

The Legal Nature of the Franchise Agreement and Its Consequences "Case Study: The United Arab Emirates"

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Abstract

The study aims mainly to identify the legal nature of the franchise agreement by explaining its concept, characteristics, significance, and identifying its consequences. The study also aims to clarify the basic principles that must be taken into account when drafting this agreement. The basic questions for the study are what is the franchise agreement, what are its provisions, and what are the consequences of its existence and absence. The problem of the study is the ambiguity of the legal nature of this agreement and its various consequences on the contracting parties in terms of rights and obligations. Also, the problem of the study is the lack of clarity of the implications of the termination of the franchise agreement. The researcher uses the descriptive and analytical approach as it is the appropriate approach that achieves the objectives of the study and finds solutions to the study problem. The study concludes with many results, the most important of which are the following. The franchise contract has a set of characteristics and advantages that distinguish it from other contracts. Moreover, the study concludes that this contract has not been legally regulated in most Arab countries, unlike foreign countries in which legislative, jurisprudential and judicial efforts have combined to develop a legal theory that is almost integrated for this type of agreement. The researcher concludes with a set of recommendations. The researcher recommends Arab legislators to work on organizing the provisions of the franchise contract by issuing legislation specific to this contract due to its significance in commercial life. The researcher also recommends legislators on issuing a special system for registering franchise contracts to ensure the seriousness of the technical knowledge contained in these contracts, similar to what is followed in many Countries.

Keywords: Franchise Agreement; Franchiser; Franchisee; Franchise Agreement.

1.Introduction

The franchise agreement is one of the important and new contracts largely used in many countries. This contract represents an effective way of transferring the technical knowledge of productive projects in a manner that achieves the objectives of the contracting parties and thus benefitting both of them. The agreement provides the franchisor with an excellent opportunity to rapidly expand his product without creating a financial burden on his capital expenditures. The agreement also provides the franchisor with an opportunity to quickly enter different and new markets. In return, this agreement is a way to attract investments that bring in advanced technology. This contract is a way to develop the national workforce through the training that it receives in the established businesses contributing to raising the efficiency of the manpower, reducing the proportions of funds invested abroad, and increasing investment in medium-sized enterprises based on successful brands. The agreement stipulates not to harm national products and stimulate local companies to rearrange their business to be able to compete against other enterprises in a way that increases the value of their product provided to the consumer (Al-Bishtawi, 2008).

2.The literature Review

The literature review is of great importance in any study as it contributes to understanding the subject of the study. Besides, the literature review helps the researcher to grasp the causes of the factors behind the origins of the franchise agreement. Moreover, the literature review helps the researcher to understand the advantages of this agreement. The significance of the literature review concerning the subject of our study is evidenced by the fact that the literature review provides information that contributes to assisting the researcher in developing the appropriate methodology to answer the questions of this study to achieve its objectives. Here, I mention the most significant literature review.

Mahiaoui (2013) in their study titled “The Franchise Agreement and Its Consequences in Algeria.” aims to shed light on recent agreements, such as the franchise agreement, which has been widely used in America due to the growth of the American economy.

The researchers use the descriptive, analytical and comparative approach. The study recommends that the Algerian legislator should issue a special law regarding the franchise agreement and not follow the general rules since the franchise agreement is a separate contract. The two researchers recommend the Algerian legislator issuing a special law for settling disputes arising from the franchise agreement, as it has certain characteristics over other contracts.

The study of (Shaheen & Shamat, 2020) in their “The Legal characterization of the Franchise Contract: A Comparative Study”. The main objective of the study is for the researchers to acquaint themselves with the legal provisions to which this type of agreement is subject. The researchers state that the problem of the study is that jurisprudence and the judiciary differ on the legal characterization of this agreement. The researchers use the comparative method in addition to the descriptive and analytical method in the study.

The study concludes that most Arab countries, unlike foreign countries, have not legally regulated the franchise agreement. Foreign countries have combined legislative, jurisprudential, and judicial efforts to

develop a semi-integrated legal theory for this type of agreement. The study concludes that there is a jurisprudential and judicial disagreement about the legal characterization of the franchise contract. At the end of the study, the researchers urge Arab legislators to establish a legal regulation for the franchise agreement, and the need to clarify the legal nature of this contract.

Mounir and Hillel (2019) state in their study "The Legal Aspects of a Franchise Agreement" that their study aims to identify the legal aspects of a franchise agreement. The problem of the study is the lack of legal regulation, as well as the difficulty in determining the legal nature of this agreement. The study problem is also the dispersion of the legal aspects regarding the nature of this agreement and its consequences on the contractors. The two researchers use the descriptive and analytical method in addition to the comparative method to achieve the objectives of their study. The study concludes with several findings and recommendations as follows. The most important results are that the concept of commercial franchising is a concept that realizes new investment opportunities leading to the establishment of new businesses as a result of the experience gained from franchisors. Also, it provides new work fields for the franchisee.

The most important recommendations of the study are to work on creating an organizational climate to spread the culture and industry of franchising to include all productive activities, whether the production of consumer goods or fast food, the production of basic or advanced industries, or the provision of educational, health and engineering services.

Qudah. (2015) in his study entitled "The Consequences of a Franchise Agreement and Its Expiration" states that the study aims to gain insight into the most important legal aspects related to the consequences of the franchise agreement by clarifying the material and moral obligations of the franchisors. The researcher states that the problem of the study is the lack of a legal system that clarifies the provisions of this contract and the consequences on its parties, which results in the loss of rights, especially on the franchisee's side. The researcher uses the descriptive and analytical method in the study. The study concludes with some results, the most important of which is that the franchise contract is separate and has its nature, although there may be some similarities with some other contracts in some parts. The study concludes that this agreement has a set of characteristics and advantages that distinguish it from other contracts. The study concludes with a set of recommendations. The researcher recommends that the Jordanian legislator needs to regulate the provisions of the franchise agreement by issuing special legislation for this contract due to its importance in commercial life. The researcher also recommends the legislator setting up a system for registering franchise contracts to ensure the seriousness of the technical knowledge in these contracts, in away similar to what is done in other countries.

3.Study Methodology

The researcher seeks through this study to obtain information to reach the results and thus achieve the objectives of the study. The researcher collects data and then extracts the principles and provisions related to the franchise contract by using the descriptive and analytical approach

4. Framework of study

In this study, we review the concept of a franchise agreement, its characteristics, legal nature, and consequences.

4.1 The concept of Franchise Agreement

The franchise contract is considered one of the most important modern agreements that has come into existence since the beginning of this century, specifically in the second half of it, but its legal nature has remained unclear. The legal systems of various countries have interpreted and applied the franchise agreement in line with their national provisions. This contract did not have a specific definition. Therefore, several international institutions tried to find a definition and establish a disciplined legal system for this agreement due to its high importance, especially following the establishment of the World Trade Organization. The International Institute for the Unification of the Rules of Private Law of the United Nations is one of the institutions seeking to find a definition for the franchise agreement since it prepared a study on this agreement in 1986 (Al-Bishtawi, 2008).

In this part of the study, we review the definitions that attempt to define the concept of a franchise agreement. **They are as follows:**

- A. The British Union defines a franchise agreement as "a contract between two parties. The first party is called the franchisor and the second party is called the franchisee. According to the contract, the franchisee is permitted to undertake, during a certain period, the execution of a specific work under a specific name belonging to or owned by the franchisor, provided that the franchisor continuously controls and oversees the business subject of the franchise agreement. The franchisor is contractually obliged to provide and assist the franchisee with everything necessary to perform the franchise work, especially organizing the administrative aspects of the work, training employees, and providing the franchisee with the needed goods.
- B. The International Franchise Federation defines a franchise agreement as a contractual relationship between two parties, the franchisor, and the franchisee, according to which the franchisor is committed to transferring technical knowledge and training to the franchisee who undertakes the work under a known trade name, form or procedures owned or controlled by the franchisor. In this contract, the franchisee invests money in the business, the subject of the franchise. However, the franchisee solely bears all risks resulting from this agreement (Sidr, 2018).
- C. The French judiciary defines the franchise agreement as a contract by which the franchisor places his trade name, in addition to the initials, trademark, technical knowledge, and a group of goods or services that are produced in original and specific ways at the franchisee's disposal. The franchisee uses these elements by following standardized technical and commercial methods that have been previously tested and are constantly supervised and controlled by the franchisor and under his supervision (Al-Sadat).

Based on the previous definitions, a franchise contract can be defined as: "A contract whereby a person called the franchisor undertakes the education of another person called the franchisee with practical knowledge including transferring technical knowledge, providing technical assistance, authorizing the usage of his trademark, and providing him with goods. As for the franchisee, he is responsible for investing this practical knowledge, using the trademark, receiving goods from the franchisor, in addition to the franchisee's obligation to pay the due prices, and the obligation not to compete against the products of the franchisor and to maintain confidentiality.

4.2. Characteristics of a Franchise Agreement

A franchise contract is a special type of leasing for a specific tangible thing, i.e., technical knowledge and other elements of intellectual property. Therefore, the franchise contract is distinguished by the characteristics of all lease contracts, noting that this contract also includes features that distinguish it from other contracts. The most important of these characteristics are:

- a) Consensual agreement: The franchise agreement is one of the consensual contracts concluded place upon the exchange of offer and acceptance between the parties.
- b) Continuous agreement: The franchise agreement, like other distribution agreements such as the commercial agency, is continuous, meaning that time is an important element of the contract.
- c) An indefinite agreement: The franchise agreement is an indefinite commercial agreement that is not specifically regulated by law nor established in a legal system and therefore it is subject to the general provisions related to contracts.
- d) Personal consideration agreement: The franchise agreement is based on personal consideration and mutual trust between the two parties as it contains the transfer of confidential technical knowledge (Al-Suraihi, 2011).
- e) A legally binding agreement: The franchise agreement is a legally binding contract for both parties, as it imposes on both the franchisor and the franchisee mutual obligations.
- f) Netting agreement: The franchise agreement is a netting agreement as each of the contracting parties is contractually obliged to pay the other party's due in exchange for his obligations, so the franchisee pays the franchisor upon concluding this contract the so-called right of entry in addition to other revenues (Mallouh, 2003).
- g) Compliance agreement: Conditions and bargaining in the franchise agreement between the parties shall only be agreed upon after ensuring that the franchisor is economically superior to the franchisee so that the franchisor can impose his will on the franchisee, and imposes conditions on the franchisee that he cannot argue against. The franchisee has to accept or reject the conditions, and if he accepts them, then it is a recognition of the conditions (Dawas, 2004).
- h) Commercial agreement: The franchise agreement is a commercial agreement since the capacity granted to the franchisor or the franchisee is consistent with the requirements required to obtain the capacity of a trader. Accordingly, the rules of the commercial law apply to this contract (Muhammadin, 1989).

- i) Training agreement: What distinguishes the franchise agreement from other agreements is that the franchisor is not only obliged to provide technical assistance, but also to train the franchisee and to prepare him to undertake the activity on his behalf. The franchisor is obligated to educate the employees of the franchisee within the framework of cooperation and the complete legal independence of each of the contractors (Maghbebg, 2006).

4.3 The Legal Nature of the Franchise Agreement

The franchise agreement is similar in many elements to some other agreements. This requires clarification of the different elements of this contract by reviewing them as follows

- The element of satisfaction: satisfaction in contracts is a legal term that means that both contractors agree on the key elements of the contract in the sense that the two wills coincide towards producing a legal effect. The contracting parties must have the legal capacity to conclude contracts and legal actions, as well as they must be free from any defects such as coercion, fraud, and deceit (Al-Sanhoury, 1970). In a franchise agreement, the franchisor sends an offer that includes specific items addressed to a specific person that the franchisor chooses, or an offer addressed to the public. Later, the franchisor chooses the franchisee from among different franchisee candidates. The contract is concluded as soon as the franchisee accepts the franchisor's offer, and the contract is concluded without requirements or any special condition (Habib, 2008).
- The Object of the agreement: The franchise agreement is concluded when both contractors agree to produce a legal effect. Will is an essential element of the contract and this will aim at achieving a legitimate goal, which is called the cause and it is the second element of the contract. The franchise Agreement creates a set of obligations for both parties (Tanagu & Mansour, 1997). In this regard, we will study the obligations based on the following issues: technical knowledge, technical assistance, and elements of intellectual property.

1. Technical knowledge

Technical knowledge or expertise has confidential nature, which is necessary to achieve and implement some technical methods with industrial objectives. There are several conditions for technical knowledge within the framework of the franchise agreement. **They are the following:**

- Technical knowledge is confidential: it is not necessary that confidentiality be absolute, as the production process at present requires allowing many workers within the business to access the used technical knowledge, which increases the likelihood that this technical knowledge will be leaked to the competing companies. Besides, the owner of the technical knowledge (franchisor) may license others than the franchisee to use this knowledge (Muhammadin, 1989).
- Right of use, right of usufruct, and right of value: This condition refers to the actual usage of the technical knowledge, which gives technical knowledge a certain utility, and thus gives the franchisor an economic advantage.

- Technical knowledge is easy to transfer technical knowledge is the main advantage of franchising, as it allows non-professionals to undertake certain tasks that were impossible for them to undertake before.
- Technical knowledge is capable of being displayed: technical knowledge displays its importance while preserving its confidentiality, and the review process for the confidentiality of technical knowledge plays an essential role in announcing the activity of the franchisor and what his business offer.
- Technical knowledge is innovative: technical knowledge adds new value to the franchisor by giving him an advantage over his competitors. This advantage would not have been achieved unless he incurred extraordinary expenses and effort (Al-Bishtawi, 2008).

2. Technical assistance

Technical assistance in the franchise agreement is to provide assistance and to give all that is technically required and to put all methods and means at the disposal of the other party wishing to obtain this technicality (franchisee). In general, technical assistance is a tangible form of technical knowledge. **The assistance provided by the franchisor includes the following:**

Preparing sales training programs or training on after-sales service methods -Improvement and renewal of goods and equipment.

- Advising the franchisee to adopt a specific tax accounting system.
- Establishing a system and holding meetings from time to time, and holding lectures at the local or international levels to implement these methods.
- Assisting the franchisee in choosing the location of the new store in which the franchisee will start his business activities.
- Assisting in choosing working hours.
- Assisting in choosing clients. It should be noted that this assistance has a price contained in the contract (Al-Haija, 2006).

3. Elements of intellectual property.

Intellectual property is one of the most important components of the franchise activity, as it is the main reason for creativity and distinction in this activity, which leads to franchise development and prosperity (Mahrez, 1998).

Here we review the elements of the intellectual property accordingly:

a. patent, b. Industrial designs, c. Logo, d. Trade Name, e. trade mark, f. Name of the website (Khater, 2005).

- The Element of a cause: The element of cause is the direct intended purpose of the contract. The validity of the cause requires that its purpose be legitimate. The jurisprudence has differed

regarding the classification of the cause, and whether it is considered an element of the contract or an element of obligation. In any case, it can be said that the cause is one of the objective key elements of any contract

According to the franchise contract, the reason for the franchisee's obligation to pay a royalty is to join the network of the franchise. Also, the franchisee pays the periodic royalty to be able to obtain the technical knowledge provided by the franchisor coupled with assistance and licensing the use of distinctive trademarks.

The reason for the franchisor to provide these elements is to obtain the amount of the royalty in addition to expanding the popularity of the franchised product (El-Shahawi, 2003).

Based on the general rules in contracts, the cause for contracting a franchise is subject to the general rule in obligations. If the cause is not mentioned in the contract, then the law provides a legal presumption according to which it is assumed that the contract has a legitimate cause, and that the presumption accepts proof of the opposite (Qurra, 1987).

As a general rule, the cause for contracting the franchise is nothing more than the same cause for the existence of commercial contracts, which is represented in achieving profit for both contractors.

4.3 Consequences of a Franchise Agreement

The franchise agreement is one of the mutually binding contracts. It arranges several obligations on both the franchisor and the franchisee of the franchise, and here we mention the most important of these obligations as follow:

a) Obligations of the franchisor.

Here we refer to the most important obligations that the contract entails on the franchisor. Failure to fulfill these obligations will result in the termination of the contract.

- Allowing the franchisee to use the trademark and all commercial signs and symbols indicating the franchisee' joining the franchise network.
- Transferring technical knowledge to the franchisee (Al-Shafi).
- Providing the necessary technical and commercial assistance to implement the franchise contract.
- Exclusively supply the franchisee as the contract includes an exclusivity clause (Shammas, 1998).

b) The franchisee's obligations

There are some obligations on the franchisee. Failure to implement these obligations gives the franchisor the right to terminate the contract and claim compensation

- Paying fees for entering the franchisor's distribution network.
- Paying the installments agreed upon in the contract (Jalloul, 2001).
- Obligation to applying technical knowledge following the franchisor's instructions.
- Obligation to maintaining the confidentiality of technical knowledge.
- Obligation to effective cooperation in implementing the franchise system.
- Obligation not to compete against the franchisor's business during the implementation of the contract (Mansour, 1999).

5. Conclusion

Based on the foregoing, it can be said that the franchise agreement is one of the newer agreements that have been widely used in many countries of the world. However, most Arab countries do not give this agreement the required importance and only consider it one of the commercial agreements, and thus its provisions are subject to the rules of general commercial agreements.

The study concludes with several results and recommendations, the most important of which are:

1. The new conditions arising from globalization and the technological revolution are among the most important aspects that have direct impacts on the establishment of the franchise agreement.
2. The franchise agreement has a set of characteristics and advantages that distinguish it from other agreements. Unlike foreign countries, this agreement does not enjoy legal regulation in most Arab countries. In foreign countries, there have been concerted legislative, jurisprudential, and judicial efforts to develop a semi-integrated legal theory for this type of agreements.
3. The specificity of the franchise agreement is centered around its legal nature, which is manifested by one or more other elements of industrial and commercial ownership, in addition to the technical knowledge that distinguishes it from other similar agreements.
4. The obligation of the franchisor towards the franchisee is not limited to franchisor's mere license to the franchisee to use one of the elements of the intellectual property belonging to him and his transfer of the technical and technical knowledge necessary for that. Rather, he must provide the necessary assistance, guidance, and supervision to the franchisee for so long.
5. The researcher recommends to Arab legislators the necessity to regulate the provisions of the franchise agreement by issuing special legislation for this agreement due to its importance in commercial life.
6. The researcher urges legislators to set up a special system for registering franchise agreements to ensure the seriousness of the technical knowledge contained in these agreements, similar to what is followed in many countries.
7. The researcher recommends using clear and explicit legal texts concerning the franchise agreement, a matter that contributes to resolving the legal and jurisprudential debate on this issue.

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