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Recent Changes to Indonesia’s Franchise Regulation: Opportunities & Challenges Ahead

Indonesia’s updated franchise rules present a mixed bag for franchisors. The good news is that the requirement to demonstrate profitability has been shortened from five years to three, making it easier for new franchisors to enter the Indonesian market. However, these changes also come with new obligations for documentation and continuous support to franchisees, which could add operational complexity.

The new regulation, Government Regulation No. 35 of 2024 on Franchising (“**GR 35/2024**”) came into effect on 2 September 2024, replacing Government Regulation No. 42 of 2007 on Franchising (“**Old Regulation**”). This update aims to address the gaps in the previous framework, especially around financial accountability and support for local franchises, to better reflect the industry’s growth and evolving needs.

Here are highlights of what franchisors need to know under GR 35/2024.

1. Franchise Criteria

GR 35/2024 clarifies franchise criteria, outlining the following key items with detailed explanations.

No.	Criteria	Remarks
1.	Franchise business system	<p>The franchise business system covers everything from daily operations to long-term strategies. It includes operational standards and procedures, covering aspects such as human resources management, administration, operational management, standard operating methods, business location selection, business premises design, employee requirements, and marketing strategies.</p> <p>The system must be thoroughly documented, easy to teach and apply, and fair for both the franchisor and franchisee.</p>

No.	Criteria	Remarks
		<p>In contrast, the Old Regulation and Minister of Trade Regulation No. 71 of 2019 on Franchise Operations (“Regulation 71/2019”) did not classify the franchise business system as a franchise criterion. Instead, it treated it as a unique business characteristic.</p> <p>Regulation 71/2019 remains in effect, provided it does not conflict with GR 35/2024. If there are any conflicting provisions between GR 35/2024 and Regulation 71/2019, the provisions of GR 35/2024 will apply.</p>
2.	Profitable business	<p>Under the new regulation, a franchised business must have operated for at least three consecutive years, easing the previous five-year requirement under Regulation 71/2019.</p> <p>In addition, franchisors must provide financial statements for the last two years that demonstrate profit and have been audited by a public accountant who issues as an ‘unqualified opinion’ (clean report) confirming that they accurately reflect the entity’s financial position according to Generally Accepted Accounting Principles (GAAP).</p> <p>However, micro and small-scale business franchisors are exempt from the requirement for audited financial statements.</p>
3.	Registered intellectual properties	<p>Intellectual properties can be in the form of trademarks, copyrights, patents, trade secrets, industrial designs, or integrated circuit layouts. Copies of the registration or recordation certificates should be available.</p>
4.	Ongoing support	<p>Franchisors must provide ongoing support to support franchisees, including training, operational management, promotion, research, market development, and other forms of support.</p> <p>Under GR 35/2024, if a franchisor fails to provide this support, the franchisor may face progressive sanctions against the franchisor, including written warnings, temporary suspension of business activities, and revocation of the franchise registration certificate (“STPW”).</p>

2. Prospectus

GR 35/2024 adjusts the timeline for franchisors to provide a prospectus to franchisees, now requiring delivery by 14 calendar days before signing the franchise agreement. This update replaces the previous two-week requirement under Regulation 71/2019. This shift to 'calendar days' clarifies the timeframe, removing ambiguity around weekends and holidays.

New requirements include that the franchise business system must be reflected in the prospectus, and that the intellectual property certificate or recordation letter must be included. Previously, franchisors could use a filing receipt for pending intellectual property registration or recordation, but GR 35/2024 now imposes stricter requirements.

In addition, while GR 35/2024 requires that the prospectus be prepared in Indonesian, it does not explicitly require prospectuses in foreign languages to be translated by a sworn translator.

3. Franchise Agreement

GR 35/2024 adds a few additional requirements for Franchise Agreements beyond the mandatory provisions set out under the Old Regulation and Regulation 71/2019. The new regulation requires that Franchise Agreements include provisions regarding the business system and a guarantee from the franchisor that the franchisee is entitled to receive compensation and/or the right to continue the franchise operation if the franchisor ceases its business. This new provision is aimed at safeguarding the franchisee's rights and clarifying the franchisor's responsibilities if the franchisor's business shuts down, though it may be a burden for the franchisor. Unfortunately, GR35/2024 does not provide further details on how this guarantee should be implemented.

4. Franchise Registration Certificate

GR 35/2024 clarifies the timeline for franchisors to apply for their STPW before preparing the Franchise Agreement, while both the Old Regulation and Regulation 71/2019 were silent about this timeline. Franchisees, on the other hand, must obtain their STPW before starting the franchise business in Indonesia.

5. Data Changes

GR 35/2024 requires both the franchisor and franchisee to update their STPW through the OSS (Online Single Submission) system if there are any changes to:

- a. the Prospectus, except for details related to the financial statements for the last two years, the number of outlets, and the list of the franchisees; or
- b. the Franchise Agreement.

Failure to comply with this requirement will result in the imposition of progressive sanctions against the franchisor and the franchisee. These include written warnings, temporary suspension of business activities, and STPW revocation.

6. Supporting Domestic Products

GR 35/2024 emphasizes that franchisors and franchisees should prioritize the use local products and/or services, as well as favor the processing of raw materials within Indonesia. This provision aims to support local industries and strengthen the domestic supply chain in franchise operations.

7. Annual Reporting Requirement

Regulation 71/2019 requires both local franchisors and franchisees to submit an annual report on franchise activity by 30 June each year. GR 35/2024 expands this requirement by mandating additional information, including the status of intellectual property registration. This to ensure that the franchisors maintain valid registration or recordation of intellectual property in Indonesia while operating their franchise business.

Failure to comply with this requirement will result in progressive sanctions for both the local franchisor and the franchisee, including written warnings, temporary suspension of business activities, and STPW revocation.

8. Prohibition on Considering an Agreement as a Franchise

GR 35/2024 imposes stricter controls on the use of the term “franchise” in business activities. Both individuals and business entities are prohibited from using the term ‘franchise’ in their business activities if they lack an STPW. This represents a stricter requirement than Regulation 71/2019, which only prohibited business entities without an STPW from displaying the franchise logo.

Conclusion

In summary, GR 35/2024 introduces detailed provisions for conducting franchise business in Indonesia and adds new obligations on franchisors as well as franchisees to ensure compliance. Franchisors and franchisees operating in Indonesia will need to need to adjust their practices to align with the updated requirements, including ensuring that any changes to the prospectus or franchise agreement are reflected in the OSS system. This may also affect existing arrangements, requiring updates to maintain compliance.

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