The Legal Aspect of Franchising in Indonesia

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The Laws

- A franchise in Indonesia is governed by Government Regulation No. 42 of 2007 on Franchise (**GR42/2007**) and several implementing ministerial regulations:
- Ministry of Trade Regulation No. 7/M-DAG/PER/2/2013 on the Development of Partnerships in Food and Beverage Franchises (**Regulation 7**);
- Ministry of Trade Regulation No. 53 M-DAG/PER/8/2012 on Implementation of Franchise (**Regulation 53**);
- Ministry of Trade Regulation No. 60/M-DAG/PER/9/2013 on the Requirement to Use Franchise Logo (**Regulation 60)**; and
- Ministry of Trade Regulation No. 68/M-DAG/PER/10/2012 on Franchises for Modern Store Outlets (**Regulation 68**).

Definition of Franchise

- Regulation 53 defines a franchise as an exclusive right owned by individuals or business entities of a business system with unique characteristics in the framework of marketing goods and/or services, which have already proven successful, and can be utilized and/or used by other parties on the basis of franchise agreements.

- According to GR42/2007 and Regulation 53, a franchise in Indonesia must satisfy the following criteria:
  - have distinctive business features
  - be proven to be profitable
  - have written Standard Operating Procedures (SOP)
  - be easily learned and applied
  - provide continuous support, including operational guidance, training and promotion;
  - have registered intellectual property rights; and
  - have been operating as a franchise business for at least five years.

- A franchise business should not portray itself as a “franchise business” unless it meets the above criteria.

Franchise Agreement

- Regulation 53 defines a "franchise agreement" as "a written agreement between a franchisor and a franchisee", and requires franchise agreements at the minimum to include:
  - information on the parties' identity and domicile;
  - type of the franchised intellectual property rights, including but not limited to patents, trade marks and trade secrets;
  - information on business activities;
  - rights and obligations of the franchisor and franchisee;
  - support, guidance, and assistance to be received by the franchisee;
  - granted territory;
  - term of the agreement;
  - procedures on the fees payment;
  - dispute resolution procedures;
  - procedures on agreement extension and termination;
  - franchisor's warranty that it will fulfill its obligations during the term of the franchise agreement; and
  - number of outlets granted to the franchisee.
- Indonesia's Ministry of Trade (**MOT**) is likely to reject the registration of the franchise agreement if it fails to meet the above requirements, in which case a Franchise Registration Certificate (*Surat Tanda Pendaftaran Waralaba* or STPW) will not be issued.

Clean Break Statement

- Where a franchise agreement is terminated early, the MOT will require a “Clean-Break Statement” (**CBS**) before it will deregister the franchise. A CBS is basically a declaration by the franchisor and franchisee that they have no outstanding obligations to each other.

- Where no CBS is available, a final court decision is needed in its place. If the franchise is exclusive, then another franchisee cannot register an exclusive franchise agreement for the same goods or services in the same territory, and cannot legally operate, until that deregistration has been completed.

Franchise Registration Certificate

- The franchisor and franchisee must obtain a Franchise Registration Certificate (STPW) in order to carry out a franchise business.
- Franchisors must register their offering prospectus with the MOT at least two weeks before the franchise agreement is signed. The prospectus must be in the Indonesian language, be accompanied by various required documents, and satisfy certain other requirements. As an example of these additional requirements, a franchisee must register the franchise agreement with the MOT or the other relevant authorities.
- A Franchise Registration Certificate is valid for five years and can be extended for five more years. Absence of a Certificate may result in financial penalties. However, we understand that the MOT plans to impose stronger sanctions, including temporary suspension of the franchised business.

Subsidiaries

- Regulation 53 restricts the granting of a franchise from a parent company to subsidiaries that it directly or indirectly controls, and a majority-owned joint venture structure is not permitted.

- Although currently no sanctions are imposed for a breach of this restriction, the MOT is unlikely to grant a Franchise Certificate to any franchisee using this structure.

Restriction on Modern Store Outlets

- Regulation 68 provides that a single company cannot have more than 150 company-owned outlets. Additional outlets may be established if 40% of the additional outlets are franchised to a local micro, small or medium enterprise (**MSME**). This means that for every 10 additional outlets, four must be franchised to an MSME.

- However, this restriction applies only to modern store outlets that are minimarkets (up to 400 square meters of store space), supermarkets (up to 1,200 square meters of space) and department stores (up to 2,000 square meters of space). Large-scale modern stores such as hypermarkets and wholesalers are exempt.

Restriction on F&B Outlets

- Regulation 7 restricts one company to a maximum of 250 company-owned food and beverage (F&B) outlets. Additional outlets must be franchised to a local MSME. If, however, a franchisor or franchisee wants additional company-owned outlets, then it can use a capital investment structure and invite a local MSME to inject capital in these additional outlets. The MSME must inject (i) at least 40% of total capital investment in outlets requiring capital of less than 10 billion rupiah, and (ii) at least 30% of total capital investment in outlets requiring capital in excess of 10 billion rupiah.

Local Content & Franchise Logo

- For their franchise business, the franchisor and franchisee must use raw materials and business equipment, and sell products, that are at least 80% domestically produced. In addition, the franchisor should cooperate with a local MSME as franchisee or supplier of domestic goods and/or services.

- Regulation 60 provides that an Indonesian franchise shall use the “official” franchise logo, which should be properly placed or displayed.

Indonesian Law & Language Requirements

- Franchise agreements must be governed by Indonesian law. In addition, the franchise agreements must be written in the Indonesian language. In practice, if the franchise transaction involves a foreign party, a dual-language agreement is usually executed.

- Failing to comply with these requirements will put a franchise agreement at risk of annulment or cancellation. A District Court in West Jakarta decided that an agreement executed only in the English language was invalid. The High Court upheld this decision, and a further appeal is currently pending before the Supreme Court.

REFERENCE

- LEXOLOGY

- THANK YOU -