

Franchising in the UAE

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When walking from the car park of the Dubai International Financial Centre to my office each morning, I pass a Costa Coffee, Caribou Coffee, Caffe Nero, a Yo Sushi restaurant, a Gourmet Burger Kitchen restaurant and a Potbelly Sandwiches outlet (among others). Thankfully the DIFC also has a Fitness First gym!

Clearly, franchising is a very popular method of conducting business in Dubai. When attending the recent Retail City Conference held in Dubai as part of the Cityscape Global event, the general impression was that notwithstanding the recent (and also the not so recent) global economic woes the retail sector in Dubai, and in the UAE generally, is remaining remarkably resilient. Certainly at Al Tamimi we continue to see a steady flow of enquiries from both franchisees and franchisors relating to the establishment of new franchised brands in the UAE.

In this article I will look at the main legal considerations for a potential franchisor in connection with the appointment of a franchisee in the UAE.

The UAE Commercial Agencies Law

The main piece of legislation to consider in the context of franchise arrangements in the UAE is Federal Law No. 18 of 1981 on the Organisation of Commercial Agencies (as amended by Federal Law No. 14 of 1988, and further amended by Federal Law No. 13 of 2006 and Federal Law No. 2 of 2010) (the “Commercial Agencies Law”). The Commercial Agencies Law has potential application not only to what would be strictly considered as agency agreements in many foreign jurisdictions but also to agreements regarding franchises, distributorships, commission arrangements, dealerships and other forms of sales representative or sales agency relationships.

I say “potential” application as the Commercial Agencies Law only applies to contracts that are registered with the UAE Federal Ministry of Economy (the “Ministry”). In order for a contract to qualify for registration with the Ministry there are a number of criteria which must be met, the main ones being:

- The franchisee must be a UAE national or an entity that is wholly owned by UAE nationals;
- The franchise agreement must grant exclusivity over all or a part of the UAE; and
- The franchise agreement must be notarized.

Some franchisees may claim that unless a franchise agreement is registered with the Ministry it is not legally valid. This is not the case (the reasons for them wanting to register such an agreement are discussed below). There are many franchise agreements in the UAE that have been entered into between foreign franchisors and local limited liability companies, for example, where such companies have a 49% foreign shareholding (i.e. they are not 100% owned by UAE nationals) or that are not exclusive which are valid arrangements notwithstanding that they do not qualify for registration with the Ministry. Further, even franchise agreements which may meet the qualifying criteria for registration with the Ministry do not have to be registered although in such circumstances franchisor’s should bear in mind that a franchisee may later approach the UAE courts for an order that the agreement be registered in order to obtain the protections offered by registration.

Unregistered arrangements are governed by the various UAE federal laws applicable generally to commercial arrangements such as the UAE Civil Code and the UAE Commercial Transactions Law. In general terms, these laws recognize the right of parties to contract with each other on such terms as they may agree although there is scope under such legislation for a franchisee to claim damages upon the

cancellation of the agreement by the franchisor even if such cancellation is done in accordance with terms of the agreement. However, in this article we will focus on the effect of registration of franchise agreements with the Ministry.

Consequences of registration under the UAE Commercial Agencies Law

If an agreement qualifies, franchisees generally prefer to register an agreement with the Ministry. The main consequences of registration are:

- The agreement cannot be terminated by the franchisor without the franchisor being able to show “justifiable cause” even if the franchisor has a clear contractual right to terminate in the franchise agreement itself.

It is very difficult for a franchisor to establish “justifiable cause”. Matters that may amount to justifiable cause would include the franchisee no longer being appropriately licensed to undertake the franchised activity in the UAE, repeated material breaches of the terms of the franchise agreement and/or gross negligence, and dealing with competitive products where this is clearly prohibited under the terms of the franchise agreement. In practice, the circumstances surrounding the termination of a registered franchise agreement will be considered in view of assessing what would be an appropriate compensation payment, if any, to be awarded to the franchisee as a result of the termination of the agreement. If a justifiable cause is found to exist then it may be that the commercial agencies committee (or court on appeal, see below) will find that no compensation is payable to the franchisee.

- The franchisee is able to instruct the UAE ports and customs authorities to prohibit any products in respect of which it is the registered agent entering the UAE without its consent. While this provides good protection against parallel imports it also puts a registered franchisee in an extremely strong negotiating position in the event that a franchisor wants to terminate an agreement and appoint a replacement franchisee. This is because the registered franchisee can force the franchisor to go to the commercial agencies committee (and, potentially, then to the local courts on appeal) to seek termination of the registered agreement and while such case is being heard the registered franchisee (who will remain registered until a judgment for de-registration is given or a settlement reached between the parties) can block the importation of the franchisor’s products into the UAE. This, in practice, restricts the franchisor from access to the UAE market, either by way of itself establishing a licensed presence in the UAE or by appointing an alternative franchisee, until the case has been finally determined or settled and the agreement de-registered. A final determination, if a decision of the commercial agencies committee is appealed to the local courts, may take in the region of 3 years (or possibly longer) to obtain.
- The factors that the commercial agencies committee (and local court, if appealed) will take into account when assessing the level of compensation payable to a registered franchisee upon termination of the arrangement include the performance of the franchisee, how long the arrangement has been in place and whether the franchisee has incurred significant expenditures in establishing the business (with more weight being given to more recent expenditures).

As a result, franchisors generally consider it preferable not to have their agreements registered. This is an issue that needs to be fully understood by any franchisor looking to appoint a franchisee in the UAE prior to the franchisor entering into any negotiations with a potential franchisee.

Recent developments regarding the UAE Commercial Agencies Law

By way of background, the UAE Commercial Agencies Law was amended in 2006 to make it more favourable to principals and less protectionist towards local registered agents. The key changes made at that time were (i) the abolition of the commercial agencies committee (a committee established under the auspices of the Ministry and whose role was to hear disputes between registered agents and principals) with the result that disputes were to be referred directly to the UAE courts (who were generally considered at that time to be less sympathetic to local agents than the commercial agencies committee had been), and (ii) allowing principals to unilaterally deregister fixed term registered agreements upon the expiry of

their term (and the practice of the Ministry at one stage extended to allowing principals to de-register agreements by notifying the Ministry of their intention to give notice of non-renewal of agreements that contained automatic renewal provisions).

However, in 2010 the Commercial Agencies Law effectively reverted to the pre-2006 position with the reintroduction of the commercial agencies committee and the removal of the right of principals to de-register agents upon the expiry of a fixed term agreement. The UAE's reaction to the economic crisis was to become more protectionist with regard to local agents. The commercial agencies committee has only just started to accept disputes and it remains to be seen what the committee's general approach it will be and how successful it is in providing a considered and fair forum for the resolution of disputes between registered agents and principals.

A few other issues.....

By way of conclusion, I thought it may be helpful to mention a few other UAE specific matters that I have come across when dealing with franchise arrangements in the UAE.

I am often asked if an agreement has to be in Arabic and/or notarized to be valid. As mentioned above, if an agreement is to be registered then it must be notarized (and in order to be notarized it must be translated into Arabic). However, if an agreement is not registered then there is no need for it to be notarized or translated into Arabic to be valid.

I have also come across certain cultural issues such as a clause regarding uniforms being amended to include a reference to "giving due regard to cultural sensitivities". While Dubai is reasonably relaxed when it comes to dress requirements other Emirates and countries in the region have stricter requirements and, for example, it is always considered appropriate for female employees to wear conservative clothing. There are also issues regarding restrictions on serving pork products and alcohol and this may also need to be provided for in the franchise agreement (for example, in the context of the franchisor being entitled to determine menu items in restaurant franchises).

I am sure that franchising will continue to play a major role in the UAE economy going forward and franchisors should not be afraid to do business here. However, there are certain UAE law specific issues that do need to be dealt with over and above the standard issues that arise in the context of negotiating franchise agreements and it is always advisable to get local law advice before entering into any franchise arrangement.

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