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UNDERSTANDING THE LEGAL FRAMEWORK FOR FRANCHISING IN INDIA

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Abstract :

Franchising in India functions within a broad legal framework, as there is no specific law dedicated solely to franchising. Franchise agreements are primarily governed by the Indian Contract Act, 1872, which requires clear terms on the rights and responsibilities of both parties. Intellectual property rights are safeguarded through the Trade Marks Act, 1999 and the Copyright Act, 1957. The Competition Act, 2002 ensures that franchise agreements do not restrict competition, while the Consumer Protection Act, 2019 holds businesses accountable for service standards. Franchise fees and royalties are subject to GST, and foreign franchisors must comply with FEMA regulations regarding royalty payments. In the absence of a dedicated franchising law, judicial rulings and industry practices influence franchise operations. Given the sector's rapid growth, there is a need for more specific regulations to ensure sustainable and compliant franchise models.

Key words ; Franchising, FEMA, Rapid growth, GST, Ensure sustainable

Introduction:

Franchising has become a widely adopted and rapidly expanding business model in India, drawing attention from both local entrepreneurs and international companies. The industry is experiencing a strong annual growth rate of approximately 30%, driven by growing consumer demand for branded products and services, favorable government initiatives, and the country's steady economic progress. Although the origins of franchising date back several centuries—tracing to feudal systems and royal licenses granted in medieval times—its formal structure began to take shape with the introduction of the guild system in 12th-century London. While franchising in India is yet to develop into a fully organized industry, it is steadily gaining momentum as a popular method for business expansion and distribution of goods and services, a trend already well-

established in countries like the United States and the United Kingdom.

Franchising presents a range of advantages for both franchisors and franchisees. However, thriving in the Indian market requires a comprehensive understanding of the country's legal framework. Key legal aspects include intellectual property rights, the drafting and enforcement of franchise agreements, regulations related to advertising and marketing, labor laws, and taxation. Proper compliance with these regulations is essential to ensure smooth operations and avoid potential legal pitfalls.

This paper aims to provide an overview of the concept of franchising, highlighting its benefits and associated risks. It further delves into the legal dimensions of franchising in India, emphasizing the critical role of a well-drafted franchise agreement. The goal is to offer a

foundational guide for those exploring or entering into franchise partnerships within the Indian context.

Franchising:

Indian law does not explicitly provide a definition for franchising. Nonetheless, in general terms, franchising can be understood as a method for distributing goods or services. According to Black's Law Dictionary, a franchise refers to a license granted by the proprietor of a trademark or trade name, allowing another party to offer products or services under that established brand.

Typically, a franchise arrangement involves two main parties:

1. The franchisor – the individual or entity that owns the trademark or trade name and the underlying business model, which is shared with others.

2. The franchisee – the individual or entity that pays an upfront fee and/or ongoing royalties in exchange for the right to operate using the franchisor's brand and established system of operations.

Key Characteristics of Franchising:

Drawing insights from definitions provided by the British Franchise Association, the International Franchise Association, and the U.S. Federal Trade Commission, several core features of franchising can be identified:

(a) Franchising is fundamentally established through a contractual agreement between the parties involved.

(b) The franchisor typically offers a proven business model or system, which is associated with a recognized brand.

(c) The franchisee usually invests a significant amount of capital at the outset and assumes ownership of the day-to-day business operations.

(d) The franchisor is generally responsible for training the franchisee, ensuring they are well-

prepared to operate within the guidelines of the established system.

(e) After the franchise is operational, the franchisor continues to offer assistance in specific areas of the business to support the franchisee.

(f) To safeguard the brand's reputation and maintain consistent quality, the franchisor routinely monitors and evaluates the franchisee's operations.

(g) In exchange for the rights granted and ongoing support, the franchisee typically pays a fee or royalty to the franchisor.

Types of Franchising Agreements:

Franchising can take several forms depending on the nature of the business, the level of control, and the territorial scope of operations. The most common types of franchising agreements include,

i. Product Distribution Franchise:

In this model, the franchisee is authorized to distribute the franchisor's products, often with the use of the brand name. This type is common in industries such as automobiles, soft drinks, and petroleum. The focus is more on product distribution than on the business format itself.

ii. Business Format Franchise:

This is the most widely used form of franchising. Here, the franchisor provides not just the product or service but also a complete business system, including branding, training, operations manuals, marketing support, and ongoing assistance. Fast food chains, retail stores, and service-based brands often adopt this model.

iii. Manufacturing Franchise:

In this arrangement, the franchisor allows the franchisee to manufacture and sell products using the franchisor's brand name, trade secrets, and proprietary processes. This is common in the food and beverage, apparel, and automotive sectors.

iv. Master Franchise:

A master franchisee is granted the right to operate and also to sub-franchise within a defined geographical area. This type is particularly useful for international expansion, where local partners understand the market better.

v. Area Development Franchise:

Under this agreement, the franchisee commits to opening and operating multiple franchise outlets within a certain region over a specified period. Unlike the master franchise, the area developer does not sub-franchise but retains ownership of all outlets.

vi. Joint Venture Franchise:

In a joint venture model, the franchisor and franchisee enter into a partnership or joint venture to run the business together. This is often used when entering a new market where local insight is critical.

Compliance issues in Indian Franchising:

Franchising is a growing business model in India, but it comes with several legal and regulatory challenges. Key compliance areas include intellectual property protection, proper drafting of franchise agreements under Indian contract law, adherence to advertising norms, employment laws, and tax obligations. Though the Indian Contract Act doesn't mandate written agreements, formal contracts are essential for franchises. Issues like franchisor liability and high taxation on royalties can discourage foreign investment. Cases like Gujarat Bottling Co. Ltd. vs Coca-Cola Co. highlight the need for clearer franchise laws. Franchisors must also ensure IP registration and that franchisees follow employment, advertising, and tax regulations.

Regulatory framework for Indian Franchise Agreements:

Laws Applicable - Indian franchise agreements are not governed by a single dedicated law but are influenced by several statutes. These include various legal enactments that collectively form the regulatory framework for franchising in India.

1.The Indian Contract Act, 1872 outlines the legal framework for all contracts, including franchise agreements. It covers essential elements like offer, acceptance, consideration, and the legal capacity of parties, along with their rights and duties.

2.The Consumer Protection Act, 1986 safeguards consumers' rights and provides remedies for faulty goods or services. Since franchisees use the franchisor's services, franchise agreements fall under this law's scope

3.The Trade Marks Act, 1999 and the Copyright Act, 1957 safeguard intellectual property like trademarks and copyrights, which are vital for franchisors to operate and protect their brand.

4.The Specific Relief Act, 1963 offers remedies like specific performance and injunctions, helping franchisees if a franchisor breaches the agreement.

5.The Foreign Exchange Management Act, 1999 regulates foreign exchange dealings in India, including royalty payments and fund repatriation to international franchisors.

6.The Transfer of Property Act, 1882 governs property transfers, including lease rights, which may apply to franchise agreements involving leased premises.

7.The Income Tax Act, 1961 imposes tax on franchisors' earnings in India, including royalties received from franchisees.

8.The Information Technology Act, 2000 gives legal validity to digital signatures and electronic records, aiding in the online execution of franchise agreements.

Standard Terms and Conditions:

The legal requirements for franchising in India include standard terms and conditions in the Franchise Agreement.

1.Franchise agreements in India should include balanced terms for both parties, covering aspects like termination, renewal, and geographic exclusivity.

2. Geographical exclusivity clauses should clearly define the area where the franchisee holds exclusive rights to operate.

3. Training and support provisions should outline the nature and extent of assistance the franchisor will provide to the franchisee.

4. Marketing and advertising clauses should clearly define each party's duties in carrying out promotional activities.

5. Termination and renewal clauses should specify the terms for ending the agreement and the process for its renewal.

Registration and approval requirements:

Franchisors in India must complete necessary registrations and approvals, such as trademark registration and licenses, before finalizing franchise agreements. Non-compliance can lead to legal penalties.

These requirements may vary across different states, depending on local regulations. Ensuring proper registration helps protect the franchisor's brand and ensures smooth business operations.

Termination and Renewal Provisions:

Franchise agreements in India must clearly outline termination and renewal conditions, detailing grounds for termination like contract breaches or nonpayment. Renewal clauses should specify how the agreement can be extended and any related fees.

These provisions ensure both parties are aware of their rights and responsibilities throughout the agreement's duration. Clear terms also help avoid disputes and provide a structured process for continuing or ending the franchise relationship.

Case study:

Domino's Pizza in India :

Domino's Pizza, a global fast-food chain, entered the Indian market in 1996 through a franchise agreement with Jubilant FoodWorks Ltd. (JFL). Since then, it has rapidly expanded across India, thanks to its effective marketing

strategies and focus on local tastes. A key factor in its success has been its adherence to India's franchising legal framework, including intellectual property protection, well-drafted franchise agreements, and compliance with registration and approval requirements.

Domino's Pizza's experience underscores the importance of following franchising laws. Other franchisors aiming to enter India should work closely with legal experts to ensure full compliance with all relevant regulations.

Suggestion :

1. A well-drafted franchise agreement is essential to clearly define roles, obligations, fees, duration, renewal, and termination conditions.

2. Trademark registration is crucial to protect the franchisor's brand and ensure legal usage rights by the franchisee.

3. Intellectual property, including business processes, logos, and trade secrets, must be legally licensed and safeguarded.

4. Foreign franchisors must comply with FEMA regulations, especially for royalty payments and remittances.

5. Though not legally required, transparent disclosure of business details builds trust and helps avoid legal conflicts.

6. Legal due diligence and expert consultation are vital before entering into any franchise arrangement to mitigate risks.

Conclusion :

Franchising in India demands a thorough understanding of various legal dimensions to ensure a smooth and compliant business operation. Although there is no single, dedicated law governing franchising, the relationship is primarily regulated through the Indian Contract Act, supported by laws related to intellectual property, foreign exchange, and sector-specific regulations. A clearly articulated franchise agreement forms the backbone of this relationship, as it outlines key terms such as

rights, responsibilities, territorial limits, duration, termination conditions, and dispute resolution methods. The protection of intellectual property, especially trademarks, is critical because the franchise system heavily relies on the brand's reputation and recognition. Ensuring that trademarks and other proprietary elements are registered and licensed appropriately safeguards the interests of the franchisor and prevents misuse by the franchisee or third parties.

In cases where foreign franchisors are involved, strict compliance with the Foreign Exchange Management Act (FEMA) is necessary, especially when dealing with royalty payments and other cross-border financial transactions. Moreover, depending on the nature of the business, additional approvals or licenses might be required under sector-specific laws such as FSSAI for food businesses, or state education regulations for educational franchises. Disputes may arise in any commercial relationship, and franchising is no exception. Hence, it is important to incorporate clear mechanisms for dispute resolution—arbitration being a preferred route in many agreements. Transparency, proper disclosures, and due diligence are also important to avoid legal complications and build a strong foundation for the franchise. Ultimately, understanding and addressing these legal aspects not only ensures compliance with Indian laws but also fosters trust, reduces risk, and contributes to the long-term growth and success of the franchising venture.

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