

Legal Protection for Recipients of Foreign Franchise Rights in Indonesia

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Abstract. Due to gobalization, world trade has increased tremendously. Franchising having surged as one of the many business models has the potential to improve the economy of the community. Basically, franchising refers to a method of goods and services distribution to consumers. The party who owns the method is referred to as the franchisor, while the party given the right to use a method the franchisee. This article examines the legal issues that arise in granting license rights from foreign franchisors to franchisees, and how the laws in Indonesia provide protection for the rights and obligations of the parties. The research employed the normative juridical method or library research. Normative legal research examines the law as a positive norm as it is written in the book. In accordance with Article 1320 and 1338 of the Indonesian Civil Code, arrangements of franchising agreement in Indonesia are based on the agreement between the parties. To provide legal protection for recipients foreign franchise in Indonesia, the government has enacted the Government Regulation No. 42/2007 on Franchise and Trade Minister Regulation No. 53/2007 on the Implementation of Franchising. In principle, the settlement of the problems that occur in international franchising agreement would be resolved by consultation or negotiation. If consensus is not reached, the parties can take the dispute to international arbitration. In general, the dispute over the franchise business concept is mostly resolved through the general justice institution.

1. Introduction

The concept of a franchise business is in demand by business people because it is almost the same as opening a business branch. The difference is that the franchise lies only in its implementation, namely the operation of the expansion of the franchise business is funded and carried out by another party called the franchisee for the risks and responsibilities of his own [1]. Business people prefer franchise business because the type of goods they are going to sell and the quality of the goods are well known to the public, so there is no need to do any more promotions [2]. Granting a franchise license requires a study, whether the Government Regulation No. 42/2007 on Franchising and Regulation of the Minister of Trade No. 53/2007 on Franchising, is effective enough to protect the interests of the parties.[3]

The definition of franchise can be found in some business literature. The committee on Small Business, United Congress defines franchise as franchising is a contractual method for marketing and distributing goods and services (franchisors) through a dedicated or restructured network of distributors (franchisees) [4]. Another meaning of the franchise is a method of doing business by which the franchisee is granted the right to engage in offering, selling, or distributing goods or services under a marketing format which is designed by the franchisor [5]. In Indonesian law, franchising is a special right that is owned by an individual or business entity against a business system with business characteristics in order to market goods and/or services that have been proven successful and can be used and/or used by other parties based on a franchising agreement [6].

One of the benefits of a franchise business system is when the franchisee starts a business, does not promote, because the customer is available. Unlike the new independent business (non-franchise), who must conduct promotions and marketing independently [7]. In addition, this business system also provides a process and regularity of work that is integrated in management, organization, administration, financial, human resources, and marketing that produces outputs of products or services with maintained quality standards [8]. Then, the business system is outlined in the form of standard operting procedures (SOPs) which serve as guidelines for working and doing the business. The SOPs is made in the form of a book or DVD called the Franchise Manual [9].

On the other hand, there are several challenges faced by franchisees, such as, difficulties in getting good cooperation from the parties. The franchisee is very much attached to the franchisor, so he has no freedom to do business creations and innovations, including in production and marketing [10]. Another weakness is the decision and business policy of the franchisor greatly affects the success and failure of the business and has an impact on the franchisee.

Prior to 1997, the franchise agreement in Indonesia was only regulated by the agreement of the parties. The agreement is guided by Article 1320 and 1338 of the Indonesian Civil Code. The law regulates general principles of contract validity, including contracts in business activities. Then, the provisions of the Indonesian Civil Code was considered irrelevant to the needs of the parties, especially in legal protection and dispute resolution. In order to fulfilling the legal needs of business people, the government issues several provisions that specifically regulate franchise agreements. Currently, Government Regulation No. 42/2007 on Franchising is the highest franchise law in Indonesia.

According to data from the Ministry of Trade of the Republic of Indonesia, the franchise industry in Indonesia has increased by 35%. There are around 698 franchises with 24,400 outlets, consisting of 63% franchises, and around 37% of foreign franchises with revenues of 172 trillion [11]. The Indonesian people's lifestyle tends to choose famous brand products from abroad [12]. This condition causes foreign franchisees to easily enter the Indonesian market. Moreover Indonesia has become a member of the ASEAN Economic Community (MEA), where the flow of trade in goods and services is easier to enter Indonesia, and makes foreign franchises more and more grow in Indonesia [13]. The franchise industry in Indonesia has significantly grown in recent years [14].

In a franchise business system, the most important thing is the agreement of both parties, namely the franchisor and the franchisee [14]. The agreement is stated in an agreement. The franchise agreement should apply equally between the franchisor and the franchisee in order to avoid the loss of the party [15]. In relation to franchising involving foreign parties, the franchisor and franchisee usually take procedures commonly used in contract law [16]. There are two different legal systems in a contract, causing the parties to reach an agreement to choose one legal system [17]. To support the development of franchise industries in Indonesia, since 2007 the government has made regulations relating to franchises. However, the regulation has not sufficiently protected against foreign franchise recipients. In practice, many franchise recipients feel disadvantaged because the agreement is only one-sided and benefits the franchisor.

The agreement is one of the most important things in the franchise business, because in the concept of the business, it contains clauses that must be agreed upon during the franchise contract. Thus, it is important to conduct a study to find out how legal protection for franchisees and forms of settlement if there is a dispute from the agreement between the foreign franchisor and the franchisee in Indonesia. The results of this study are expected to provide input for improving franchise regulations, as well as the application and supervision.

2. Method

The legal protection theory is the basis of analysis to find the substance of the franchise agreement, by assessing the laws and regulations made by the competent authority and agreements made by the parties. Observations and interviews are conducted to complete understanding of the effectiveness of the form of dispute resolution. Normative research is directed at the Government Regulation of the Republic of Indonesia No. 42/2007 on Franchising (Government Regulation on Franchising) and Regulation of the Minister of Trade of the Republic of Indonesia No. 57/M-Dag/Per/9/2014 on Amendments to the Regulation of the Minister of Trade No. 53/M-Dag/Per/8/2012 on Franchising Organizations (Ministerial Regulation on Organizing Franchises). The results of the study are then analyzed and described qualitatively.

3. Discussion

3.1 Franchise Agreement

By law, a franchise is an engagement whereby one party is given the right to use and or use intellectual property or a meeting of the characteristics of a business owned by another party with a reward based on the requirements set by the other party in the context of providing and or selling

goods and services. Franchising grew in the 1980s when foreign franchises entered Indonesia, such as Kentucky Fried Chicken (KFC), Mc Donald's, Burger King and Wendy's [18]. Franchise Industry can grow rapidly because the marketing methods and business development facilities are used by various types of business fields, from restaurants, retail businesses, hair salons, photos, hotels, car dealers, and others.

The example of a growing franchise in Indonesia is Kentucky Fried Chicken (KFC), which is in various places, and the example of a local franchise that is developing in Indonesia is Indomaret, with its outlets spread in various strategic places. Until 1997, there was no legal basis specifically for regulating franchises. In Indonesian civil law the franchise agreement made by the parties including the agreement is not named, so the agreement is made based on a written agreement, which refers to the principle of freedom of contract as stipulated in Article 1338 of the Indonesian Civil Code.

Prior to the enactment of Government Regulation No. 16/1997 on Franchise and Decree of the Minister of Industry and Trade of the Republic of Indonesia No. 259/MPP/Kep/7/1997 on Provisions and Procedures for Franchise Business Registration, franchising can still be carried out through an agreement stipulated in the Book III of the Indonesian Civil Code, because all agreements can be justified as long as they are legally carried out as well as not against the law and decency [19]. In civil law, there are at least five important principles that must be fulfilled, including: the principle of freedom of contract; principle of consensualism; the principle of legal certainty (*pacta sunt servanda*); the principle of good faith (*geode trouw*); and personality principles (personality) [20]. The agreement that has been made cannot be withdrawn, other than by agreeing on both parties, or for reasons stated by law. The agreement must be carried out in good faith. Thus, the franchise agreement is not specifically regulated, because the system adopted in the Indonesian agreement law is an open system and contains a principle of freedom of contract [21].

In the contract law, the concept of a franchise business is a special agreement because it is not regulated in the Civil Code [16]. This agreement is acceptable, because the principle of freedom of contract is the right of the parties. Agreements made legally apply as laws for those who make them. Based on the analysis and conditions of the agreement conditions, the franchise is held according to a written agreement between the franchisor and the franchisee. If the agreement written in a foreign language, it must be translated into Indonesian and delivered at least two weeks before signing the agreement to be studied by prospective franchisees. The franchisee must have proof of legality legalized by a notary and a certificate from the Indonesian trade attache or representative officer in the origin country.

According to Article 2 of the Government Regulation No. 42/2007 on Franchising, there are several criteria that must be met in a franchise agreement, including: Having a business characteristic; proven to have provided benefits; have a standard for services and goods and/or services offered made in writing; easy to teach and apply; continuous support; and registered intellectual property rights. In the Ministerial Regulation concerning the Implementation of Franchising, also regulated the processes and obligations that must be carried out by both parties, in running the franchise business, one of which is about the obligation of the franchisee to have the Franchise Registration Certificate (STPW) and register the franchise agreement.

The latest provisions regarding the prohibition of monopolistic practices and unfair business competition, determine that the franchise agreement is included in the jurisdiction of business competition law. Especially, in some aspects related to price fixing or resale price maintenance, tying agreement, exclusive dealing contract, and post expiry non competition. Based on Article 6 of the Ministerial Regulation on Organizing Franchises, franchise business activities must comply with the provisions of legislation in the field of consumer protection, health, education, environment, spatial planning, labor, and intellectual property.

In classical theory, there are two forms of franchise organizations, namely, Franchising Association and Manufacturer Sponsorship franchise. The first form refers to the implementation of wholesalers for marketing products or services. While, for the second form, the manufacturer (franchisor) forms independent distribution networks, based on the conditions set by the manufacturer. Modern franchise refers to the type of Business Format Franchises (BFF). More than 80% of franchises in the world apply this type. There are three known BFFs, such as: Product and Trade Name Franchises (PATNF); Business Format Franchises, and Conversion Franchises (CF) [22].

At present, the BFF type is the most widely used. In this type, franchise recipients are only permitted to run their business strictly. All production processes and business activities, such as business operations, promotion, physical design of outlets must be standard. Unlike, the PATNF, the rules are more flexible. In certain contexts, PATNF is similar to brand or product licenses or dealership systems, as well as marketing automotive products in Indonesia. While, in the CF type the franchisee is a company that has experience in operating similar businesses. This type is not only applied by the hotel industry, but also by consultants and real estate.

Each franchisee is required to have standard operating procedures (SOPs) that become a reference in the company's business, which includes: Operational and service manuals; manual purchase of goods/raw materials and storage methods; marketing, promotion and advertising manuals, bookkeeping manuals and royalty payments, field assistance manuals (field support); quality control and audit manuals; training manual; and site analysis manual (site analysis) [23]. After all requirements have been met, the franchise agreement must be registered with the Ministry of Trade, in Jakarta. Whereas for domestic franchisees or domestic advanced franchise recipients, who already have STPW from the Ministry of Industry and Trade, registration of a franchise agreement can be submitted to the licensing service in the franchise business area.

In addition, in the franchise agreement, the franchisor provides a description of the prospectus regarding the data or information of the business correctly to the franchisee which at least contains: The franchisor's identity, intellectual property rights or findings or characteristics of the business that is the object of the franchise; investment costs; and assistance or facilities provided by the franchisor to the franchisee; and the rights and obligations between the franchisor and the franchisee.

Basically, there are three franchise concepts applied, namely: *Single Unit*, which is a direct relationship between the franchisor and the franchisee; *Multi Unit*, is the relationship between the franchisor and the main franchise recipient in an area or a country, where the main franchisee is permitted to build more than one outlet and is self-managed; and *Sub Franchise*, is the granting of rights from the franchisee to the main franchisee to recruit other franchise recipients [24]. The concept is also generally developed in Indonesia.

Regarding franchise criteria, there are no clear rules governing it. There is no obligation to include financial statements in recent years and has audited by a public accountant, to ensure that a franchise business has been proven reliability. In addition, the criteria for franchising in Indonesian law are not specifically related to intellectual property. Those are some critical notes to improve the franchise law, so that it can provide rules that protect the interests of the parties, and the growth of this business.

3.2 Intellectual Property Rights of Franchise

From an economic perspective, the franchise gives special rights to a person or business entity, to produce or assemble, sell, market a product or service. In the business context, franchise means the freedom to run a business independently in a particular area. Whereas in terms of law, franchise is a legal agreement between two parties in cooperating to produce, assemble, sell, market a service product. As compensation for the use of license rights, the franchisee must pay royalties according to the agreement [25].

Franchising involves areas of contract law, specifically agreements on granting licenses, laws on names of commerce, brands, patents, models, and designs [22]. All of these laws can be grouped in the fields of treaty law and the legal field of intellectual property rights [26]. Elements of intellectual property rights as the most important part of the franchise can be seen from the provisions of Article 1 point 1 of Government Regulation No. 42/2007 on Franchising, which emphasizes franchising as special rights owned by individuals or business entities against business systems with business characteristics in marketing goods or services that have been proven successful and can be used and used by other parties under the franchise agreement. Intellectual property is a component of intangible assets that are important in increasing the growth of the world economy [27].

The substance of regulation of franchise intellectual property is also regulated in Regulation of the Minister of Trade Number 12/MDag/Per/3/2006 on Provisions and Procedures for Issuance of Franchise Business Registration Certificates (Ministerial Regulations Provisions and Procedures for Issuance of Franchise Business Registration Certificates). Based on the provisions of the regulation, intellectual property is a core element of franchises in Indonesia. A business will not be franchised if

it does not contain an element of intellectual property. The franchise agreement has regulated the protection of intellectual property specifically, namely by promising certain restrictions that must be obeyed by the franchisee, aimed at protecting this right from the franchisor. Protection of wealth includes brands, patents, copyrights, and trade secrets [28].

The franchise agreement includes: a). Franchise rights, location, and trial period, b). Franchise period, c). Franchise fees and payment methods, d). Royalties, and e). Image maintenance [29]. In the context of granting the right to use trade secrets, the trade secrets must be something unique and different from the forms of formats, formulas, characteristics, methods, procedures, procedures, or systems that are of a unique nature and have commercial value. Something that does not have a certain uniqueness that can be distinguished from goods or similar services or consists only of a series of information processes that are publicly available and can be held and carried out by everyone without the need for special assistance or guidance is clearly not a trade secret [30].

Previous studies show that the Government Regulation No. 42/2007 on Franchising and Regulation of the Minister of Trade Number 12/MDag/Per/3/2006 on Provisions and Procedures for Issuance of Franchise Business Registration Certificates, has not been effective in providing protection for foreign franchise recipients in Indonesia. In practice, the registration obligation is not always followed by the franchisee. This situation causes supervision by the local trade service to not run well.

3.3 *Franchise and License*

International business development can be done in several ways, such as export, licensing, franchising, joint ventures, acquisitions. As an alternative to expanding the market and reducing costs, a form of cooperation is called for as a license [31]. The license is the permission by competent authority to act which, without such as permission would be illegal, a pass, a tort, or otherwise would not allowable [32].

In relation to the franchise agreement, the license is a right to carry out one or a series of actions provided by the authorized party. Without permission, the action is prohibited and illegal. Through a license, the authorized party to another party to make or sell a product or service. Those who give permission are entitled to receive royalties. The royalty is always connected with the number of products or services sold within a certain period of time. In practice, exclusive or not exclusive licenses not sufficient for the parties. Especially, if the licensor intends to homogenize, which includes the rights and obligations of the operational system and activities.

As the licenses, franchises also rely on the ability of business partners to develop their business through the procedures, processes and codes of conduct, and systems determined by the franchisor. As part of the compliance of business partners to the rules, the franchisee is granted the right to use intellectual property, either in a trademark, copyright on logos, industrial designs, patents, or trade secrets. Then, the franchisor is entitled to royalties. Therefore, franchises and licenses can be used to expand business extensively throughout the world, without borders.

In Indonesian law, licenses are regulated in several intellectual property laws. Especially in trademark, copyright, and trade secret laws. In the law, the issuance of permits is essential in the license, which is made in an agreement by the parties. If there is a licensing agreement that can cause consequences that harm the national economy or unfair business competition, the government will cancel the agreement. In principle, licenses differ from the provision of technical assistance related to project implementation. However, it is a permit to use intellectual property rights.

4. Conclusion

The legal protection of intellectual property owned by the franchisor regulates the protection of intellectual property rights specifically, namely by promising certain limits that must be obeyed by the franchisee, which is directly or indirectly intended to protect intellectual property rights by the franchisor. In a franchise agreement that provides intellectual property protection, the provisions of a franchisee must protect the trade secrets provided by the franchisor for a period of at least two years after the franchise term expires. Franchisees are obliged to protect the rights and interests of the franchisor as the holder of the rights to the brand. Settlement of disputes in Indonesia is usually done by deliberation / consensus as an Indonesian legal culture. If a dispute cannot be resolved through deliberation / consensus, then the parties submit the case to the judiciary, in this case the District

Court as the first court. In addition to settlement through the judiciary, it can also be resolved outside the court through alternative dispute resolution by means of consultation, negotiation, mediation, conciliation, or expert judgment carried out peacefully or can also be resolved through an arbitration body.

This study is limited to fast food franchises from the United States. For further research, it is necessary to conduct research on franchises of several business sectors from other countries, with franchise recipients in several cities in Indonesia. Thus, the results of subsequent research can contribute more broadly and significantly.

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