor buying or taking over all or some of the shares in an existing private company that has already established a business or will establish a business. Such shares can be held directly by the foreign investor. There is no restriction on foreign shareholding levels. Share certificates in respect of shares purchased by foreigners should be endorsed non-resident for exchange control purposes. There is no minimum capital requirement;
- the investor setting up a branch office. If the investor is a company or corporation this will involve registering the branch as an external company in terms of the Companies Act;
- the investor forming a joint venture with a South African entity, either through a South African subsidiary or directly in partnership;
- the investor setting up a business trust; or
- the investor forming a partnership with another investor or with a South African person. The investor can also establish a business of their own as a sole proprietor. Partnerships and sole proprietors do not enjoy limited liability in South Africa.

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

On 1 January 2001, South Africa moved from a source-based income tax system to a residence-based income tax system. The new system entails that South African residents get taxed on their worldwide income, as opposed to the old system, where income was taxed from a source within or deemed within South Africa.

Tax consists of direct taxes (corporate and individual) as well as certain indirect taxes including VAT, stamp duty and uncertified securities tax.

The corporate rate of tax for companies and close corporations is currently 29 per cent.

Secondary tax on companies (STC) of 12.5 per cent is paid on dividends declared by any resident company. The combined effect of the corporate tax rate and STC is that companies that distribute the greater portion of their profits by way of dividends, are effectively taxed at a rate of 36.89 per cent.

The current VAT rate is 14 per cent. VAT is payable on the supply of goods and rendering of services by a South African-registered VAT vendor on goods imported into South Africa. Any person (including corporations) carrying on a business in South Africa, and whose business taxable supplies exceed the threshold of 300,000 rand (excluding VAT) per annum, is expected to register as a VAT vendor.

Dividends declared by local companies are exempt from tax. Dividends declared by foreign companies with shareholders resident in South Africa are taxable.

A withholding tax of 12 per cent is levied on royalties. The withholding tax on royalties or similar payments is not payable where the royalty is paid to a non-resident company, where the royalty is derived from any trade carried on through a branch or agency in South Africa and the amount of the royalty is subject to tax in South Africa, or where the royalty is paid to a person (other than a person whose place of residence is in a neighbouring country) in respect of the use of any printed publication of any copyright. Royalties payable to a non-resident from a South African source are subject to a withholding tax of 12 per cent.

Capital gains tax (CGT) became effective from 1 October 2001. The maximum CGT rate is 10 per cent for individuals, 14.5 per cent for companies and close corporations, and 20 per cent for trusts.

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?

Employment in South Africa is regulated by the law of contract and by statute. There is a network of legislation providing minimum protection for employees out of which employers and employees may not contract. This legislation is found in a number of acts that regulate, inter alia, maximum hours of work, overtime rates, minimum periods of annual leave, notice of termination, organisational rights in respect of trade unions, strike law, rights and responsibilities of employers and workers in the event of retrenchments, insolvency and transfers of businesses, protection from unfair dismissal and the prohibition of unfair discrimination.

It is extremely unlikely that a franchisee or an employee of a franchisee could be deemed an employee of the franchisor, as the franchisor and franchisee corporate entities are completely separate. Only if the franchisor did something different, such as entering into an employment contract with the franchisee or an employee of a franchisee which would engender, suggest or imply an employer-employee relationship, could this risk arise. In the ordinary course of a typical franchisor-franchisee relationship, where they are contracted by a way of a franchise or licence agreement, the franchisee or the employees of the franchisee will not be deemed employees of the franchisor.

7 How are trademarks and know-how protected?

Trademarks are regulated by the Trademarks Act 1993. The Act is administered by the Registrar of Trademarks, based in Pretoria, who controls the register of trademarks. The Act allows for the registration of trademarks capable of distinguishing the goods or services of a person in respect of which they are registered, or proposed to be registered, from the goods or services of another person either generally or (if applicable) subject to limitations.

Trademarks are registered for 10 years, but may on application be renewed for an unlimited number of 10-year periods. The Act makes provision for the protection of well-known international marks. Some protection is also provided for unregistered trademarks under the common law relating to unlawful competition and 'passing-off'.

Know-how and trade secrets are protected under the common-law principles pertaining to unlawful competition. There are no registration formalities, but the information must in fact be secret in the sense that it is only known on a confidential basis to a limited circle of people, and must be of economic value to the trader in his business. An action for damages for unlawful competition must be brought within three years of the infringement becoming known to the plaintiff. In the case of ongoing infringement, proceedings for an injunction may be brought for as long as the infringement continues.

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

South Africa has an advanced land registration system in place. Title registration is possible because each registered unit of land is surveyed and represented on a diagram or general plan. South Africa has an accurately beaconed boundary system.

In addition to the conventional title deed registration system, there is also a sectional title system in place to cater for larger buildings, such as blocks of flats and commercial property complexes, similar to condominium development in many other countries. Each major regional centre in South Africa has a Deeds Registry Office covering all land in the region and controlled by a registrar of deeds.

A person domiciled in another country is free to acquire immoveable property in South Africa.

An external company may also acquire immoveable property in South Africa, provided the company registers its memorandum and articles of association in the Companies Office.

Laws and agencies that regulate the offer and sale of franchises

9 What is the legal definition of a franchise?

In terms of the new Consumer Protection Act that came into operation on 1 April 2011, the definition of a 'franchise agreement' is as follows:

[A]n agreement between two parties, being the franchisor and franchisee, respectively;

- (a) in which, for consideration paid, or to be paid, by the franchisee to the franchisor, the franchisor grants the franchisee the right to carry on business within all or a specific part of the Republic under a system or marketing plan substantially determined or controlled by the franchisor or an associate of the franchisor;*
- (b) under which the operation of the business of the franchisee will be substantially or materially associated with advertising schemes or programmes or one or more trademarks, commercial symbols or logos or any similar marketing, branding, labelling or devices, or any combination of such schemes, programmes or devices, that are conducted, owned, used or licensed by the franchisor or an associate of the franchisor; and*
- (c) that governs the business relationship between the franchisor and the franchisee, including the relationship between them with respect to the goods or services to be supplied to the franchisee by or at the direction of the franchisor or an associate of the franchisor.*

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

Foreign persons are free to conclude franchising agreements with local persons. Franchising is regulated by common law. In addition, the new Consumer Protection Act deals with certain aspects of franchising. It introduces aspects such as equity, reasonableness and no unjust prices.

In terms of the new Consumer Protection Act there are certain formalities to entering into a franchise agreement. Under section 7 of this Act a franchise agreement must:

- be in writing and signed by or on behalf of the franchisee;
- include any prescribed information or address any prescribed categories of information, such as disclosure which has been published in the regulations; and
- be in clear and understandable language.

Furthermore, a franchisee may cancel a franchise agreement without cost or penalty within 10 business days of signing said agreement by giving written notice to the franchisor, and the minister may prescribe information to be set out in franchise agreements either generally or within specific categories or industries. Regulations were published and came into force on 1 April 2011.

Most contracts tend to be subject to South African law, but there is no general bar to any foreign law serving as the governing law as long as there is some nexus between the law and the contract. The parties are free to agree on which court will have jurisdiction, or alternatively, agree that any disputes will be referred to mediation or arbitration. In short, the parties have, to some extent, free scope to regulate their relationship as they deem fit.

11 Describe the relevant requirements of these laws and agencies.

See question 10.

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

See question 10.

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

There is no law or regulation currently in place (other than the provisions of the Consumer Protection Act), which creates a requirement that must be met before a franchisor may offer franchises.

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?

With regard to the recruitment of franchisees, there are black empowerment laws and policies in place, particularly for South African entities in terms of which certain benefits can be derived if there are black franchisees. There are no restrictions on requirements relating to the number of franchisees or the number of franchises, held by a single franchisee, or in respect of their locations. There is also no restriction generally regarding the local content of goods and services purchased by franchisors or franchisees. Foreign investment is encouraged and there is no legislation preventing foreign investment into South Africa, including in relation to the franchise industry. There is also no yearly growth requirement for a franchise system.

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

In terms of Regulation 3 of the Consumer Protection Act Regulations, (the CPA Regulations) every franchisor must provide a franchisee with a disclosure document, dated and signed by an authorised officer of the franchisor, at least 14 days prior to the signing of the franchise agreement. There are no requirements regarding how often the disclosures must be updated.

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 Association of South Africa (FASA), which is a voluntary membership, non-profit organisation, requires that a disclosure document be furnished to the prospective franchisee or sub-franchisee by the entity with whom they are contracting. It would be reasonable to disclose at least that a franchisor-sub-franchisor or franchisor-master franchisee relationship exists.

According to the Consumer Protection Act regulations, if the franchise agreement is related to a master franchisee, the master franchisee's identity must be disclosed.

The definition of a franchise agreement is set out in question 9. The parties to a franchise agreement are described as a franchisor and franchisee. In terms of the disclosure requirements, every franchisor must provide the prospective franchisee with a disclosure document, dated and signed by an authorised officer of the franchisor, at least 14 days prior to the signing of a franchise agreement. Both a master franchise agreement and a sub-franchise agreement will fall within the definition of a franchise agreement. It is

our understanding that in each agreement, it is the person or entity granting the rights who is obliged to provide a disclosure document.

17 What information must the disclosure document contain?

In terms of Regulation 3 of the CPA Regulations, disclosure must be given at least 14 days prior to the signing of a franchise agreement and this must include the details set out below.

Although international best practice has for many years dictated that competent disclosure should be given to franchisees, this has previously not been law in South Africa. FASA has, for many years, however, required for membership that franchisors should furnish franchisees with a competent agreement, a compliant disclosure document, as well as an operations manual. The CPA Regulations also set out requirements in relation to disclosure documents that are required to be furnished to franchisees at least 14 days prior to the signing of a franchise agreement.

As a minimum a disclosure document must contain:

- the number of individual franchised outlets;
- the growth of the franchisors turnover, net profit and the number of individual new franchised outlets for the immediate preceding year;
- a statement of confirmation that the franchisor is able to pay its debts as and when they fall due; and
- written financial projections of the franchised business or of franchises of a similar nature, together with particulars of the assumptions upon which these representations are made.

The disclosure document must be accompanied by an accounting officer or auditor's statement confirming, inter alia, that the business of the franchisor is a going concern, that it is able to meet its current and contingent liabilities, as well as its financial commitments and that the franchisors annual financial statements have been prepared in accordance with generally accepted accounting practice.

In addition, the disclosure document must also be accompanied by a list of current franchisees, their contact details, and a clear statement that the prospective franchisee is entitled to contact any of the franchisees listed, or alternatively to visit any outlets operated by those franchisees. In addition, an organisation chart depicting the support system in place for franchisees should also be attached.

18 Is there any obligation for continuing disclosure?

No.

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

The Consumer Protection Act and its regulations came into operation on 1 April 2011, and it is not yet entirely clear how the Consumer Protection Commission would enforce the disclosure requirements. A claim process and related provisions have been published.

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?

Franchisees will be entitled to institute proceedings in terms of the relevant franchise agreement if a violation of the disclosure requirements occurs. The legal remedies would include cancellation of a contract and claiming damages on the basis of misrepresentation or non-disclosure. Damages would be calculated on the actual losses of the franchisee. This may include reimbursement or damages or both.

As mentioned above, it is the franchisor or the entity granting the rights in each instance that is required to provide disclosure. If disclosure is given by a franchisor to a master franchisee, who then provides the same disclosure to a sub-franchisee and this is found to be incorrect or inaccurate, the franchisor could certainly be liable for the losses incurred or damages suffered as a result.

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?

See question 20. A director or member of a corporate entity can be held personally liable in certain instances, for example, if it trades recklessly with the corporate entity.

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?

Common law applies to all contracts entered into and in relation to which South African law applies. Key concepts of the new Consumer Protection Act include reasonableness, equity and no unjust prices. It is also necessary in terms of the CPA regulations to include provisions in the contract which relate to assignment of rights. The leading franchise association in South Africa is FASA (www.fasa.co.za).

While Regulation 2 of the Consumer Protection Act deals with what must be included and dealt with in the Franchise Agreement, Regulation 3 sets out what should be included in the Disclosure Document, which must be furnished to a prospective franchisee 14 days prior to the signing of a Franchise Agreement.

The disclosure document must as a minimum contain the following:

- the number of individual outlets franchised by the franchisor;
- the growth of the franchisor's turnover, net profit and the number of individual outlets, if any, franchised by the franchisor for the financial year prior to the date on which the prospective franchisee receives a copy of the disclosure document;
- a statement confirming that there have been no significant or material changes in the company's or franchisor's financial position since the date of the last accounting officer, or auditor's certificate or certificate by a similar reviewer of the company or franchisor, that the company or franchisor has reasonable grounds to believe that it will be able to pay its debts as and when they fall due; and
- written projections in respect of levels of potential sales, income, gross or net profits or other financial projections for the franchised business or franchises of a similar nature with particulars of the assumptions upon which these representations are made.

Each page of the disclosure document must be qualified in respect of the assumptions contained therein.

The disclosure document must be accompanied by a certificate on an official letterhead from a person eligible in law to be registered as the accounting officer of a close corporation, or the auditor of a company, as the case may be, certifying that:

- the business of the franchisor is a going concern;
- to the best of his or her knowledge the franchisor is able to meet its current and contingent liabilities;
- the franchisor is capable of meeting all of its financial commitments in the ordinary course of business as they fall due;
- the franchisor's audited annual financial statements for the most recently expired financial year have been drawn up:
 - in accordance with South African generally accepted accounting standards;
 - except to the extent stated therein, on the basis of accounting policies consistent with prior years;
 - in accordance with the provisions of the Companies Act (No. 61 of 1973 or any legislation which replaces this Act), and all other applicable laws; and
 - fairly reflecting the financial position, affairs, operations and results of the franchisor as at that date and for the period to which they relate.

The disclosure document must be accompanied by:

- a list of current franchisees, if any, and of outlets owned by the franchisor, stating, in respect of any franchisee;
- the name under which it carries on business;
- the name of its representative;
- its physical address; and
- its e-mail and office telephone number, together with a clear statement that the prospective franchisee is entitled to contact any of the

franchisees listed, or alternatively to visit any outlets operated by a current franchisee to assess the information disclosed by the franchisor and the franchise opportunity offered by it; and

- an organogram depicting the support system in place for franchisees.

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?

See question 17.

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?

The Consumer Protection Act assists with aspects such as fraud and deceptive practices. There are, however, remedies under common law for fraudulent, negligent or innocent non-disclosure or misrepresentation, which include cancellation, damages or both.

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?

See question 10.

26 Do other laws affect the franchise relationship?

In accordance with section 3 of the Competition Act, the Act applies to all economic activity within, or having an effect within, South Africa. The Act aims to promote and maintain competition in South Africa through provisions relating to merger control, restrictive practices and the abuse of dominance. Nevertheless, the objects of the legislation are not merely limited to the promotion of competition but include public-interest objectives, such as ensuring that small and medium-sized enterprises have an equitable opportunity to participate in the economy.

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

See question 26.

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?

The new Consumer Protection Act regulates certain aspects of franchising including, inter alia, reasonableness, equity and no unjust prices. It is also regulated by common law. The rights and obligations of the parties would be set out primarily in the franchise agreement.

Certain formalities are set out in the Consumer Protection Act as mentioned above. Franchise agreements must be in writing and signed by or on behalf of the franchisee. Legal firms are able to provide all necessary assistance. Most contracts tend to be subject to South African law, but there is generally no bar to any foreign law serving as the governing law as long as there is some nexus between the law and the contract. The parties are free to agree on what court will have jurisdiction, or alternatively, agree that any disputes will be referred to arbitration. In short, parties have, to an extent, free scope to regulate their relationship as they deem fit, provided that the provisions of the Consumer Protection Act are complied with.

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

The new Consumer Protection Act that deals with certain aspects of franchising introduces, inter alia, reasonableness, equity and no unjust pricing. Franchising is also regulated by common law. The rights and obligations of the parties would, primarily, be those reflected in their written agreement.

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

See question 29.

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

Yes. The franchisor should insert appropriate provisions into the franchise agreement.

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

The new Consumer Protection Act deals with certain aspects of franchising including, inter alia, reasonableness, equity and no unjust pricing. It is also regulated by common law. In most instances reasonable market-related provisions are inserted.

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

South Africa's National Credit Act regulates the maximum amount of interest that may be charged on overdue accounts from one period to another.

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

South Africa's exchange control provisions regulate payments to foreign franchisors. Application for exchange control approval is, in most instances, a fairly straightforward process and is primarily dealt with by leading banks. If difficulties arise, assistance can be sought from a law firm.

35 Are confidentiality covenants in franchise agreements enforceable?

Yes. Confidentiality and non-disclosure covenants and agreements are enforceable in South African law.

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?

The new Consumer Protection Act introduces concepts such as, equity, reasonableness and no unjust pricing. These principles are similar to acting in good faith. Common law also provides remedies for fraudulent, negligent and innocent misrepresentation and non-disclosure prior to entering into agreements. Certain actions may also be contra bonos mores.

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

A new Consumer Protection Act came into operation on 1 April 2011 and treats franchisees as consumers.

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

The regulations for the new Consumer Protection Act that came into force on 1 April 2011 are intended to deal with disclosure requirements. We recommend, at least for practical purposes, that these be in English, as it is the primary business language in South Africa.

39 What restrictions are there on provisions in franchise contracts?

In accordance with section 3 of the Competition Act, the Act applies to all economic activity within, or having an effect within, South Africa. The Act aims to promote and maintain competition in South Africa through provisions relating to merger control, restrictive practices and the abuse of dominance. Nevertheless, the objects of the legislation are not merely limited to the promotion of competition but include public interest objectives, such as ensuring that small and medium-sized enterprises have an equitable opportunity to participate in the economy.

The concerns of the Competition Commission include horizontal and vertical relationship collusion, retail price maintenance, exclusive territories, exclusive dealing, tying of products and intellectual property rights.

The Competition Commission, which enforces the provisions of the Competition Act, recognises the nature and contribution of franchising. It also recognises that franchise agreements are not necessarily anti-competitive, despite the provisions of the Competitions Act, and that there may be, in fact, efficiency, technology and pro-competitive benefits. It is essential that franchisors do not dictate minimum prices and minimum discounts to franchisees.

The new Consumer Protection Act provides that franchise agreements must be drafted in clear and understandable language.

The definition of a franchise agreement in terms of the Consumer Protection Act is fairly broad, and includes a full business concept franchise arrangement as well as similar arrangements such as licence, distribution and agency arrangements or contracts.

It is very important to note that, in terms of the Act, there is no threshold whatsoever in relation to any franchise or similar agreement or arrangement. As a result, any such agreement or arrangement falls within the Consumer Protection Act and its regulations.

There are fairly comprehensive provisions in the regulations as to what a franchise agreement should include, and these are set out below:

- a franchise agreement must reflect, at the top of the first page, a statement to the effect that 'a franchisee may cancel a franchise agreement without cost or penalty within 10 business days after signing such agreement, by giving written notice to the franchisor';
- a franchise agreement must contain provisions which prevent the following:
 - unreasonable or overvaluation of fees, prices or other amounts;
 - conduct that is unnecessary or unreasonable in relation to risks to be incurred by one party; and
 - conduct that it is not reasonably necessary for the protection of the legitimate business interests of the franchisor, franchisee or franchise system;
- a franchise agreement must also contain a clause in terms of which the franchisor is not entitled to any undisclosed direct or indirect benefit or compensation, unless this is disclosed in writing, together with an explanation thereof; and
- a franchise agreement should contain numerous other provisions.

We would like to highlight the following:

- a description of the goods or services which the franchisee is entitled to render or sell;
- obligations of the franchisor;
- obligations of the franchisee;
- a description of the business system;
- direct or indirect consideration payable to the franchisor;
- details of territorial rights, if granted;
- a description of the proposed site, premises or location;
- details of the intellectual property licensed;
- details of the master franchisee, if relevant;
- details of initial training and ongoing training and assistance;
- terms and conditions relating to the duration, renewal, goodwill and assignment;
- full details of any marketing fund, including that the funds are deposited into a separate account, that any such funds are used for marketing and advertising purposes of the goods and services of the franchise system and that full financial statements of all receipts and expenses will need to be provided;
- any restrictions imposed on the franchisee;
- full particulars of the financial obligations of the franchisee including the initial fee, working capital, royalties, total investment required and other amounts payable;
- the effect of termination or expiration of the franchise; and
- if requested in writing, an explanation of terms or sections not understood.

Although some of the points are traditionally found in the average competently-drafted franchise agreement, franchisors will now need to check and audit their franchise agreements to ensure that they are compliant. The regulations may, of course, be updated from time to time and franchisors will therefore need to remain abreast of any such new or updated regulations. Further, if any written explanation of a term or section is given, this must be legally correct, failing which the franchisor risks being bound to an incorrect explanation.

Although international best practice has, for many years, dictated that competent disclosure should be given to franchisees, this has previously not been law in South Africa. FASA has for many years, however, required for membership that franchisors should furnish franchisees with a competent agreement, a compliant disclosure document, as well as an operations manual. The CPA regulations also set out requirements in relation to disclosure documents that are required to be furnished to franchisees at least 14 days prior to the signing of a franchise agreement.

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

See question 39.

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

South Africa has an independent High Court judiciary drawn principally from the ranks of senior advocates (barristers), attorneys (solicitors) and academics. At present, there is a split bar divided between attorneys and advocates, but attorneys can acquire the right of appearance in the High Court. Both branches of the profession are well established and competent. There is an established and sophisticated hierarchy of courts, namely:

- magistrates' courts in each town and city with limited jurisdiction, for example up to certain amounts;
- High Courts with territorial jurisdiction over provinces or parts of provinces and the power to adjudicate, generally, on all disputes, plus certain appeal functions;
- the Supreme Court of Appeal, which sits in Bloemfontein, exercising appellate jurisdiction over all the High Courts; and
- the Constitutional Court, which sits in Johannesburg and has both original and appellate jurisdiction on constitutional matters.

The High Courts and the Supreme Court of Appeal may make an order concerning the constitutional validity of an act of Parliament, provincial

legislation or administrative conduct of the government, but an order invalidating the legislation of Parliament must be confirmed by the Constitutional Court.

Alternative forms of dispute resolution have become increasingly popular. Arbitration is governed by the Arbitration Act 1965.

Professional bodies specialising in arbitration services and alternative dispute resolution have been formed and are used extensively, particularly in labour-related matters. All building and engineering contracts can and generally should contain clauses providing for mediation and arbitration. Parties are free to agree on a governing law and to the jurisdiction of international arbitration forums such as the ICC and LCIA. FASA provides a mediation service, primarily to its members.

FASA is in the process of developing an ADR system that will include negotiations, mediation and arbitration.

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

One of the advantages of arbitration is that, if properly managed, it can be quicker and less expensive than litigation in the courts. A significant advantage is to be able to choose a good arbitrator who may be a specialist in the subject matter of the dispute. The parties also have far greater control of the time, place and process to be followed in an arbitration than they do in court proceedings. Arbitration proceedings can also, however, be more expensive because the costs of the arbitrator need to be paid for, and if the parties do not cooperate, difficulties and delays could arise.

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

Foreign franchisors are generally not treated differently. There are, however, various statutes or aspects that would be relevant and need to be dealt with, such as exchange control regulations and tax.

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