BUSINESS FRANCHISE: THE LEGAL FRAMEWORK AND PRACTICE IN ETI-OPIA

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BUSINESS FRANCHISE: THE LEGAL FRAMEWORK AND PRACTICE IN ETHIOPIA

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Declaration page

Declaration

I, the undersigned, declare that the thesis comprises my own work. In compliance with widely accepted practices, I have duly acknowledged and referenced all materials used in this work. I understand that non-adherence to the principles of academic honesty and integrity, misrepresentation/fabrication of any idea/data/fact/source will constitute sufficient ground for disciplinary action by the University and can also evoke criminal sanction from the State and civil action from the sources which have not been properly cited or acknowledged.

Signature

Name of Student

University Id. Number

Date
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My all times favorite spiritual song lyrics express my praise for the Almighty God and Virgin Mary,

You helped me climb the mountain
You helped me through the hardship
You helped me walk through storm
For all these, I praise thee!

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Table of Contents

Title page ................................................................. i
Thesis approval page .................................................. ii
Declaration page ........................................................ iii
Acknowledgement ......................................................... iv
Table of Contents ....................................................... v
List of abbreviations/Acronyms ...................................... vi
Abstract ................................................................... vii

1. CHAPTER ONE: INTRODUCTION ................................ 1
   1.1. Background of the Study ........................................ 1
   1.2. Statement of the Problem ........................................ 6
   1.3. Objectives of the Research ..................................... 7
   1.4. Research Questions .............................................. 7
   1.5. Significance of the Study ....................................... 8
   1.6. Literature Review ................................................. 8
   1.7. Methodology of the Study ...................................... 9
   1.8. Scope and limitation of the Study............................ 10
   1.9. Overview of Chapters ......................................... 10

2. CHAPTER TWO: BACKGROUND OF FRANCHISE ........... 12
   2.1. Background of Franchise ....................................... 12
       2.1.1. Element of Franchise Definition ......................... 14
   2.2. Historical Evolution of Franchise ............................ 17
       2.2.1. Theories of Franchise ..................................... 19
       2.2.2. Types of Franchise ....................................... 23
       2.3.3. Franchise and Other Similar Arrangement ......... 25
       2.2.4. Advantage and Disadvantage of Franchise ......... 26
   2.3. Franchising in Ethiopia ....................................... 32
       2.3.1. Franchising Role in Economic Development and Technology . 34
       2.3.2. The Key Attraction of Franchising in Ethiopia .... 36
3. CHAPTER THREE: LAWS IN RELATION TO FRANCHISE BUSINESS IN ETHIOPIA

3.1 Market Entry for Franchise Business in Ethiopia

3.2 The Pertinent Principles of Contract Law of Ethiopia Applicable to Franchise Agreement

3.3 Intellectual Property Right Protection for Franchisor and Franchisee under Ethiopia law

3.3.1 Brand Recognition and Enforcement

3.3.2 Copyright and Patent Protection under Ethiopian laws

3.3.2 Trade name Registration under Ethiopian law

3.4 Franchisor's Tax liability and franchisee tax obligation under Ethiopian Tax Law

3.5 Foreign Exchange Regime Ethiopia Relevant to Franchise Business

CHAPTER FOUR: PARTIAL LEGAL PROBLEMS AND THE WAY FORWARD OF FRANCHISE BUSINESS IN ETHIOPIA

4.1 Enforcement Problems Related to Franchise Relevant Laws

4.1.1 Lack of Awareness about Franchise Business

4.1.2 Weak and Fragile Infringements Controlling Mechanism

4.1.3 Reliance on Authentication than Investigation Based on Relevant laws

4.1.4 Lack of Incentive to Promote Franchise Business

4.1.5 Lack of coordination Between Enforcement Agencies

4.2 Discrepancy of Franchise Relevant laws from Other Countries Specific law

4.3 Legal Problems Encountered by Franchisee and Potential Franchisor

4.3.1 Prevalence of Management Contract than Franchisee Arrangement

4.3.1 Lack of awareness on how to Sells Legally Protected Knowhow

4.4 Does Ethiopia Need to Enact Franchise Specific Law

4.4.1 Defects of the New Draft Law

4.5 Conclusion and Recommendation

4.5.1 Conclusion

4.5.2 Recommendation

Bibliography

Annexes
### List of abbreviations/Acronyms

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
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<tbody>
<tr>
<td>AGOA</td>
<td>American Growth and Opportunity Act</td>
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<tr>
<td>EIA</td>
<td>Ethiopian Investment Agency</td>
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<td>EIPO</td>
<td>Ethiopian Intellectual Property Office</td>
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<tr>
<td>ETB</td>
<td>Ethiopian Birr</td>
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<tr>
<td>FTC</td>
<td>Federal Trade Commission Franchise Rule</td>
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<tr>
<td>MoT</td>
<td>Ministry of Trade</td>
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<tr>
<td>PLC</td>
<td>Private Limited Company</td>
</tr>
<tr>
<td>Proc. No.</td>
<td>Proclamation Number</td>
</tr>
<tr>
<td>To.Mo.Ca</td>
<td>Torrefazione Moderna Café’ (Modern Coffee Roasting)</td>
</tr>
<tr>
<td>SME</td>
<td>small and micro enterprises</td>
</tr>
<tr>
<td>UNIDROIT</td>
<td>International Institute for Unification of Private Law</td>
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<tr>
<td>USD</td>
<td>United States Dollar</td>
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Abstract

Franchising is the most effective technique for product distribution and services delivery. Developing and emerging countries have equipped their legal framework to benefit from this growing business. Emerging middleclass society, vivid development and high number of small and micro enterprises are ripe Ethiopia for franchise. Transfer of knowhow and technology makes franchise an attractive business for development. Less failure rate, first day profit, brand loyal customers are benefits of franchise compared to independent business.

Franchise is a legally regulated business. As such the proper legal and institutional infrastructure for its regulation must develop side by side with it. To do so, the nature, theories, types and regulation of franchise in other jurisdictions should be studied. Identifying existing franchise relevant laws that have direct or incidental impacts for franchise development is crucial. However, lack of scholastic works in the area caused confusion with respect to our attitude towards foreign franchisors. Despite immense opportunity in terms of vast markets and the absence of market barriers, there are few franchise businesses in Ethiopia.

African Development Bank recommended specific franchise law to African countries. Studying the practical enforcement of franchise relevant law is a necessary step to be carried out to decide whether Ethiopia needs to have franchise specific law or not. This study ascertained that there are scattered rules here and there in Ethiopian laws that are franchise friendly. However, weak and fragile enforcement of relevant laws through different regulatory agencies made implementation unpredictable. Franchise is at its saturation in Europe and America market. Now the focus is on emerging countries and developing countries markets. In Ethiopia, international hotel brands are engaged in the hospitality market they considered as franchised outlets but use management contract arrangements. Their role in contribution of knowhow and management skill is negligible.

Ethiopia has organic agricultural products highly demanded by foreign markets. Domestic potential franchisors are receiving many franchise offers from foreign investors. Unfortunately, because of lack of awareness they rejected the opportunities. Legal preparation is one of essential steps for the development of franchise in one country. The Ministry of Trade’s attempts to regulate franchise business through specific law is appreciated. Be that as it may, there is no comprehensive work done to make sure proposed law is achieving its goals. Moreover, the draft law misses the core point of franchise regulation, protection of franchisee and the mechanism of pre-contractual disclosure. This study is thus a modest attempt at identifying the problem along these lines and forwarding possible points of recommendation thereof.
CHAPTER ONE
INTRODUCTION

1.1. Background of the Study

Franchises are a common way of doing business in developed nations.\(^1\) Currently, there are similar restaurants, which have similar seating arrangement and identical taste in every major city of the world.\(^2\) In fact, it is difficult to drive more than a few blocks in most cities without seeing a franchise business.\(^3\) One can eat his dinner in another continent at similar table what he has eaten his breakfast, but different waiters in the same uniform. MacDonald, one of the largest chains of fast food restaurants in the world has been well known in franchise businesses with 35,000 outlets across the globe.\(^4\) The majority of McDonald's outlets outside of the United States are franchises.\(^5\) A franchise is the best way to achieve a broader international recognition for a company trade name, business reputation and identity in foreign market.\(^6\) International business scholars said franchise is non-establishment form of doing business that moves the progression of penetrating the foreign market even closer to the final step of foreign direct investment (FDI).\(^7\) Oxford Dictionary of Law\(^8\) defines franchise in more comprehensive way than other dictionaries\(^9\) and institutional\(^10\) attempts. It define franchise as

> a license given to a manufacturer, distributor, trader, etc., to enable them to manufacture or sell a named product or service in a particular area for a stated period. The holder of the license (franchisee) usually pays the grantor of the license (franchisor) a royalty on sales, often with a lump sum as an advance against

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\(^1\) Franchising" at [http://www.ifa.com] (last accessed January 12, 2016)
\(^2\) Ibid.
\(^3\) Ibid.
\(^4\) "Countries and outlets of MacDonald" at [http://www.aboutMacDonald.com], (last accessed December 21, 2015)
\(^5\) Ibid.
\(^7\) Ibid.
\(^10\) "Franchising" at [http://www.ifa.com] (last accessed January 12, 2016)

International Franchise Association (IFA) defines franchising as a "continuing relationship in which the franchisor provides licensed privilege to do business, plus assistance in organizing, training, merchandising and management in return for a consideration from the franchisee"
royalties. The franchisor may also supply the franchisee with a brand identity as well as finance and technical expertise. Franchises are common in the fast-food business, petrol stations, travel agents, etc.

In general franchising is a business system where under the franchise agreement the franchisor grants a license to the franchisee to use the franchisor’s diverse intellectual property rights, know-how, designs, brands, trademarks, patents, and trade secrets along with the franchisor’s proven name, reputation and marketing techniques to market the franchisor’s products or services in return for a sum of money.

Multiple economic and legal reasons make franchise attractive for both parties. The most notable ones are first day profit and fewer risks. From the perspective of franchisee, franchise offers an opportunity to lawfully use intellectual properties that belong exclusively to franchisor. Franchisee is able to obtain the status of an independent business and the use of valuable business methods and knowledge all under the guidance of an experienced company. The reputation and well-known brand of the franchisor enables the franchisee to make a profit, the day he opens his business. Moreover failure rate of franchisees are five times lower than those of independent business. On the other hand, the franchisors penetrate the market without having to risk large sum of money by way of direct investment. The franchisor also has the opportunity to make a substantial income and capital profit without complying legal requirement of different countries.

Overall, "as a vehicle for entrepreneurship and investment, franchising allows for efficient expansion of good business practices, the development of intellectual property both domestically and internationally, and the promotion and growth of small businesses". While Ethiopian small and micro enterprise challenged by a high failure rate and inconsistent profitability, franchising

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11 Oxford dictionary of law, s.v. "Franchise"
13 Model Franchise Disclosure Law, 2002, International Institute for the Unification of Private Law (UNIDROT), Rome.<www.jus.com/unidroit.franchise> [last access 15 December, 2015] [Here after, Model franchise disclosure law]
14 "Franchise Influx Require Legislative Demand " at www.addisfortune.com [last accessed November 19, 2015] [Here in after, Franchise Influx Require Legislative demand]
15 Daniel, International Business Transaction p. 377
would have made things better for the businesses as well as the economy at large.\textsuperscript{18} However, franchise has its own disadvantage on entrepreneurship capacity of local business.\textsuperscript{19} The question whether franchise is necessary for developing countries or not remains disputable. Some argue supporting domestic enterprisers to establish their own local brand is better than paying royalties for foreign franchise. Other argues testing the untested road of franchising to ensure the survival of small businesses should be major targets of developing country.\textsuperscript{20} Drain effect of large consumer retailer companies on local market also another area were different perception reflected.\textsuperscript{21}

Business relation between franchisor and franchisee is established through contractual agreement. Bundle of rights that are a subject matter of different statue are part and parcels of the franchise agreement. Existing legal clauses, which found flung in different legislation make enforcement of franchise agreement difficult. For that reason, the mere civil code contract provisions are unable to regulate franchise. To regulate this complex business formant, many countries enact a compressive franchise law. U.S. Federal trade commission rule on franchise\textsuperscript{22} and People Republic of China regulation on administration of business franchise are among the well-known legal frameworks on the matter.\textsuperscript{23} These laws contain provisions that impose strict obligation on franchisor and entitled right to franchise.

Ethiopia is currently one of the fastest growing nations in Africa with vast market opportunity of about 84.4 million populations.\textsuperscript{24} The recent expansion of the country’s middle class and urban population and its per capital income has made the country ripe for international franchising businesses, especially those involved in the consumer retail business.\textsuperscript{25} Despite all

\textsuperscript{18} Mulugeta, Agaze, 'Franchising Unlocks Ethiopian Small Business Potential', \textit{Addis Fortune}, Vol. XII, No.583, (03 July. 2011, [Here in after, Mulugeta, Franchising Unlocks Etiopian Small Business Potential ]

[Last accessed, Feb.20,2016]

\textsuperscript{20} Mulugeta, , Franchising Unlocks Ethiopian Small Business Potential

\textsuperscript{21} Tilman, Altenburg, \textit{et al}, \textit{Making Retail Modernization in Developing Countries Inclusive A Development Policy Perspective}, German development Institute, Bonn,2016, P.21

\textsuperscript{22} Federal Trade Commission Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunities; Final Rule, 2007, \textit{Federal Register}, Vol. 72, No. 61. [Here in after, FTC rule ]


\textsuperscript{24} Mulugeta, Franchising Unlocks Etiopian Small Business Potential

these rounded business opportunity, "the current lack of interest or active protection of goodwill and intellectual property by the part of international franchisors will complicate any future entry".26 This result, very little franchising activity to took place between the 1960s, when the Hilton and Coca-Cola entered the market, and the 1990s when the Sheraton Addis opened for business.27

Currently, major international hotels brand operators sealing deals with local investors this cause shifting of gears in hospitality industry.28 Marriott, Radisson Blu, Golden Tulip, Ramada, Four Point by Sheraton and Pullman are franchising that have recently entered to Ethiopian market.29 Among the world global food chain, Kentucky Fried Chicken (KFC) is under preparation to open unspecified number of restaurants in 2016.30 However, according to U.S department of commerce and International copyright, doing franchise business in Ethiopia is complicated.31 They stated that difficulties in product quality control, banking regulations, and continuing foreign exchange convertibility issues make franchising difficult.32

Even though Ethiopia is one of the favorite destinations for tourists, only few internationally accepted well-known hotels to satisfy their consumption. Let alone other regional cities, foreign tourist cannot see well-known branded fast food restaurants in the African capital. However, franchising contributes a phenomenal 12 percent of GDP of South Africa, a figure that exceeds the success of franchise in Australia and United State.33 The efficient franchise legal framework of South Africa has a prominent role for such achievement.

Nevertheless, common and identical thing that one observes in different areas of Addis Ababa is cafes and fast-food restaurants, which have identical feature of franchise business.34 Currently, there is growing domestic business that has good potential for franchise. The prominent example

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26 Franchise Business Under Ethiopian Law
27 Franchise Influx Require Legislative demand
29 Ibid.
32 Ibid.
33 Babette, Franchising in Africa, P129.
34 Ethiopian Business Review, Dec 2015
is Kaldi's Coffee, which has 19 branches across Addis Ababa. Some other goes further and franchise their trade name, trademark & Knowhow, Chicken Hut has three-franchise outlet in Addis. Ethiopia will be home of international well-known franchises in the coming years. The vivid development, vast market opportunity and its process to accede World Trade Organization will force this fact to happen soon. Paradoxically, it seems current existing business are not able to compete with the coming transnational companies.

The above factual situation goes worse when we examine the country's legal framework. Even though many nations across the world have enacted franchise law, there is no law enacted exclusively for regulating franchise business in Ethiopia. At this time, foreign or domestic franchisor that has an interest to start franchise business will be governed by a multiple of codes and proclamations, rather than a single comprehensive regulation. Since, the main relationship between a franchisor and a franchisee flows from a contractual agreement the civil code is the primary one. Moreover, other pertinent areas of law are also applicable to the franchise business. The Commercial code, Investment law, Intellectual Property law, Tax law, Competition law and Consumer Protection law, Labor laws, and Trade and Registration law are among others laws related to it.

Despite fragmented laws that are applicable for single franchise agreement and without having compressive law that govern franchise business, many countries lawyers like India, try to attract foreign direct investment and technology transfer by developing guide for compliance of franchise business legal framework for foreigner franchisors. However, there is no written lawyers of Ethiopia have no sufficient information about franchise business itself, let alone writing compliance guide to foreign investors. An almost non existing academic article, books, thesis in this area shows that how much the subject matter is ignored by Ethiopian lawyers. Surprisingly, a review of subsequently published legal commentaries on the Civil Code also

39 Franchise Influx Require Legislative demand
contains no reference to franchise law.\textsuperscript{40} There is no specific law there is no government or private body concerned with this matter.\textsuperscript{41}

Thus, it is very important to make study about sufficiency of Ethiopia's legal framework to regulate franchise business in this globalization era. Identifying specific laws that a foreign franchisor should comply with establishing franchisee business is also crucial for attracting foreign investment. Additionally, looking out how the practices work on existing few franchised business has significant role to have a clear understanding about the practice. Finally, the study will serve as momentous to identify the problem and suggest the solution.

1.2 Statement of the Problem

Lack of comprehensive law to regulate franchise business is one cause for low interest of foreign franchisor. This problem creates confusion for franchisor to predict and rely on the legal protection. Ignorance of academician to identify and assess the sufficiency of the legal regime of the country opens a door for wrong information. As stated on background information, for U.S department of commerce doing franchising business in Ethiopia is difficult. However, for the one who knows the investment policy of Ethiopia, this kind of wrong conclusion is very absurd. Letting such kind of information has harmful effect on developing economy of the country.

It is obvious that different legislations of Ethiopia, which are relevant to the area, demand a franchisor and franchisee to act accordingly. However, the question of what kind of law, in what extent applies to foreign and domestic franchise is yet studied. This deters stakeholder to know sufficiency of the existing legal framework to regulate franchise agreement. The compatibility of the existing legal regime to other country's comprehensive franchise laws is not also studied. These facts make the legal regime of Ethiopia regarding franchise business is untouched.

Currently, many domestic investors in the service sector have well known trademarks, mainly in Addis Ababa. Rather than using franchise business as way for investment, still some try to open another branch by themselves\textsuperscript{42}. They may have various reasons. Specifically, how many of them acquire proper guidance to be a franchisor, to prepare manuals, guidelines that have intellectual property law protection remains question. In this regard, other practical problems that are related

\textsuperscript{40} Franchise Influx Require Legislative demand
\textsuperscript{41} Franchise Business Under Ethiopian Law
\textsuperscript{42} Ethiopian Business Review Magazine Oct.2014, P. 32
to legal aspects of franchise business, which domestic potential franchised business faces need to be studied.

Currently, there is vivid development and a country move towards trade liberalization. These cause emerging of international hotel brand franchise in the capital city. The government also has an intention to invite giant consumer retailers to solve shortage of consumer goods but hesitate towards its implementation. Focus of international franchisor in hospitality industry and its impact on local developed brand also need a consideration. If the government is committed to invited giant consumer retailers, there may be a tension between local small and micro enterprises and foreign companies. The role of local franchise to ensure the survival of small and micro enterprises required to be studied.

Therefore, all the aforementioned problems, among many others, and the need to assess practical functions of franchise business made imperative to conduct this proposed research both in doctrinal and empirical approach.

1.3 Objective of the Research

The general objective of this research is to examine the existing legal frameworks that regulate franchise business and investigate practical legal problems encountered by selected franchise and assess the role of a legal framework in developing local franchise.

The specific objectives are,

- To exhaustively find out the kind of laws and the extent they apply to regulate franchise business in Ethiopia
- To make short survey on experience of other jurisdiction in regulating franchise business and compare their achievement in developing local brands.
- To find out practical legal problems that the existing selected franchise business encountered in doing franchise business.
- To identify the impact of current existing laws on developing domestic franchise business.

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To generate concrete and possible recommendation on what ought to be done to promote franchise and develop local franchise in Ethiopia.

1.4 Research Questions
The main research question targets to answer what is the impact of existing legal framework on forthcoming foreign franchisors, existing franchisees and prospective domestic franchise.
With this, the following are specific questions,

1. What are major laws that regulate franchise business in Ethiopia and there difference from other countries comprehensive laws?
2. How does nonexistence of comprehensive franchise law affect forthcoming franchise business in Ethiopia?
3. What are the practical legal problems that current functioning franchisees encountered so far?
4. How existing franchise legal framework can be utilized to develop future domestic franchise?
5. What measures need to be taken to solve the legal problems relating to franchise?

1.5 Significant of the Study
✓ The study will serve as explaining guide for foreign franchisor and domestic franchise to explore the legal framework of Ethiopia.
✓ The study will have certain contribution for stakeholders in creating awareness on franchising.
✓ It serves as a reference and input for further research in the area.
✓ Finally, it may provide a benchmark for domestic businesspersons to consider and evaluate opportunity of doing franchise business.

1.6 Literature review
It is hardly possible to get any comprehensive literature written on franchise business in Ethiopia. Deresurafel Bezawerk tried one and only attempt in his senior essay in 2003.44 This essay is not exhaustive, deep in details. Chapter Three tries to show contents of franchise contract by taking provisions from sample franchise contract. The last chapter deals how

franchise was regulated under 1979 American franchise law and franchise federation code of conduct of South Africa.

Beside its shallowness, relevant laws that govern franchise are not discussed, their enforcement is not considered, practical legal problem that franchisee and franchisors encountered are not incorporated. Moreover, the essay is unable to distinguished exclusive dealership agreement, bottling agreement from business format franchise. Therefore, this study aims to exhaustively identify franchise relevant laws and explore their enforcement. It also further discovers the practice and legal challenges of existing franchisee and potential domestic franchise in Ethiopia.

The reader of this study may see a fancy cover book in Amazon titled "Franchising in 2014 Legal and Business Considerations". It is Fifteen (15) page pamphlet issued by legal firm in England that cost USD$ 45. Eleven uniform questions asked for lawyers of twelve African countries and it includes Ethiopian response for each question. It is an advertising not a research work. The reason that it mentioned here is to ascertained the novelty of this study.

1.7 Methodology of the Study

Research questions are answered by employing qualitative research approach. This method is chosen because the research focuses on analysis of the existing legal framework and practical problems, which are not to be generalized. Some of the questions included in the research questions answered by investigation of doctrinal sources. The rest of the questions are addressed by employing empirical data that help to assess the existing practical problems.

The subjects of the study are agencies in charge enforcing laws relevant to franchise business directly and incidentally. Hence, primary source (interview) used to acquire and analyze practical related information and come up with comprehensive finding. All regulatory agencies respondents are educated persons so that the researcher employed structural interview. On the other hand, for respondents from potential domestic franchisors and foreign franchised out let semi structured interview are employed. This method helped a lot for the researcher to adjusted designed questions based on respondent's ability to answer.

Laws are heavily referred as primary sources and utilize as basic structural for doctrinal analysis. Moreover, comparative research approach applied to enrich the study with perspectives of other jurisdictions. In addition to primary sources, various relevant secondary sources such as articles,

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*Kendal, Tyre, etal* "Franchise in Ethiopia 2014 Legal and business considerations", LexNorir Foundation, 2014
essays, books, sample franchise contracts and other research works are used to analyze the research problems.

Without employing sampling, all eight regulatory agencies that enforce franchise relevant laws were target groups for data collection. Other target business selected based on purposive sampling techniques. Domestic businesses that have many branches, good will and identical taste on their product are selected for interview. International hotels that used well-known franchisors brand are selected for primary data collection, as they presumed to conducting business format franchise. Two Trade associations are similarly selected because of their respective responsibility related to franchise development. Rule of data saturation (redundancy) limited the number of target business organization in both categories.

The data collected through interview systematically interpreted based on respondents’ common situation. Respondents’ education background, year of services in the field takes as a parameter to evaluate responses of regulator institutions employees. The type of business they run, the reputation of the business, background of the institutions, educational background businessperson and other important parameter used to evaluate response of businesspersons.

1.8 Scope and Limitations of the Study

This research primarily focuses on the assessment of relevant laws that have direct or incidental impact in franchise business. As such, the scope of the research does not cover all aspects of doing franchise business in Ethiopia. Besides, it does not deal with other factors that have direct or indirect impact on development of franchise business in the country. As can be noted from the title, the researcher tries to see the practice. Hence, issues related to economics, cultural and social aspect franchise business is outside the ambit of this research.

As stated in the background information, lack of compressive research work, relevant data and other published material impede an in depth investigation of the issue at hand. Moreover, lack of cooperation in one international hotel forced researcher to use anonymous sources. Additionally, time and budget limitation poses challenges in conducting the research. Variety of research techniques used to minimize possible impact on the research.

1.9 Overview of Chapters

Generally, the study coverage is broad as it critically analyzed the legal framework and practical application. In doing so, the researchers plan to divide the whole part of the research in three
Chapters. Chapter two briefly discussed what mean franchise, element of franchise, theories of franchise, historical development franchise business, right and obligation of parties, its role for foreign direct investment and technology transfer. The contents of the chapter also assigned to discuss how franchise regulated in other countries compressive franchise law. Chapter three identified relevant laws that have directly and incidentally influence in franchise regulation in Ethiopia. The extent of such law impact in franchise development also discussed. Questions raised by foreign franchisor about the sufficiency of the legal protection of the Ethiopia also addressed.

The data collected through structured and semi structured interview analyzed in chapter four. The practical enforcement franchise relevant laws are examined. The contents of the chapter also assigned to discuss how franchise regulated in other countries compressive franchise law. Problems that hinder the development domestic franchise are identified. Ministry of Trade attempts to regulate franchise and its defects discussed. Legal challenges faced by potential domestic franchisor so far also assessed. Finally, the research has conclusion derived from the overall analysis of the study. At last, possible recommendations are included which are forwarded based on the finding of the research process.
regulates them. Franchisors can place outlets too close together, terminate the franchisee in order to reopen a franchisor owned outlet at the same location, force franchisees to purchase inputs from the franchisor, misappropriate advertising royalties, and write the franchise contract so it favors the franchisor in disputes.\(^{53}\) Franchisees also use its independent position to hurt the franchisor interest. A franchisee may release the franchisor’s proprietary information, fail to pay royalties, and not adhere to quality standards.\(^{54}\)

For a legal profession, it matters little whether consumers, economists, and the parties themselves call or consider a particular business relationship a franchise. What really matters is whether the relationship is a “franchise” under the various pieces of legislation that regulates franchising. Hence, this is a matter of definition, pure and simple. If a relationship satisfies the legal definition of a “franchise” under particular statues, then the franchisor has various legal duties to its franchisee and vise versa.\(^{55}\)

The root word “Franchise” comes from old French meaning privilege or freedom.\(^{56}\) In the Middle Ages, a franchise was a privilege or a right.\(^{57}\) Black’s Law Dictionary defines Franchise as, “the sole right granted by the owner of a trademark or trade name to engage in business or to sell a good or service in certain area.” \(^{58}\) The definition lacks many features of franchise. It confined franchise with trademark and trade name only. It fails to include “knowhow” a body of non-patented practical information, resulting from experience and testing by the franchisor, which is secret, substantial and identified. For comprehensive definitions, it is necessary to examine laws that regulate franchise. United States is a pioneer of franchise business development and its regulation. As a result, quoting Federal Trade Commission Franchise rule (Here in after FTC), which is the first in kind and source for other countries statutes is acceptable.\(^{59}\)

\(^{53}\) James, et al. Franchising: A Review and Avenues to Greater Theoretical Diversity, P,911

\(^{54}\) ibid.

\(^{55}\) William, Killion, 'History of franchising', in Alexander, Meiklejohn (ed.), The Franchise cases Material and Problem, American Bar Association, P,3 [Here in after William, History of Franchising]


\(^{57}\) Franchise Influx Require Legislative Demand.

\(^{58}\) Black's law Dictionary, s.v. "Franchise."

\(^{59}\) FTC rule,
The FTC definition of franchise in rule 436 is too long.\textsuperscript{60} It may be paraphrased as follows.

A franchise is continuing commercial relationship in which (i) A franchisee redistributes goods or services which are identified by the trademark, commercial symbol or advertising of the franchisor or where the franchisee operates its business under a name using the franchisor's trademark, commercial symbol or advertising, and (ii) The franchisor provides significant assistance to or imposes significant controls over the franchisee's method of operation, and (iii) The franchisee is required to pay the franchisor (or its affiliate) \$ 500 or more (except for the bona fide wholesale price of inventory goods) at any time through the first six month after the franchisee commercial business.\textsuperscript{61}

The European Union (hereafter EU) also defines franchise under block exemption for vertical restraints as, "...a package of industrial or intellectual property rights relating to trademarks, trade names, shop signs, utility models, designs, copyrights, know-how or patents, to be exploited for the resale of goods or the provision of services to end users."\textsuperscript{62} This definition categorizes franchise as bundle of right that can be transferred from one person to another. The regulation further defines franchise agreement as

Franchise agreements contain licenses of intellectual property rights relating in particular to trademarks or signs and know-how for the use and distribution of goods or services. In addition to the license of IPRs, the franchisor usually provides the franchisee during the life of the agreement with commercial or technical assistance. The license and the assistance are integral components of the business method being franchised. The franchisor is in general paid a franchise fee by the franchisee for the use of the particular business method. Franchising may enable the franchisor to establish, with limited investments, a uniform network for the distribution of its products. In addition to the provision of the business method, franchise agreements usually contain a combination of different vertical restraints concerning the products being distributed, in particular selective distribution and/or non-competes and/or exclusive distribution or weaker forms thereof.\textsuperscript{63}

2.1.1 Elements of Definition of Franchise

Franchising is one of the most common ways of doing business in most highly developed countries. The United States of America is the best example of a country with a well-developed

\textsuperscript{60} Ibtd.

\textsuperscript{61} Minnesota department of employment and economic development, \textit{An introduction to franchising}, Briggs and Morgan, 3\textsuperscript{rd} ed. Minnesota, 2008, p.22. [Hereafter, \textit{An introduction to franchise}]

\textsuperscript{62} Regulation on the application of Article 85(3) of the Treaty to categories of franchise agreements, No 4087/88, European community, November,30, 1988. Art. 1 A.[Hereafter, EU franchise regulation]

\textsuperscript{63} Block Exemption Regulation on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices, No. 330/2010/EC
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and healthy franchising culture.\textsuperscript{64} Thus, it is very essential to pinpoint three important elements of franchise from FTC and EU definitions. All three elements must be satisfied to create a franchise under UNIDROT (International Institute for the Unification of Private Law) model franchise law\textsuperscript{65}. If one of the elements is missing, there will not be franchise. The following paragraphs elaborate the three necessary elements of franchise.

1. Trademark element: - The franchisee is given the right to distribute goods and services that bear the franchisor’s trademark, service mark, trade name, logo, or other commercial symbol. For EU regulation, the core of the franchising arrangement is a license agreement, granted by the franchisor to the franchisee, to use its trademark and the franchised system.\textsuperscript{66} In United States, the franchisee is only allowed (not necessarily required) to use the grantor’s trademark, logo, trade name or advertising in connection with distribution of goods and services.\textsuperscript{67} The mere fact that the agreement is silent as to the franchisee’s use of the franchisor trademark does not mean there is no trademark element. The agreement must affirmatively prohibit the grantee from using the grantor’s trademark, trade name, logo or advertising.\textsuperscript{68}

Sometimes, it is difficult to differentiate ordinary dealership and distributorship from franchise. Courts in United States use tests to identify whether or not the trademark element exist. The following scenarios show the existence of trademark element. First, if a distributor or a dealer utilizes franchisor's trademark probably in the way that leads customer to think that the dealer or distributor is a part of franchisor business organization rather than an independent merchant. Second, the use of common advertising or advertising closely associating the dealer with the franchisor may be enough to throw the arrangement to the category of franchise.\textsuperscript{69}

2. Significant Control or Assistance: - The franchisor has significant control of or provides significance assistance to the franchisee’s method of operation. The following will be considered as examples of significant control. These includes approval of the site, requirements for site design or appearance, designated hours of operation, specified production techniques, and

\textsuperscript{64} Robert, Franchise as consumer, P.456
\textsuperscript{65} Model Franchise Disclosure Law
\textsuperscript{67} Ibid.
\textsuperscript{68} An introduction to franchise, P.16
\textsuperscript{69} Id. p.15
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64 Robert, Franchisee as consumer, P.456
65 Model Franchise Disclosure Law
67 Ibid
68 An introduction to franchise, P.16
69 Id p.15

15
required accounting practices, required participation in promotional campaigns, training programs and providing an operations manual.

3. Required Payment: - Franchisee fee element is what most often separates ordinary dealership or distributorship from franchisees. Dealers or distributors do not pay separate consideration for the right to enter into or maintain the relationship, at least in combination with a grant of right to use the grantor’s trademark or other trade identification.\(^70\) Based on FTC rule a franchisee is required to pay the franchisor at least US $500 either before or within six months after opening for business. Required payments include any payments the franchisee makes to the franchisor for the right to be a franchisee.\(^71\) These include franchise fees, royalties, training fees, payments for services, and payments from the sale of products. The EU and UNIDROIT franchise laws are silent about the required least amount of fee.

Even though all three elements are the basic things in definition of franchise, this is not always true in other countries and federal state regulation. For instance, Chinese franchise regulations specifically provides that only "enterprises" (and not individuals or other entities) may engage in franchising as franchisors.\(^72\) Moreover, to engage in franchise activity in China a franchisor shall own at least two directly operated outlets and shall operate more than a year.\(^73\)

The EU definition of franchise used the term undertaking which oxford dictionary defines as a company or business.\(^74\) Therefore, similar to China the EU definition exclude individual person from becoming a franchisor. In twelve States of America, the three elements of the legal definition of a "franchise" are Marketing Plan, association of trademark and required fees.\(^75\) Even though the definitions of franchises vary, there are several common themes. In five other states\(^76\) legal definition of franchise, Community of interest is one element in addition to trademark license and required fee.\(^77\)

\(^{70}\) An introduction to franchise, P.17
\(^{71}\) FTC rule, Sec. 436(1) S
\(^{72}\) China franchise regulation, Art.3
\(^{73}\) Id., Art.7
\(^{74}\) A franchisor engaged in franchising activities shall own at least 2 directly operated outlets, and shall be in operation for more than 1 year.
\(^{75}\) Concise Oxford English Dictionary, 11th ed., s.v “undertaking”
\(^{76}\) An introduction to franchise, P.14
\(^{77}\) Id., P 15 These states are Hawaii, Minnesota, Mississippi, Nebraska, and South Dakota
\(^{77}\) Id., P 16-20
If all the above three elements are present, then the relationship will be considered as a franchise. If any one element is missing, there will not be a franchise. The above two prominent definitions noted that Franchise law does not apply solely to written contracts. A purely oral arrangements or even a single transaction can also satisfy the statutory definition if it contains all of the required elements.\textsuperscript{78}

### 2.2. Historical Evolution of Franchise

In the middle ages, a franchise was a privilege or a right.\textsuperscript{79} In those days, the local sovereign or lord would grant the right to hold markets or to hunt on his land.\textsuperscript{80} Beginning from the 1830s a new form of agency emerged called exclusive agent that share some features of modern franchise.\textsuperscript{81} Exclusive agent stands to someone with the sole right to sell the manufacturer’s product into a particular market.\textsuperscript{82} This concept of exclusive agent widely used in 1840 in Germany.\textsuperscript{83} Certain major beer brewers granted a certain taverns the exclusive right to sell their beer.\textsuperscript{84} In 1851, Singer Sewing Machine Co. began granting distribution franchises for its sewing machines in America.\textsuperscript{85} Isaac M. singer practiced modern franchising by using exclusive agent distribution method.\textsuperscript{86} Once exclusive agents became dependent on a single manufacturer, they lost a great deal of their freedom of action and the relationship shifted to franchisor and franchisee.\textsuperscript{87}

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\textsuperscript{78} An introduction to franchise, P.14.
\textsuperscript{79} Oxford Dictionary of Law, s.v. "franchise". Franchise means a special right conferred by the Crown on a subject. Also known as a liberty, it is exemplified by the right to hold a market or fair or to run a ferry, "franchise"
\textsuperscript{80} William, History of franchising, p.6
\textsuperscript{81} Ibid.
\textsuperscript{82} Blavk's Law Dictionary, s.v. "Exclusive agent"
"Exclusive agent Exclusive agency generally fall into three classes: (1) where the contract does not prevent the principal from making direct sales but deprives him of the right to appoint other agents; (2) where the agent is the only one with any right to sell; and (3) where the exclusive agency is accompanied with a stipulated right to commissions on all sales whether made through the agent or not."
\textsuperscript{83} William, History of franchising, P.10
\textsuperscript{84} Ibid.
\textsuperscript{85} Ibid.
\textsuperscript{86} Ibid.
\textsuperscript{87} An introduction to franchise, P.9
Even though exclusive distributorship that has been cited prototype to modern franchising began in Europe, modern franchise started in America.  

At the beginning of the Twentieth Century, franchising started growing at food service establishments in the US. Howard Johnson and Reginald Sprague established the first modern restaurant franchise. Johnson began franchising restaurants in 1935, and by 1939, more than 100 restaurants carried his name. Then franchises spread through automobile, soft drink bottling, and gasoline industries after 1930's. As a result, business format of franchising, as we know it today, began on April 15, 1955 in the United States. On that day, Ray Kroc opened his first McDonald's restaurant in Des Plaines, Illinois.

According to researchers, the dynamic growth of franchise in United State is attributed to three factors. First development of television paved a way to establish nationwide brand names and familiar trademarks. Second, growing interstate high ways, increasing automotive ownership caused the public to travel farther from home. An increase in travel by consumer meant that consumers were more often shopping in unfamiliar geographical areas, in which national but not local brand names would serve as signals of quality. Finally, a continuing increase in the real income of consumers led to a further increase in the opportunity costs of search in retail markets, again enhancing the information value of brand names. These factors resulted in a significant increase in the use of franchise system in the mid 1950s with an apparent increase in the efficiency of national brand names.

In the 1960s Business format franchising, the dominant mode of franchising today, had arisen in popularity and dominance. Literatures show that development of business format franchising is the poster child of Ralph Waldo Emerson's admonition that "there is properly no history; only

88 William, History of franchising, p.11
89 William, History of franchising, p.11
90 Id, p.14
91 Ibid.
92 Ibid.
93 Ibid
95 Ibid
96 Ibid
97 Ibid
98 Ibid
99, The Histroy of Franchise
biography. What Ralph wants to say is business format franchising in particular is the story of entrepreneurs ultimately perfecting a unique method of distribution through trial and error. Reading of every successful franchisor story gave as a clear picture how modern franchising evolved in America and spread throughout the world.

2.2.1 Theory of Franchise

Principally, franchise provides capital as well as the managerial talent for business. Abundant theoretical and empirical research has been conducted to explain why firms choose franchise. Most franchising research has been grounded in either resource scarcity or agency theory. However, other studies assured that, for potential franchisors, franchising realized the dream of making big business. More recently, another competing theory has emerged which seeks to explain the prevalence of the franchise system based on the organizational characteristics that differentiate it from other forms of ownership; and this is the Plural Organization Theory. Be that as it may, Luis and other select 117 articles ranging from 1966 to 2012 find out five most relevant theories of franchise. All five theories discussed below.

1. Resource scarcity theory: Franchising is simply a business technique, a means of distribution or providing goods or services to the consumers. Franchising is also a method of expanding an existing business. When firms are very young and small, it is difficult to raise adequate capital for growth through traditional financial markets (e.g., through public stock offerings) or from existing operations. The franchisor faces a need for growth to achieve economies of scale and

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1. William, History of franchising, p.5
2. Id., p.5-14
3. "Modern business format franchising was ultimately the product of the drive and ambition of American entrepreneurs. Who are often not particularly educated, with names like Harry Axene, a sales manager for a farm equipment company, who spread the Dairy Queen franchise throughout the United States; Kemmons Wilson, a high-school dropout who developed the Holiday Inn chain of hotels; Harland Sanders, who started Kentucky Fried Chicken at age 62 by licensing restaurants".
4. James, Franchising: A Review and Avenues to Greater Theoretical Diversity, P.909
6. Ibid
7. Luis, Theoretical perspective in franchising: A network analysis, P. 1-16.
8. The study investigates the five most relevant theories in franchising Resource Acquisition, Agency Theory, Transaction Cost Analysis, Signaling Theory, and Property Rights
10. Franchise is one of the most creative of various marketing techniques that have emerged in this century
11. James, Franchising: A Review and Avenues to Greater Theoretical Diversity, P.910
market share.\textsuperscript{109} Resource Scarcity proposed that firms franchise in order to access scarce resources, particularly financial and managerial (i.e., local decision-making and market knowledge) resources.\textsuperscript{110} The franchisee brings together money and management. Based on resources scarcity theory, franchising has an additional benefit than pooling resources. This significant benefit is keeping control of the company management. Indeed, selling company shares to external investors implies losing strategic control.\textsuperscript{111} Alternatively, using franchising implies that the partners are individual franchisees who are financing the growth, but does not hold share in the company; so the franchisor keeps full strategic control of his company.\textsuperscript{112} Therefore, franchising would be a temporary organizational resource used to deal with the difficulty to access the basic resources necessary for growth.

However, facts in the real world show some paradox to this theory. Many franchising companies gave financial support to their franchisees. Even empirical evidence shows many franchising chains continue franchising even though they have plenty of resources.\textsuperscript{113} Resource scarcity thesis of ownership redirection, which predicts that the franchisor will stop franchising once he has the necessary resources to fund growth, is not always true.\textsuperscript{114}

2. Agency theory The above factual paradoxes of resources scarcity are the main reason to doubt the thesis. In this regard, Agency theory views franchising as a mechanism for improving the alignment between firm and outlet level incentives.\textsuperscript{115} Some researchers have highlighted the idea that the franchising system has indeed a more important aspect than financial resources, the motivation of the franchisee.\textsuperscript{116} In ordinary agency relationship, the principal delegates authority to an agent. However, agents are assumed to be self-interested and to possess goals that diverge from the principal’s goals. To ensure his interest is protected, the principal expends resources called agency costs. This problem refers to the conflict between a firm and its outlet manager.

\textsuperscript{109} Ramone, \textit{An analysis of the three confronting theories}, p.167
\textsuperscript{110} James, \textit{Franchising: A Review and Avenues to Greater Theoretical Diversity} P.911
\textsuperscript{111} Ramone, \textit{An analysis of the three confronting theories}. p.168
\textsuperscript{112} Id., p.167
\textsuperscript{113} Ibid.
\textsuperscript{114} Id., p.168
\textsuperscript{115} James, \textit{Franchising: A Review and Avenues to Greater Theoretical Diversity}, P.909
\textsuperscript{116} Ramone, \textit{An analysis of the three confronting theories}. p.168
Researchers developed the idea that the franchising system is an effective response to the classic principal agent problem.\textsuperscript{117} Agency Theory explains that franchising avoid agency problem because franchising contract aligns the interests of both the franchisor and the franchisee and sets a common goal that both share. Franchisees are superior to employees because franchising gives the franchisee manager all profits after expenses. Therefore, franchisees do not reduce effort because their income is tied to their effort. Employee managers in contrast will shirk because they do not possess strong ownership incentives.\textsuperscript{118} The idea is that the franchisees are risking their own money in the franchised business; they are the owners of the business, so they have all the incentives to work hard and make it a profitable operation.\textsuperscript{119} The logic behind the Agency Theory explanation why firms decide to franchise, and the conclusion should be that, because franchising is such a powerful motivator, to take full advantage of it.

Similar to resources scarcity agency theory has some problem, horizontal franchisees problem. Because all outlets operate under a shared brand name and customers transfer goodwill associated with one outlet to others. Certain investments in the brand that franchisees make have spillover benefits for other franchisees.\textsuperscript{120} For example, the cleanliness of one outlet affects customers' perceptions of all outlets. Because the benefits are shared, franchisees prefer to free ride on others rather than to invest. Unless a franchisor follows up his individual franchisee's there is always a possibility of that his failure to do so will damage his brand.

3. Plural Organization Theory

The above two theories have their own prediction. Resource Scarcity said once the franchisor acquired the required resources it would repurchase the franchise outlet and fully company owned chains. Perhaps, Agency theory predict opposite forecasting fully franchised chains. In reality, most of the franchising chains maintain a mix of company owned and franchising structures. Based on plural organization theory, franchising is a way to achieve uniformity and adaptation.\textsuperscript{121} Under this theory, the reason to franchise is to have simultaneous access to the

\textsuperscript{117} Ramono, An analysis of the three confronting theories, p.168
\textsuperscript{118} James, Franchising: A Review and Avenues to Greater Theoretical Diversity, P.911
\textsuperscript{119} Ramono, An analysis of the three confronting theories, p.168
\textsuperscript{120} James, Franchising: A Review and Avenues to Greater Theoretical Diversity, P.912
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most important advantage of the company owned structure uniformity and the most important advantage of the franchised structure, adaptation.\textsuperscript{122}

Uniformity means that the customer must find a common image, design, and service experience in any outlet under the same brand; namely, the brand image, which has to be consistent all over the brand’s properties whether they are franchised or company owned.\textsuperscript{123} Adaptation means almost the opposite, the chain must adapt to changing markets to take advantage of new threats and opportunities and to adapt to the local markets where it is competing.\textsuperscript{124} Plural Form allows the company to achieve the two goals simultaneously. Franchisor strict quality controls are carried out to assure that the product and service quality meets the standards defined by the chain. On the other hand, the franchised units provide an entrepreneurial and innovative spirit for the chain. Control in the company owned units do not create a context hospitable to innovation and adaptation.\textsuperscript{125}

4. Property right theory

Property theory describes that the existence of property right on intellectual property urge people to utilize that property right in effective way. Therefore, franchise is a result of property rights that involve the notion of control and ownership over the use of scarce resources, and the rights of sales and transferences related to this control.\textsuperscript{126} The assignment of property rights in franchising is important to achieve an efficient resource allocation.\textsuperscript{127}

5. Signaling theory

The theory is Austrian in character and emphasizes the key role played by information in the competitive process.\textsuperscript{128} “signaling theory focus on the externalities of market imperfections and knowledge asymmetries to explain franchising”.\textsuperscript{129} In an environment where there is an information gap, firms may use several signs to provide information about themselves and their

\textsuperscript{122} Ramone, \textit{An analysis of the three confronting theories}, p.169.
\textsuperscript{123} Ramone, \textit{An analysis of the three confronting theories}, p.170.
\textsuperscript{124} Ibid.
\textsuperscript{125} Ibid.
\textsuperscript{126} Theoretical perspective in Franchising: A network Analysis, at <http://www.anpad.org>, [last accessed March 28, 2016]. [here in after, Theoretical Perspective in Franchising: A network Analysis]
\textsuperscript{127} Ibid.
\textsuperscript{128} Antony W. Dnes "Franchise contract", The Nottingham Trent University, 1999, P.1096 [ Here in After Antony, Franchising Contract], [ here in after, Antony, Franchise contract]
\textsuperscript{129} Ibid.
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\textsuperscript{122} Ramono, An analysis of the three confronting theories, p. 169.

\textsuperscript{123} Ramono, An analysis of the three confronting theories, P. 170.

\textsuperscript{124} Ibid.

\textsuperscript{125} Ibid.

\textsuperscript{126} Theoretical perspective in Franchising: A network Analysis, at <http://www.anpad.org>, [last accessed March 28, 2016], here in after, Theoretical Perspective in Franchising: A network Analysis

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\textsuperscript{129} Ibid.
products, as pricing, advertising and warranties\textsuperscript{130}. Franchisors draw on the local knowledge of franchisees, which concerns local tastes and market conditions.\textsuperscript{131} Franchising allows the use of the trademark to be exchanged for the franchisee’s local entrepreneurship, which is defined as noticing and acting upon opportunities.\textsuperscript{132} One company may not be able to provide by its self but franchise cover the defect.

2.2.2 TYPES OF FRANCHISE

The EU and United States have their own distinct systems of franchising. EU classified franchising in three types; service franchise, product franchise and distribution franchise. Business format franchise and product distribution franchise are the two types of franchise in United States. United States merged product and service franchise of EU and called them business format franchise.

Distribution Franchise or Product distribution franchise: - In product distribution franchising, the franchisor licenses its trademark and logo to the franchisees but typically does not provide them with an entire system for running their business. It can be described as a franchise agreement where the franchisee sells certain products in a shop, which carries the franchisor business name and or symbol.\textsuperscript{133} Franchisees simply sell the franchisor’s products and they have supplier dealer relationships. The industries where you most often find this type of franchising are soft drinks, automobiles and gasoline.\textsuperscript{134} Some familiar product distribution franchises include Coca-Cola, Goodyear Tires and Ford Motor Company\textsuperscript{135}

Business format franchise:- Although product distribution franchising represents the largest percentage of total retail sales, most franchises available today are business format franchises.\textsuperscript{136} Service franchise and product franchise are arrangements, EU stated that, in which the franchisee offers services or manufactures products under the business name or symbol and sometimes the trademark of the franchisor, and follows the franchisors instructions. Business format franchises of US, on the other hand, not only use a franchisor’s product, service and trademark, but also the

\begin{footnotesize}
\textsuperscript{130} Theoretical Perspective in Franching: A network Analysis
\textsuperscript{131} Antony, Franchising Contract, P.1096
\textsuperscript{132} Antony, Franchising Contract, P.1096
\textsuperscript{133} Intellectual Property: Licensing and Franchising
\textsuperscript{134} International Franchise Association, "An introduction to franchising", IFA Education Foundation, Washington, 2010, P. 6 [Here in after IFA, A introduction to franchising]
\textsuperscript{135} Ibid
\textsuperscript{136} Ibid.
\end{footnotesize}
complete method to conduct the business itself, such as the marketing plan and operations manuals. The 10 most popular franchising opportunities are in these industries, fast food, retail service, automotive, restaurants, maintenance, building and construction, food business services and lodging.

Because so many franchisors, industries and range of investments are possible, there are different types of contractual franchise agreement used by both types of franchise.

1. Single unit (direct-unit) franchise is an agreement where the franchisor grants a franchisee the rights to open and operate one franchise unit. This is the simplest and most common type of franchise. It is possible, however, for a franchisee to purchase additional single-unit franchises once the original franchise unit begins to prosper.

2. A multi-unit franchise is an agreement where the franchisor grants a franchisee the rights to open and operate more than one unit. Multiple unit franchise is divided into two further arrangements: Area development and Master franchise. Under an area development franchise, a franchisee has the right to open more than one unit during a specific time, within a specified area. For example, a franchisee may agree to open five units over a five-year period in a specified territory. The franchisor grants the franchisee exclusive rights for the development of that territory.

Master franchise agreement gives the franchisee more rights than an area development agreement. In addition to having the right and obligation to open and operate a certain number of units in a defined area, the master franchisee also has the right to sell franchises to other people within the territory, known as sub-franchisees. Therefore, the master franchisee takes over many of the tasks, duties and benefits of the franchisor, such as providing support and training, as well as receiving fees and royalties.

137 If: A Introduction to franchising P.7
138 Ibid.
139 Ibid.
140 Ibid.
141 Ibid.
143 Ibid.
144 Ibid.
Another hybrid-type of multi-unit franchise is an area representative franchise. In this model, the area representative buys a territorial franchise to sell and service unit franchisees in the territory. The area representative does not contract with the unit franchisees (who sign agreements directly with the franchisor), but does receive a portion of the initial fees and ongoing fees paid by the unit franchisee to the franchisor.

2.2.3 Franchise and Other Similar Arrangements Distinguished

Distributorship and Licensing are two popular methods that have similar features of franchise. These two arrangements are business expansion methods used by business organization to expand their market. Clear identification of each method from franchise arrangements is necessary. Unless, one closely examines these arrangements, they may lead to wrong understanding. For instance, Black's Law Dictionary defines distributorship as "A franchise held by a person or company who sells merchandise, usually in a specific area to individual customers." However, franchise has its own characteristic that distinguishes it from distributorship and other organizational forms.

Franchise's distinct characteristics that distinguish it from other similar arrangements are two. One, franchising typically occurs in businesses where there is a notable service component that must be performed near customers. The result is that service providing outlets must be replicated and dispersed geographically. The second key characteristic is that franchise contracts typically reflect a unique allocation of responsibilities, decision rights, and profits between a centralized franchisor and decentralized agents' franchisees.

In a distributorship, the distributor usually has a contractual relationship with the supplier, buys from the supplier in bulk and sells in smaller quantities. The distributor is familiar with local markets and customers may do business with many companies, more than a single supplier or producer. The distributor may not receive contractual support and training from the supplier and producer like a franchisee. A franchisee with a great deal of leeway in how to run the business.
may look like an independent distributor. A distributor may be subject to many controls by the supplier or producer and begin to resemble a franchise.

Black's Law Dictionary also defines licensing as "The sale of a license authorizing another to use something (such as computer software) protected by copyright, patent, or trademark". Licensing is a contract between the licensor who is the owner of the intellectual property and the licensee who is authorized by such contract to use the intellectual property of the licensor in exchange for the payment as consideration for such use that may be in the form of fees-or royalty. In the same way as the other contracts require an element of consideration to be present in order to constitute a valid contract, the licensing contract also requires a consideration in the form of payment from the licensee to the licensor in exchange of such transfer of right to use its intellectual property.

Thus, licensing provides an opportunity to the licensor to spread out its business without actually investing for such expansion. Unlike franchises, in which the franchisor exerts significant control over the franchisee's operations, licensors are mainly interested in collecting royalties and supervising the use of the license rather than influencing the operations of the business. Both the licensor and licensee own some of the assets, and both exercise control as independent decision makers regarding the use of their assets. Therefore, licensing is characterized by the fact that the licensor does permit the licensee to use the licensor's brand name, trademark, and/or logo as the name of licensee's business. However, the licensor does not exercise control on the partners' local market operations and marketing activities.

2.2.4 Advantage and Disadvantage of Franchise

Reason for short spread of franchise business is its proven benefit. Generally, franchise provides an established product or service, which may already enjoy widespread brand-name recognition. This gives the franchisee the benefits of a pre-sold customer base, which would

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150 IFA, Introduction to franchising, P.9
151 Black's Law Dictionary, s.v. 'Licensing'
152 Intellectual Property: Licensing and Franchising
153 IFA, Introduction to franchising, P.9
154 Intellectual Property: Licensing and Franchising
155 Ibid.
156 IFA, Introduction to franchising, P.10
ordinarily take years to establish. Despite basket full of opportunity for both parties, franchise has its own disadvantage. Tremendous literatures list out a quite lot of list as pros and cons of franchise. However, the researcher prefers to summarize them in three important aspects: economic, management, and brand development from both parties perspective.

**Advantages of Franchising from franchisor perspective**

From economic perspective, franchising is a medium for growth and expansion. Normally, a franchisor is required to invest his funds or to borrow funds. Franchise gives an opportunity for franchisors to expand their business through the efforts of the franchisees. Moreover, franchisors will receive additional income in the form royalties. The fact that franchising requires lesser amounts of capital to a distribution system than what is required in methods such as joint ventures and other forms of shared equity arrangements made it economically advantageous. Another economic benefit of franchise is it usually reduced the cost of compliance with countless local legal requirements to operate business.

In regards to managerial benefit, having independent owner is better than employed manager for business expansion. Suppose that franchisor select a franchisee prudently, franchising affords the benefit of committed operators who not only manage their franchised locations but who also have a vested equity interest in the business. When consumers enter into shopping mall or commercial complex almost anywhere in the world, they see similar brands. Brand names that attained worldwide recognition are common in many countries shops, fast-food restaurants, clothing retail stores, and service providers. Many of these businesses do not belong to giant companies. Thanks to franchise, local entrepreneurs independently own them. This is the great advantage of franchise brand development.

**Advantage of franchise for franchisee**

For franchisee, franchising also offers managerial benefit. Franchisee is able to obtain status as an independent business and the use of valuable trademarks, trade names, business methods, and knowledge all under the guidance of an experienced company. Franchisor provide professional

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157 IFA, *Introduction to franchising*, p.10
158 *Intellectual Property: Licensing and Franchising*
training, marketing assistance, a proven operating system, ongoing system support functions, and improved resell skill to the franchisee.

Creating ownership mentality the Franchisee will have an attitude of being a business owner (not merely dealing with one product line among many) and is more likely to devote time, attention and capital to growing the business, following the approved system and not walking away from occasional business challenges. Franchisee does not require spending huge money for acquiring good name. The well-established name of the franchisor serves as key to acquire profit with in short time. Franchise reduces the cost of advertising and promotion in the franchisee part.

Disadvantages of Franchise for franchisor

Franchisor is not free from negative effects of franchise in managerial perspective. Since franchising is highly regulated form of business activity. Franchise registration in some countries may be conditioned on compliance with unpublished, undiscoverable regulations imposed as “policies” by franchise law administrators. Compliance to these stringent requirements calls for additional skilled professionals that increased management burden of franchisor.

Unfortunately, franchise also has a negative effect on brand and good will development of business. The failure of franchisee or weaknesses of franchisor have spillover effect on the brand. A damaged, system wide image can result if other franchisees are performing poorly or the franchisor runs into an unforeseen problem. Even though franchisors usually insured risks of vicarious liability, it cannot avoid damage on the brand.

Disadvantage of franchise for franchisee

Franchise has negative economic impact for franchisees that have small startup capital. In addition to the initial franchise fee, franchisees must pay ongoing royalties and advertising fees. These cause considerable cost and risk compared to other methods of distribution. Quite often, the term (duration) of a franchise agreement is usually limited and the franchisee may have

Advantage and disadvantage of franchise at <http://www.holmeslofstrom.com>, [last accessed Feb, 20, 2016]
Ibid.
Intellectual Property: Licensing and Franchising
IFA, Introduction to franchising, P.14
Ibid.
Ibid.
little or no say about the terms of a termination. Costs and regulatory burden associated with franchising make it a poor choice for a very small-scale program or short duration effort. The overhead and ongoing administrative costs of franchising can be a significant problem for firms that are unfamiliar with the area.

Managerial disadvantage of franchise emanates from active involvement of franchisor. Franchisees do not have independent decision-making power. They are required to operate their businesses according to procedures and restrictions set forth by the franchisor in the franchise agreement. These restrictions are usually with respect to controlling retail pricing, redistribution of products, tie-in, exclusive dealing including products or services, which can be offered. For some people, this is the most serious disadvantage to becoming a franchisee.

2.2.5 Development of Specific Franchise Regulation Laws

The high growth and emerging popularity of franchising in the 1950s, 1960s and 1970s encouraged the startup of a number of ill-conceived, get-rich-quick schemes. The nature of business format franchise is exposed for fraud and abuse by hoax franchisors. William L. Killion expressed the situations like this, "The line between wholesome free enterprise and harmful greed is often thin. The "wild west" of business format franchising that emerged after WWII and created substantial wealth for a broad variety of American citizens served the interests of dishonest individuals looking to make a quick buck at the expense of vulnerable would-be franchisees."

Those abuses became the grist for legislative, regulatory, and sometime judicial intervention in franchise relationship beginning in the 1960s, reaching a peak in the 1970s, and continuing today. Numerous countries have responded to this rise in franchising by enacting franchise disclosure laws and, sometimes, franchise relationship laws as well. The franchise sector was first regulated in the 1970s in the United States and Canada. Initially, several states of United

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[167] An introduction to franchise, P. 49
[168] IFA, Introduction to franchising, P. 15
[169] Ibid
[170] Id., P. 15
[171] The History of Franchising
[173] Id., P. 5
[174] Robert, South Africa franchisees as consumer P. 456
States attempted to address these problems by using state securities regulation laws and unfair trade practice laws to regulate abuses in the offer and sale of franchises.¹⁷⁵ These efforts were largely unsuccessful.¹⁷⁶

Then, different committee chairperson senators of American congress initiate bill that aims to control franchise. The initial moves of lawmakers are too aggressive to franchise. However, franchisor through their association tackles the senate move. The most prominent example is International Franchise Association (IFA) of America that was created with the specific intent of uplifting the professionalism of the entire industry. The IFA holds training in all aspects of franchising which greatly enhances the industry.¹⁷⁷ Members of the IFA are required to adhere to the IFA’s Code of Ethics, which sets a high standard.¹⁷⁸ The IFA works closely with the US Congress and the Federal Trade Commission on improving how the industry relates to the franchisees. By doing intensive work on shaping the behavior of franchisor, IFA change franchise to viable law abiding business concept.

Regulation by the Federal Trade Commission in 1979 helped to legitimize franchising as widely accepted method for business expansion.¹⁷⁹ By 1990, France and Mexico enacted laws that regulate franchise. As of 2000, thirteen countries had enacted franchise legislation, including Australia, Brazil, China, Taiwan, Indonesia, Malaysia, Romania, and Spain.¹⁸⁰ Currently, over thirty countries, representing about one-third of the nations where franchised businesses operate, have enacted franchise-specific regulation.¹⁸¹ Moreover, in Africa there are at least eight countries with franchise laws in 2012.¹⁸² Two countries, namely South Africa and Tunisia have expressly regulated franchising.¹⁸³ Kenya, Nigeria, Uganda, Egypt Angola and Cape Verde islands regulate franchising through technology transfer legislation, application of agency laws or application of consumer protection legislation.¹⁸⁴

¹⁷⁵ *An Introduction to franchise*, p.29
¹⁷⁶ Ibid.
¹⁷⁷ William, *History of franchising*, P. 29
¹⁷⁸ Ibid.
¹⁷⁹ The History of Franchising
¹⁸⁰ Robert, *South Africa franchisees as consumer*, p.457
¹⁸¹ Ibid.
¹⁸² Babette, *Franchising in Africa* P.133
¹⁸³ Ibid.
¹⁸⁴ Babette, *Franchising in Africa* P.133
Generally, there are three approaches of specific laws regulating franchise in the world. These are franchise disclosure laws, franchise registration laws and franchise relationship laws. In disclosure laws, the law typically mandates that prior to signing any franchise agreement and/or before any consideration is paid, the franchisor must provide to a prospective franchisee a disclosure document setting forth specified information relating to the franchisor and the franchising business.\(^{185}\) In relationship laws, the law regulates some aspects of the relationship between franchisors and franchisees and can regulate issues such as grounds for terminating a franchise and the rights and responsibilities of franchisors and franchisees.\(^{186}\) In registration countries, the laws merely spell out who and what must be registered in connection with a franchise operation. Such laws may require the registration of the franchise businesses and the registration of the franchise agreements.\(^{187}\)

For instance, Brazil Franchise law requires franchisors to provide each prospective franchisee a disclosure document in writing and in clear and accessible language.\(^{188}\) In Indonesia, "the Franchisor shall provide a franchise offer prospectus to the prospective franchisees at least 2 (two) weeks prior to signing of franchise agreement".\(^{189}\) Most African legal system does not impose pre-contractual disclosure requirements on franchisor, except South African and Tunisia.\(^{190}\)

On the other hand, franchise registration laws require things like, registration of the franchise, registration of franchise salespersons and registration of franchise advertising. Franchise relationship laws also govern certain aspects of the relationship between franchisor and franchisee, such as grounds for terminating a franchise, notice and cure periods before termination, grounds for not renewing a franchise and equal treatment of franchisees.\(^{191}\)

\(^{185}\) China Franchise Regulation 2007


\(^{189}\) Indonesia Franchise Regulation, Art 4(1)

\(^{190}\) Babette, Franchising in Africa, p.133

\(^{191}\) An introduction to franchise, 6
The followings are the most common types of violation of franchise laws. Offering or selling unregistered franchise, failing to provide a franchise disclosure document on time, failing to provide all required disclosures in the document, making misrepresentations to franchisee prospects and improperly terminating or not renewing a franchise. Some scholars even today oppose the strict regulator action of state by saying "....in developing laws designed to protect franchisees from a lack of information about a franchise opportunity or to curb abusive practices by franchisors, legislatures and courts have rarely lost sight of the importance of franchising to the country economy and the unique opportunities it presents to entrepreneurs". 192

3. Franchising in Ethiopia

The history of franchise in Ethiopia trace back to the Imperial period. 192 International franchising contacts concluded with bottling companies and international hotel starting from 1950's. 194 Hotel franchising began with the opening of Hilton International in the nineteen sixties in Addis Ababa 195 Coca Cola was first bottled in Ethiopia in Addis Ababa in 1959 by the Ethiopian Bottling Share Company, which later opened a second branch in Dire Dawa in 1965. 196 Pepsi cola also came to Ethiopian market during the same period. 197 International brand hotels began with the opening of Hilton Addis in the nineteen sixties in Addis Ababa. In general, however, franchising in the country is at a very low level of development.

According to Derfesurafel, though their number is limited there are companies in Ethiopia who run their business under franchise agreement. 198 Pepsi Cola (Moha Soft Drinks Industry share Company), and Cadbury Schweppes (Summit Partners PLC) are example. 199 "In addition dealership ship agreements between oil companies such as Mobil Oil and Shell and individual dealer have many element that make them franchising" 200 In other part of the research writer said actual arrangement of the above companies is exclusive appointment and resell

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192 William, History of franchising, p.6
193 Franchising under Ethiopia law
194 ibid.
195 ibid.
196 ibid.
197 East African Bottling Constructing 420m Bkr Plant in Bahir Dar at www.capitalethiopian.com, [Last accessed march 4,2016].[Here in after, East Africa Bottling]
198 Derfesurafel, Franchising of business, P.46
199 ibid.
200 Derfesurafel, Franchising of business, P.46
agreements.\textsuperscript{201} As discussed in 2.3.3 (franchise and other arrangement distinguished) essential element of franchise significant control is missing form exclusive agent and resell agreements.

After 1991, to speed up the integration of the economy and encourage the wider participation of the private sector in the development of the national economy government promotes liberalization.\textsuperscript{202} In practices, the market is not fully liberalized some services sectors reserved to Ethiopian national and other domestic investors.\textsuperscript{203} Such sector include retail trade and brokerage, motels, pensions, tea rooms, coffee shops, bars, night clubs and restaurants.\textsuperscript{204} Moreover, it includes travel agency, trade auxiliary and ticket selling services.\textsuperscript{205} The above sectors are most favorable areas for franchise business. Non-liberalization of the services sector fully contributed for low number of franchise after 1991.

The reasons for underdevelopment of the franchising market during this period are many. Nevertheless, the most important cause was the 1974 military coup and the subsequent adoption of Soviet style communist economic policies that overnight wiped out the private sector in Ethiopia.\textsuperscript{206} For instance, the pioneer franchisor coca cola two plants were nationalized in 1975 and ran as public companies until 1996, when Ethiopian investors purchased them.\textsuperscript{207} Before a year, only three international brand hotels operate in the country, while about three others are in the pipeline to join the hospitality industry.\textsuperscript{208} Currently, Marriott, Radisson Blu, Golden Tulip, Ramada, Four Point by Sheraton and Pullman are International brands that have recently entered to Ethiopian market.\textsuperscript{209} Most hotels considered as five star, however, Hilton Ethiopian first

\textsuperscript{201} Id., P. 21
\textsuperscript{202} Pikremarkos Mesro. \textit{et al.}, Review of legal and institutional frame work for Ethiopia, Private Sector Development Hub/Addis Ababa Chamber of Commerce and Sectoral Associations, Addis Ababa, 2009, P. 107. [Here in After, Pikremarkos, Review of legal and institutional frame work for Ethiopia]
\textsuperscript{203} Investment Amendment Proclamation, 2002, \textit{Federal Negarit Gazetta}, Proc. No. 280, 8\textsuperscript{th} year, No. 27, Art 6. [Here in After Pro. No. 280/2002]
\textsuperscript{204} Investment Incentive and Investment Areas Reserved for Domestic Investors regulation, 2003, \textit{Federal Negarit Gazetta}, Reg. No. 84, 9\textsuperscript{th} year, No. 34, Schedule. [Here in After, Pro. No. 84/2003]
\textsuperscript{205} ibid.
\textsuperscript{206} East Africa Bottling
\textsuperscript{207} Franchise Under Ethiopian Law
\textsuperscript{208} Cucina Trading, Spur Corporation to open franchise restaurant, <http://capitalethiopia.com>, (last accessed Feb, 2016)
\textsuperscript{209} Four point by Sheraton join hospitality industry at http://www.ethiopiareporter.com, (last accessed 4, March, 2016)
international branded hotel opened in 1969, first downgrading to four star then went down to three star in latest hotel standard ranking of Ethiopia Tourist Commission.  

Recently, new international franchising emerged in the country’s business environment and some Ethiopian businesses are moving towards the still rare practice of franchising. It has been common for a while for a number of cafes and restaurants to open more than one branch across different locations of Addis Ababa. Addis Ababa Trade and Industry Bureau latest data shows that there are seven thousand two hundred thirty five (7235) cafes and food preparation units in the city. They are doing it on their own and with their own management and staff as well as a central kitchen to maintain uniformity of service to their customers. These business entities obviously share characteristics of franchise and have the potential to be franchisors.

Some argue that this is the result of economic development registered during the past consecutive years. A recent International Monetary Fund report identified Ethiopia among the ten fastest growing economies in the world. Currently, the government strives to elevate the society life to middle class economy. In cities like Addis Ababa, the middle class is now witnessed developing the culture of shopping in malls. It is increasingly becoming brand conscious, demanding more convenience, more choice and more brands.

3.1 Franchise’s Role in Economic Development and Technology Transfer

Franchise has a vital role on developing the economy of a country. It is used to create jobs quickly and efficiently by helping local peoples to set up Small and Micro Enterprises under franchise system. It provides investment opportunity for both franchisee and franchisor. Increasingly, even very large multinational companies choose franchise investment as short cut to entry into unfamiliar business culture of a new country. Franchise is a means to get faster and easier brand recognition throughout the world for multinational companies.

The government of Ethiopian is committed to bring economic development and some visible changes are recorded. The Ethiopian economy is projected to grow at an annual rate of 11.2%
annually.\textsuperscript{216} Franchising has become a globally accepted business model for small and medium enterprise development in most economies.\textsuperscript{217} The government of Ethiopia should use franchising to ensure national branding and local economic development.\textsuperscript{218} Franchising has become a globally accepted business model for small and medium enterprise development in most economies. Therefore, the government should stress creating a favorable investment climate that can support franchising as principal development policy direction.\textsuperscript{219}

Industrial Development Strategy has relevancy to foreign and domestic franchise. The industry policy that has been in place since August 2001, clearly stipulate that Ethiopia follow the free market economy.\textsuperscript{220} The key principles of the strategy are recognizing the role that can be played by the private sector as an engine of industrial development.\textsuperscript{221} The state devoted to avoid obstacles that hinder development of private sectors. Hence, no appreciable adverse impact is observed against competition and competitiveness of the private sector.\textsuperscript{222}

Based on the investment laws, both domestic and foreign private investments are extremely encouraged. The investment law encouraged private sector to invest in almost all areas of economy including those sectors formerly reserved for the government, namely defense industries, hydropower generation, and telecommunications services.\textsuperscript{223} Likewise, Ethiopia does not impose local content, technology transfer or export performance requirements on foreign investments.\textsuperscript{224} There are no restrictions on repatriation of earnings, capital, fees or royalties. Now, the country execute Growth and transformation plan (GTP). According to GTP, the Ethiopia vision specifically on economic sectors includes,

\textsuperscript{218} Mulugeta, Franchising Unlocks Ethiopian Small Business Potential
\textsuperscript{219} \textit{Ibid.}
\textsuperscript{221} \textit{Ibid.}
\textsuperscript{222} Trade competition and consumer protection proclamation, 2013, \textit{Federal Negarit Gazetta}, Proc. No. 813, 21th year, No. 28, preamble. [Here in after, Proc. No. 813/2013]
Building an economy which has a modern and productive agriculture sector with enhanced technology and an industrial sector that plays a leading role in the economy, sustaining economic development and securing social justice and increase per capital income of citizens so as to reach the level of those in middle income countries.\textsuperscript{225}

To achieve the GTP plan of using enhanced technologies in the industrial sector franchise play vital role. Franchising affords Ethiopia an opportunity to build its commercial infrastructure, develop its domestically oriented businesses in an efficient and profitable manner. It also offers the opportunity to import and develop foreign technology transfer. Yet, with the exception of some major international franchisors, few have come to Ethiopian market. Therefore, to achieve the GTP plan and other policies of the country encouraging domestic franchise and facilitate smooth and attractive environment for foreign franchisor is necessary

\section*{3.2 The Key Attraction of Franchising in Ethiopia}

\begin{enumerate}
\item Shortage in consumer goods:- Former Ministry of Finance Sofian Amhed once told routers "retail distribution is not competitive, it is archaic".\textsuperscript{226} The Ethiopian consumer retailer business is a source of public grievance and discontent. Necessary consumer products are not found in yesterday price for today. With Ethiopian SMEs challenged by a high failure rate and inconsistent profitability, franchising would have made things better for the businesses as well as the economy at large.\textsuperscript{227} As far as many other countries have ensured improved business survival through franchising, there would have been no need to reinvent the wheel.\textsuperscript{228} In developing countries such as Ethiopia, small business failure is highly correlated with product quality.\textsuperscript{229} Franchising creates a stringent product quality control system, and it guarantees a business a success rate of more than 75pc.\textsuperscript{230}

In order to avert shortage of consumer products, the Ethiopian government at prime minister level announces the government will be forced to invite giant retailers, like Wal-Mart and other strip franchisors.\textsuperscript{231} Unfortunately, the government changed its ideas and established "Ale

\begin{footnotesize}
\textsuperscript{225} Growth and Transformation plan 2010/20, P.21
\textsuperscript{226} Ethiopia wants Wal-Mart and Nakumatt managers, but not their stores
\textsuperscript{227} Mulugueta, Franchising Unlocks Ethiopian Small Business Potential
\textsuperscript{228} ibid
\textsuperscript{229} ibid
\textsuperscript{230} ibid
\textsuperscript{231} Ethiopia Keep Walmart Waiting at <http://www.blogs.ft.com>, [last accessed March 4,2016]
\end{footnotesize}
Bejimela" by taking management skill from giant retailers. However, in near future international franchisor who participates in consumer retailer business may come to Ethiopia. Either the inability of domestic retailers or joining Ethiopia to WTO made it mandatory.

2. Lack of security market: The Ethiopian government rejects the proposal submitted by business community to have security market in Ethiopia. By declaring, the state has no capacity to regulate it. This causes financing one's business in Ethiopia to be dependable in banks loan. Even the loan from banks are not easy to acquire state owned banks gave loan for business who participate in manufacturing sector. Franchise is a solution for resources pooling in a country that has no security market. For local potential franchisor that aims to increase their financial capacity franchising is a solution (they can collect money in the form of royalty and profit sharing).

3. Lower Capital Requirements – If a foreign investor want to invest in Ethiopia it should registered $ 200,000. However, franchising is an excellent way for both Ethiopian and foreign corporations to expand their businesses and make their brand names known in Ethiopia without having to risk large sums of money. For foreign franchisor, the franchisees finance the expansion of the business in Ethiopia. In return, they have the opportunity to make substantial income and capital profits.

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Meles zenawi met senior Walmart executive face to face years ago and negotiation are continuing under meles's successor Hilemariam.

222 Ethiopian Version of Walmart Officially Opened at [http://www directed com], [last accessed 21 Feb, 2016]
223 Us Retailer walmart in Ethiopia: Negotiation underway at [http://www ethiopiapforum com], [last accessed 24 Feb, 2016]
234 "MNCs may use their dominant position or resort to anticompetitive practices to control the market at the expense of the infant local firms. Given the very limited capacity of the competition agencies in countries like Ethiopia, it would often be difficult to investigate anticompetitive practices by the MNCs and take the necessary measures".
236 Proclamation No. 769/2012, Art 11(1)
4. Geographical extent of the country – Franchising can enable a company to take advantage of the vast Ethiopia market of over 84.8 million people.\textsuperscript{237} There is an ever-growing demand of goods and services such as fast food and beverages, clothing, electronic goods, computer hardware and software in the country. These are a huge market opportunity for international franchisor.

5. Business cultural of a society – Franchising well suits the entrepreneurial culture of Ethiopia. Ethiopia business people are fiercely proprietary and feel a need to have ownership and control over their business operations. The existence of limited share companies and PLC shows how much the society wants to have his own business. When we see the number of business organization, the highest number is sole proprietary ship.\textsuperscript{238}

6. Exploit local market knowledge – Ethiopia franchisees offer the foreign franchisors direct access to substantial market knowledge and a considered and sophisticated approach to its exploitation. A company needs a great deal of knowledge of the different regional markets in Ethiopia. Franchising provides sure and easy way of accessing the right level of relevant local market knowledge.

\textsuperscript{237} Investment Guide to Ethiopia,2014,P.3
\textsuperscript{238} Addis Ababa Trade and Industry Bureau Valid business Licenses Registration Data Base Report on April,2016

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CHAPTER THREE
LAWS IN RELATION TO FRANCHISE BUSINESS IN ETHIOPIA

A well-defined legal structure is indispensable for the effective functioning of any business operation. A country that has specific regulation has successful history in franchise, United States America, Australia and South are best examples. By its nature, franchise business requires government's strict regulation from contractual stage until termination. Even if the concept of franchising seems simple, several issues must be dealt with before commencing a sound franchising arrangement. Although franchise is an emerging and very little known form of doing business in Ethiopia, it is very likely that at some point major international franchisors will enter the Ethiopian market. Yet, there is no law enacted solely for regulating the growing business of franchising in Ethiopia. However, various businesses related regulatory laws would govern franchise directly or otherwise.

Franchising is a sophisticated form of licensing in which the franchisor authorizes the franchisee to make use of its intellectual property e.g. its trademarks, trade dress, copyright, knowhow, trade secrets, business concept, methodologies and relevant designs and patents to the franchisee. Owing to the absence of a comprehensive law governing franchise, on the one hand, the franchisor is at liberty to offer whatever terms he wishes to his franchisees. On the other, franchising in Ethiopia leads to the applicability of multiple laws to a franchise transaction.

3.1 Market Entry Procedures for Franchise Business in Ethiopia

As stated above, Ethiopian law does not have anything to offer on franchise. Despite this fact, the investment law has made some progress in regulating technology transfer. Franchise is one of the ways by which technology is transferred from developed countries. Different from

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231 Franchise business under Ethiopian law
240 The Role Intellectual Property in Franchise Arrangement, at <http://www.wipo.com>, [last accessed April, 12, 2016] [Here in after, The Role Intellectual Property in Franchise Arrangement]
previously repealed laws, proclamation No.769/2012 give emphasis for technology transfer. Based on the preamble one of the rationales for enactment of the proclamation is to speed up transfer of technology. Ethiopian Investment Agency (EIA) has duty to register technology transfer agreement related to investment.

Ethiopian Investment Law defines transfer of technology as "the transfer of systematic knowledge for the manufacture of a product, for the application of improvement of a process or for the rendering of a service, including management and technical knowhow as well as marketing technologies, but may not extend to transactions involving the mere sale or lease of goods". Franchise definitions of other jurisdictions have similar elements of technology transfer definition of Ethiopian investment law. China's franchise law, for example, defines transfer of technical knowhow as an element of franchise. Every franchise agreement in one way or another contains systematic transfer of knowledge.

Historically, there is evidence that Ethiopian investment Authority considered franchise as technology transfer. There was an attempt to define franchise under a draft directive that was issued to execute the repealed technology transfer regulation No.121/1993. Draft Transfer of Technology Directives defined franchise agreement as "a business arrangement in which knowledge, expertise and often a trade mark or trade name is licensed to an operator or recipient." If the technology transfer agreement is associated with a franchise agreement, "the franchiser (supplier) must have developed a special business format through which the goods or services are sold under the trademark or name and the good will attached to it."

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242 Proc. No. 769/2012, Art. The Preamble
243 Id. Preamble.
244 Id. Art. 28(10)
245 Id., Art. 2(10)
246 China franchise regulation 2007, Art 3
247 Ibid.
248 Franchise means such business operations by which an enterprise that possesses a registered trademark, enterprise mark, patent, know-how or any other business resource confers the aforesaid business resource to any other business operator through contract, and the franchisee conducts business operations under the uniform business model as stipulated by the contract, and pay franchising fees to the franchiser.
250 Draft Directive for Approval and Registration of Technology Transfer Agreement, Ethiopian Investment Commission, Art 3(3), [here in after, Draft Technology transfer Directive]
251 Id, Article 5(4).
previously repealed laws, proclamation No. 769/2012 give emphasis for technology transfer. Based on the preamble one of the rationales for enactment of the proclamation is to speed up transfer of technology. Ethiopian Investment Agency (EIA) has duty to register technology transfer agreement related to investment.

Ethiopian Investment Law defines transfer of technology as "the transfer of systematic knowledge for the manufacture of a product, for the application of improvement of a process or for the rendering of a service, including management and technical knowhow as well as marketing technologies, but may not extend to transactions involving the mere sale or lease of goods". Franchise definitions of other jurisdictions have similar elements of technology transfer definition of Ethiopian investment law. China's franchise law, for example, defines transfer of technical knowhow as an element of franchise. Every franchise agreement in one way or another contains systematic transfer of knowledge.

Historically, there is evidence that Ethiopian investment Authority considered franchise as technology transfer. There was an attempt to define franchise under a draft directive that was issued to execute the repealed technology transfer regulation No. 121/1993. Draft Transfer of Technology Directives defined franchise agreement as "a business arrangement in which knowledge, expertise and often a trade mark or trade name is licensed to an operator or recipient." If the technology transfer agreement is associated with a franchise agreement, "the franchiser (supplier) must have developed a special business format through which the goods or services are sold under the trademark or name and the good will attached to it." 

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242 Proc. No. 769/2012, Art. The Preamble
243 Id., Preamble.
244 Id., Art. 28(10)
245 Id., Art. 2(10)
246 China franchise regulation 2007, Art 3
247 Ibid.

Franchise means such business operations by which an enterprise that possesses a registered trademark, enterprise mark, patent, know-how or any other business resource confers the aforesaid business resource to any other business operator through contract, and the franchisee conducts business operations under the uniform business model as stipulated by the contract, and pay franchising fees to the franchiser.

250 Id., Article 5(4).
Unfortunately, the draft transfer of technology directive has never entered into force and regulation No.121/1993 was repealed.\textsuperscript{251} Ethiopian investment laws changed frequently after proclamation since Pro. No. 37/1996. Proclamation number 769/2012, contained refined details provision that deals about technology transfer than the previous proclamation 375/2003.\textsuperscript{252} However, none of them has specific reference to franchise agreement as once attempted in the draft directive. The latest investment laws set procedures for registration of technology transfer agreement.\textsuperscript{253} The statutory approach will be discussed further in this paper.

When an investor intends to conclude technology transfer agreement related to his investment, he shall submit it to the agency for approval of registration.\textsuperscript{254} An application form signed by the recipient of technology should submit with the following document.\textsuperscript{255} A photocopy of authenticated technology transfer agreement accompanied by valid recipient business licenses or investment permit.\textsuperscript{256} In addition, certificate of registration or business licenses of provider of a technology are also required for registration of the agreement.\textsuperscript{257} If the required documents are fulfilled certificate of registration shall be issued for the investor by the agency obliged to notify relevant federal executive organs.\textsuperscript{258} According to sources from the EIA, these agencies are the Ministry of Science and Technology and the National bank of Ethiopia.\textsuperscript{259} A technology transfer agreements that is not registered has no legal effect in Ethiopia.\textsuperscript{256} Therefore, one can conclude that as a franchise agreement has similar feature of technology transfer it should be registered in accordance to investment law.

In other jurisdictions, there is regulation that excludes foreign franchisor from participating in sectors reserved for domestic investors.\textsuperscript{261} But there is no clear restriction of foreign franchisor

\textsuperscript{251}Draft Technology Transfer Directive  
\textsuperscript{252}Proc. No. 769/2012, Part five  
\textsuperscript{253}Ibid Art. 21  
\textsuperscript{254}Id., Article 21(1).  
\textsuperscript{255}Id., Article 21(2) A  
\textsuperscript{256}Id., Article 21(2) B and C  
\textsuperscript{257}Id., Article 21(2)D  
\textsuperscript{258}The Agency also charge 200 Ethiopian Birr for services charge.  
\textsuperscript{259}Id., Article 21(3 ) and (5)  
\textsuperscript{260}Interview with Mr. Yonas Abebe, Public prosecutor III Federal trade competition and consumer protection Authority; on regulator enforcement and impact Ethiopian competition law on franchise, April,21, 2016. [Here in after, Interview with Mr. Yonas]  
\textsuperscript{261}"Franchise in India simply what the market need", at <http://www.SSRN.com>, [ last accessed January 28, 21016] [ Here in after, Franchise in India Simply what the market need]
from entering the Ethiopian market.\textsuperscript{262} Investment incentives and areas reserved for domestic investor regulation no 270/2012 has no restrictions on foreign franchisors in areas that are common to franchise business, restaurants and retailers chains.\textsuperscript{263} Business areas that are not allowed for foreign investor are limited in certain business sectors. The number of areas of investments that are not allowed to foreign investors diminished from 18 sectors in 2003\textsuperscript{264} to 11 sector in 2012. Even the previously reserved areas like retail trade, hotels, motels, pensions, tearooms, coffee shops, bars, nightclubs and restaurants and other are now free to foreign investors.\textsuperscript{265}

3.2 The Pertinent Principles of Contract Law of Ethiopia Applicable to Franchise Agreement

Generally, one can hardly speak of the existence of a special legal regime for the regulation of franchise contracts in Ethiopia other than the general rules of the 1960 Civil Code on the Law of contracts. Generally, the franchise agreement is subject to the principles of contract law. Issues in franchising arise as a matter of contract terms, alleged breaches, and remedies.\textsuperscript{266} Franchisor lawyers draft franchise contracts in many situations. "A basic rule of thumb is that one who controls the draft controls the negotiation."\textsuperscript{267} Thus, franchise relationships are guided by contract terms, which are skewed in favor of the franchisor.\textsuperscript{268} Even if it saves money to franchisee, franchise law practitioners advised, do not let a franchisor lawyer draft the contract alone.\textsuperscript{269}

One of the legal issues that arise in franchise contract is enforceability and validity of the franchise agreement. Based on civil code of Ethiopia for an agreement to be valid and enforceable it should fulfill requirements of capacity, consent, object and form in Ethiopia.\textsuperscript{270} Every franchising agreement would necessarily meet the above four criteria in order to be legally

\textsuperscript{262} Investment Incentives and Investment Areas Reserved for Domestic Investor Regulation, 2012, Federal Negarit Gazette, Regulation. No. 270, 19th year, No. 4, article 3.[ here in after, Pro.No. 270/2012]

\textsuperscript{263} Ibid.

\textsuperscript{264} Pro. No. 84/2003

\textsuperscript{265} Id, schedule for areas of investment reserved for domestic investors.


\textsuperscript{268} Robert, Franchise as moral right, P.558

\textsuperscript{269} Warren, International Franchising Arrangements and Problems in Their Negotiation. P. 194

\textsuperscript{270} Civil Code of Ethiopia, Article 1678
enforceable. The contract law does not stipulate franchise contract has to be in writing. However, contracts for long period like insurance, guarantee and other contracts that the law requires should be concluded in writing.\textsuperscript{271} Since franchise contracts are contracts for long period it is advisable to have a formal and written franchising agreement that precisely lay down the rights and obligations of the franchisor and the franchisee.

Another issue that could arise in franchise contract is object of the contract. The object of the contract is required to be lawful and moral.\textsuperscript{272} Usually, the franchisor imposes restrictions on franchisee and the franchisee demands territorial exclusivity and other rights in franchise contract.-As in all other forms of contract, in a franchise agreement the contracting parties should make sure their agreement is not against the law, mainly competition law of Ethiopia. Other countries experience shows such kinds of cases are common.\textsuperscript{273} Fundamentally, parties are presumed to have agreed to benefit from the contract fairly and equitably. The Contract law applies principles of good faith in following situation but not limited on them. One, in cases of contractual mistake the contracting party is required to invoke his mistake was made in good faith.\textsuperscript{274} Second, the law requires the parties to be bound by the terms of the contact and incidental obligations attached to it by custom, equity and good faith.\textsuperscript{275} Third, the law requires the contracts should be interpreted in accordance with good faith and having regarded the loyalty and confidence that should exist between the parties.\textsuperscript{276} Moreover, in case of non-performance when the parties seek cancellation the law imposes an obligation on a court to settle a dispute by considering good faith.\textsuperscript{277}

Another contractual problem that arises in franchise agreement is in the nature of franchise contract. Franchise contracts are mostly adhesion contracts\textsuperscript{278} that are based on “take it or leave it” proposition. Mostly, franchisees raise this fact when dispute arises with franchisors. In contract

\textsuperscript{271} Civil Code of Ethiopia, Art 1725

\textsuperscript{272} Id., Article 1711 and 1716


\textsuperscript{274} Civil Code of Ethiopia, Art 1702

\textsuperscript{275} Id., Art. 1713

\textsuperscript{276} Id., Art. 1732

\textsuperscript{277} Id., Art. 1785(1)

\textsuperscript{278} Black’s Law Dictionary, S.V “Adhesion contract.” A standard-form contract prepared by one party, to be signed by the party in a weaker position, usu. a consumer, who adheres to the contract with little choice about the terms.
law of Ethiopia, the fact that the contract is adhesion contract does not mean the contract is unenforceable. However, the court shall interpret the provisions or words in the adhesive contract against the party who prepared such contract whenever the need for interpretation the contract or a provision thereon comes into the fore. 279 This approach is also followed by other country courts, probably due to the “David and Goliath” view of the franchise relationship, where courts try to protect the party with the weaker position inside the negotiating stage prior to the contract formation. 280 Franchisees are disadvantaged when negotiating the terms of a franchise agreement, and sometimes they need to resort to the courts to have their rights vindicated. 281

The franchisor’s ability to terminate franchisees is a central focus of economic analyses of franchise contracts and their regulation. 282 Many developing and developed nations regulate franchisor termination power. 283 Contract law of Ethiopia requires fulfillment of conditions in the agreement or advance notice for unilateral termination of a contract before expiry of the date. 284

Franchise contract can be terminated by three conditions under the Ethiopian contract law. Termination of contract can be either, by the agreement of parties, unilateral by one party, or judicial by court order. 285 Normally, unless the period is extended by the agreement of the parties, a contract ends when that period expires. Besides that, in order to be an effective and easily implementable contract, it should provide and exhaustively enumerate those factors that may lead to the extinction of contract. 286 There is no restriction on the unilateral termination of franchisor in Ethiopia except provision of notice. The time of notice is subject to legal and customary fixed periods or expected to be reasonable, if law and custom failed to set. 287

279 Civil Code of Ethiopia, Article 1738(2)
"Stipulations inserted in general provisions, model or forms of contract prepared by one party shall be interpreted in favor of the other party".
280 Robert, Franchise Enchroachment, P.244
281 Ibid.
283 Indonesia Franchise Regulation
284 Civil Code of Ethiopia, Art. 1820 and 1821
285 Id., Art.1819-1825
286 Id., Art. 1820(1)
287 Id., Art. 1822
In other countries, many states and territories codify a "good cause" standard; this approach requires franchisors to make an affirmative showing of "good cause" before terminating or otherwise affecting franchisee.\textsuperscript{288} The Ethiopia law has no good cause requirement for unilateral termination rather focus on whether the invoked agreement entitled franchisor such right or not.\textsuperscript{289} The law even gave an additional right for termination of contract by franchisor. "A party may apply to the court to order the termination of a contract which requires a special confidence, cooperation or community of views between the parties, where such requirements are no longer present".\textsuperscript{290}

Franchise business is based on an established product or services reputation. This reputation should be maintained to ensure the consistency of good will and quality standard of the services up to the expectation of loyal customers. In case the franchisor did not foresee during conclusion of contract, the above civil code provision paves way for franchisor to invoke grounds stated in the law to assure the standard. Generally, Ethiopia law does not have any good cause protection for unilateral termination of franchisor.

3.3. Intellectual Property Right Protection for Franchisor and Franchisee under Ethiopia Law

Franchise is one of the most effective means of exploiting Intellectual Property.\textsuperscript{291} Franchised system is a package of intellectual property rights, such as the rights to use the Trade Mark, Trade names, logos, any inventions such as patents or designs, trade secrets, and knowhow of the business and any relevant advertising or copyrighted works relating to the manufacture, sale of goods or the provision of services to customers.\textsuperscript{292} Brand names are deemed to be the keystone of a competitive economy, where individuals are encouraged to do the best they can and make their products recognizable to the public, who will determine their eventual success.\textsuperscript{293} The


\textsuperscript{289} Civil Code of Ethiopia, Art. 1820(1)

\textsuperscript{290} Id., Art. 1823

\textsuperscript{291} The Role Intellectual Property in Franchise Arrangement

\textsuperscript{292} Franchise in India Simply What the Market Need

franchisor acquires market acceptance and customer loyalty as a result of innovation, intensive system development and product refinement.²⁹⁴

The trademark is usually the most important element because it is the foundation on which the brand has been built; brand recognition is what draws customers and stimulates demand.²⁹⁵ Coca Cola Company the world's most valuable brand has immense value of IP assets, according to Forbes's most valuable brand list score number 3 with USD$ 81.5 billion in 2014.²⁹⁶

Every potential franchisor should satisfy the legal requirements of owning intellectual property rights. A franchisor cannot grant its franchisees the right to use a name and trademarks over which it does not have any proprietary rights.²⁹⁷ Therefore, franchisor must then carry out a "legal audit" of its intellectual property rights and make certain that the corner stone's of the franchise agreement, the trade name, trademarks and other intellectual property rights do in fact belong to him.²⁹⁸

For exploitation of intellectual property, providing legal protection and establishing enforcement institution is crucial. A country's legal infrastructure has paramount importance to franchise development. The laws that regulate copyright, trademark, trade name, and patent in Ethiopia have direct impact on franchisor intellectual property right. The Ethiopian Intellectual Property Office/EIPO/ is established as regulatory agency in 2003.²⁹⁹ It is responsible for implementation of national laws governing intellectual property and rendering efficient and effective service for its customers.³⁰⁰

3.3.1 Brand Recognition and Enforcement

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²⁹⁴ Franchise in India Simply What the Market Need
²⁹⁵ World intellectual property organization, In good company managing intellectual property issues in franchising, 2012, P 10
²⁹⁶ Cook Uses Innovation to Boost Brand Value, accessed <at http://www.cocacolacompany.com >,[ last accessed May,26,2016]
²⁹⁷ Frequently asked question in franchise, at < http://www.franchise.org >,[ last accessed May,1,2016],[Here in utter, Frequently asked question in franchise]
²⁹⁸ ibid.
³⁰⁰ Id., Art. 6
Until 2006, Ethiopia had no specific legislation governing the protection of trademarks and service marks. Before that, trademark directive issued in 1986, used to centrally deposit trademarks, which are used by local and foreign enterprises to distinguish their goods or services. Based on the directive, holders of marks published notices in local newspapers to third parties about the existence of the holders’ rights to the marks. That practice were problematic because taken as a whole, it had little legal significance. The deposit certificate did not confer any significant legal right to the holder of the certificate. Disputes related to trademark infringement were adjudicated using unfair competition provisions scattered throughout Ethiopia's commercial, civil, and penal codes. Realizing the need to fix the problem and the importance of trademark protection for socio-economic development, the Ethiopian government issued the Trademark Law.

Franchisors should not even think of negotiating a franchise overseas prior to the registration of relevant trade names, logos, and marks in the target country. Domestic franchisors also required to registering their trademark under the prescribed procedure of the regulation. Article 4 of trademark registration clearly states, "Ownership rights of a trademark shall be acquired and be binding on third parties upon the grant of a trademark registration certificate." Therefore, franchisors should acquire a certificate of registration that last for seven years until its renewal.

300 The role intellectual property in franchise arrangement
In broad terms, a “trade mark” is any sign capable of being represented graphically which distinguishes one entity’s goods or services from those of its competitors. The US Supreme Court has declared that a trademark can be “almost anything at all that is capable of carrying meaning.

303 Ibid.
304 Ibid.
305 Ibid.
306 Ibid.
307 Ibid.
308 Ibid.
309 Ibid.
310 Ibid.
311 Ibid.
312 Ibid.
312 Pro.No. 501/2006, Art 4
Under trademark law of Ethiopia, there are four stages of registration. These are filing of application, examination, publication and opposition, and registration stages. Based on article 8, an application for a trademark registration shall contain applicant name, address, and statement description of the mark and three copies of the mark of one trademark. An applicant cannot submit more than one trademark in one application. If the mark fulfills substantive requirements set under article 6 and 7 of the trademark law, the mark is publicized and call for opposition, if any, is made.

Publication in newspaper allows third parties to oppose the registration of the mark on different grounds. A third party who has an opposition should pay a fee 1500 birr. The registrar should register the mark, where there is no opposition or no valid opposition is instituted. However, due to subjectivity nature of the decision passed by the examination officer, similarity and proliferation of marks that presented to the office, the probability of failure in application is high. Over all, the procedures stated in the regulation that enacted to execute the proclamation are very extensive. One should pass through prolonged procedures, as it takes more than six months in the fastest procedure without for any opposition to be submitted from third party.

Pursuant to article 8(4) trademark law of Ethiopia, "an applicant who is a foreigner shall appoint an agent domiciled in Ethiopia". The regulation requires, "If the application is filed through an agent, the certificate of registration of the agent and a duly authenticated power of attorney should be submitted to the office. The regulation defines the term agent as a trademark agent registered by the Office in accordance with the Regulation. The time duration to registered trademark is long, it may forced a foreign trademark owner to appoint certified trademark agent. Authenticated power of attorney is also required while trademark agent submits a foreign trademark application.

313 Pro. No 273/2012, Art 4, "Any document filed with the Office forming part of an application for registration of a trademark or any proceedings in the Office shall be in the Amharic or English language"
314 Pro. No 501/2006 Art. 8/2/
315 Id. Art. 12.
316 Id. Art. 13.
317 Id. Art.15.
318 Pro. No 273/2012, Art. 9(4)
319 Id., Art. 2(4)
320 Id., Art. 9(4)
Chapter 13 of the regulation is devoted to regulate a person who acquires trademark agent status and the procedure thereof. A resident of Ethiopia who is at least 21 years old and has a license to practice law in Ethiopia or a person who has acquired at least middle level qualification in the relevant field of study, and has a work experience in the area of trademark for not less than three years can apply to be a trademark agent.\textsuperscript{321} If the applicant has no record of conviction for criminal offence or professional misconduct by the court having jurisdiction or relevant regulatory body and passed the evaluation test administered by the office can be licensed for one year to be a trademark agent.\textsuperscript{322}

Foreigners\textsuperscript{323} shall have the same rights and obligations as Ethiopians in regards to trademark registration.\textsuperscript{324} These rights are subject to the principles of reciprocity or terms of any treaty that Ethiopia is a party.\textsuperscript{325} The foreign trademark has acquired registration once it passes the similar procedure of registration of local trademark. However, submission of an authenticated home registration certificate is necessary for foreign trademark to be registered in Ethiopia.\textsuperscript{326} The authentication is required to be made by a notary of the country where the foreign applicant resides, then submitted to Ethiopian embassy where the foreign application originated. The Ministry of Foreign Affairs collects it from the Ethiopian Embassy, for transfer to Ethiopian Notary.\textsuperscript{327} After the Ethiopian notary authenticates it, the document is sent to Ethiopian intellectual property office.\textsuperscript{328} Legal practitioners said that this prerequisite, which is not common in other jurisdictions, is cumbersome and costly in practice.\textsuperscript{329}

The trademark law and regulation recognize priority right based on article 10 and 13 consecutively. The date\textsuperscript{330} an earlier application filed in a foreign country shall be treated as the

\textsuperscript{321} Pro.No 273/2012, Art. 51
\textsuperscript{322} Id.
\textsuperscript{323} Id.
\textsuperscript{324} Pro. No 501/2006, Article 2(4)
\textsuperscript{325} "foreigner" means a person who is not domiciled or has no registered business in Ethiopia
\textsuperscript{326} Id., Art. 3
\textsuperscript{327} Ibid.
\textsuperscript{328} Interview with Mr. Andhalem Ayele, Trade mark and industrial design protection business processor, Public Ethiopian intellectual property office, on regulator enforcement and impact intellectual property law on franchise, April 18, 2016
\textsuperscript{329} Ibid.
\textsuperscript{330} Ibid.
\textsuperscript{329} Ibid.
\textsuperscript{330} Kendal, New intellectual property regulation
\textsuperscript{330} Pro.No. 501/2006, Art 2(4)

"Priority date" means the date of an earlier application that serves as the basis for the right of priority.
date of an application submitted to the Office for registration of a trademark. The regulation provides that the country in which the application is filed should be a party to the Paris Convention for the Protection of Industrial Property or provide similar right. Second, the applicant should submit a certified copy of the earlier application or a priority certificate issued by other country, where the previous application was filed. A certified copy of a business license registration from the home country must accompany foreign trademark application.

3.2 Licensing Trademark under Ethiopian Law

Black's law dictionary defines licensing as the sale of a license authorizing another to use something protected by copyright, patent, or trademark. A license arrangement is a business arrangement where licensor allows the licensee to use, make and sell the product or name for a fee without censure. In a Trade Mark license, the licensee will be granted full privilege to use the trademark on goods or services if the use is in accordance with agreed protocols and quality guidelines. There is usually no training component, product development strategy and limited marketing support.

One of the distinct nature of franchise contract is the franchisor allows the franchisee to use his registered trademark. Even though Ethiopian trademark law does not mention the term franchise, it has well defined procedures on how an owner of a trademark allows the other party to use his trademark. Distinguished from other contracts, trademark application, which is still in process, can be licensed to other person. Based on the trademark law registration is not a validity requirement to license a contract. However, this does not mean that a license contract would be effective forthwith on third parties. The last paragraph of Art 29 (2) provides “...the license contract shall have no effect against third parties until so registered”.

Pursuant to article 2 (7), "License contract means a contract whereby the owner grants to any other person to use a trademark for all or part of goods or services in respect of which the
trademark is registered”. The contract shall be made in writing and shall indicate the extent of the licenses, whether it is for all or part of the goods or services in respect of which the trademark is registered. An application for the registration of license contract of a registered trademark shall be made by filling the form prescribed by the Office for such purpose and be accompanied by a copy license contract and proof of payment of ETB 1,300. The license agreement must be registered at the office of intellectual property registry. By registering a user agreement, the owner prevents the user from getting a right to be the registered proprietor of the mark through use.

In other jurisdictions, the trademark licensing requirements and procedures similarly apply to franchise agreement; Rwanda and Bosnia Herzegovina are examples.

3.3.2 Copy Right and Patent Protection under Ethiopian Laws

Operations manual is the embodiment of the knowhow of the franchise; franchisor invests in creating and developing an operations manual that captures all operational aspects of the business. Franchisors can protect their manuals containing the entire technique of establishing and running the business, videos relating to the use of the product, etc. under the copyright law of Ethiopia. The author of a work shall, irrespective of the quality of the work and the purpose for which the work may have been created, be entitled to protection, for his work without any formality and upon creation. A domestic franchisor’s works acquire automatic recognition based on article 3/1 of copyright law.

The protections of the law towards foreign works are limited in specific situations. A foreign national who his principal residence is Ethiopian, he will get the same protection as of the

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341 Id. Art. 29
342 Ibid
343 Trademark law of Bosnia Herzegovina, The Parliamentary Assembly of Bosnia and Herzegovina at the 8th session of the House of Representatives, held on April 7, 2010, Article 60(7), at <http://www.WIPO.com>, [last accessed Feb. 28, 2016]. [Here in after, Trademark Law of Bosnia Herzegovina]
344 All procedures relating to licensing contract shall apply to franchising contract accordingly.
345 Frequent asked question in franchise
347 Pro. No. 410/2004, Art. 6
348 Pro.No 410/2006, Art. 3(1) A and B
349 Scope of application of copy right law shall apply to on works of authors who are nationals of, or have their principal residence in Ethiopia; Works first published in Ethiopia and, works first published abroad and also

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Ethiopian author. Therefore, unless the work of the foreign national first published in Ethiopia or published abroad and published in Ethiopia within 30 days, it will not be a subject matter of copyright protection. Therefore, a franchisor who publishes or produces operation manuals should insert confidentiality provision in franchise agreement or meet the legal requirement.

In franchising, the industrial property rights made available to the franchisee by the franchisor remain the latter's property. Inventions, Minor Inventions and Industrial Designs, Proclamation No. 123/1995 regulate patent right in Ethiopia. The proclamation provides four forms of protection, patents, and patents of introduction, utility model certificates and certificates of registration of Industrial Designs. Patent means "the title granted to protect inventions, the inventions may relate to a product or a process". In order to be granted a patent, an invention must fulfill three conditions, it must be new, should be capable of industrial application, it must be non-obvious. Certificate of patent issued by the authority certify the exclusive rights of the patentee over his invention.

Right of a patentee include, making, using and, exploiting the patented invention in any other way. The term in any other way, means the patentee has a right to use his invention as a personal property. In other jurisdiction, the common way in which patents are exploited is by licensing contract. Rwanda intellectual property law states a license may be exclusive or non-exclusive. An exclusive license is an agreement under which the owner of a patent grants the licensee permission to use the patented technology to the exclusion of third parties including the licensor. On the other hand, non-exclusive license is simply an act that permits the licensee to

published in Ethiopia within 30 days, irrespective of the nationality or residence of their authors; audiovisual works, the producer of which has his headquarters or principal residence in Ethiopia.  
345 Pro.No 410/2004 Id., Art. 3(1)A  
346 Id., Art. 3(1)(B)  
348 Id., Art. 2(5)  
349 Id., Art. 3(1)  
350 Id., Art. 15  
351 Id., Art. 22(1)  
353 Id., Art. 5(9)  
354 Id., Art. 5(10)
use the patented, just as one of the licensee of the patent owner.\textsuperscript{358} Unlike, trademark law patent law of Ethiopia has no detail provisions on licensing.\textsuperscript{359} However, a third party who wants to use the patented invention has to get the authorization of the owner as per the law.\textsuperscript{360} By entitling this protection, the law creates a favorable environment for local invention and encourages the transfer and adoption of foreign technology.\textsuperscript{361}

Ethiopia follows first to file rule and the right of priority.\textsuperscript{362} When two or more persons who have independently made the same invention separately file applications for patents in Ethiopia on the same subject matter, the right to the patent shall belong to the person who filed the first application.\textsuperscript{363} Exceptionally, subject to reciprocity when foreign applicant files his application in Ethiopia within twelve months from the date that he first filed in a foreign country by furnishing the necessary document he will acquire priority.\textsuperscript{364} Moreover, Ethiopian law gives five years protection for industrial design and utility model certificate.\textsuperscript{365} Criteria of protection for industrial designs\textsuperscript{366} is originality, industrial applicability and not contrary to public order or morality.\textsuperscript{367} For invention that involves small adaptations of existing technology and does not qualify for patent protection, the law provides a utility model certificate.\textsuperscript{368}

So far, Ethiopia patent law does not have provisions that deal with recognition of foreign-awarded patent certificate. Foreign or domestic franchisor needs to register their patent in Ethiopian Intellectual Property Office. Right of prior user recognition of the law has a risk for franchisor who fails to register his patent.\textsuperscript{369} However, patent introduction should serve as mechanism for foreign technology transferor to protect his patent right. "A patent of introduction issued to an invention that has been patented abroad and not expired but has not been patented in

\textsuperscript{358} Intellectual property of Rwanda. Art. 5(11)
\textsuperscript{359} Pro.No. 501/2006, Art 29
\textsuperscript{360} Pro.No. 410/2004, Art. 22(1)
\textsuperscript{361} Pro.No. 123/1995, The Preamble
\textsuperscript{362} Id., Art11(1)
\textsuperscript{363} Ibid.
\textsuperscript{364} Id., Art. 11(2)
\textsuperscript{365} Id., Art. 44 and 50
\textsuperscript{366} Id., Art 2(2)

"Industrial Design" means any composition of lines or colors or any three-dimensional form whether or not associated with lines or colors, provided that such composition or form gives a special appearance to a product of industry or handicraft and can serve as a pattern for a product of industry or handicraft. See art
\textsuperscript{367} Id., 46(1)
\textsuperscript{368} Id., Art.38.
\textsuperscript{369} Pro.No. 123/1995 Art. 26
Certificate will serve as prima facie evidence of entitlement and validity trade name in case a dispute arises.386

The Ministry of Trade, regional trade bureaus and investment agencies, upon delegation, conduct trade name registration.381 Domestic and foreign businesspersons who apply for trade name registration are required to make sure all validity requirements are fulfilled.382 Generally, the proposed trade name shall be free from, misleading consumers, affect interest of third party, harm morality of the society and obtain proper authorization to use name of renowned individuals.383 A foreign businessperson additionally requires to submit properly authenticated commercial registration and trade name registration certificate issued in his country.384

Ethiopia follows registration principle for recognition and protection of trade name.385 Principally, there is no protection for a trade name that is not registered by the concerned organ. However, in few circumstance trade names are protected despite not being registered by authorities.386 One of validity requirements set under article 23 is the proposed name should not be among trade names well known in other countries or is not the one that has international recognition.387 Even though not registered as a trade name in Ethiopia, unless an authorization by the owner to use it has been secured, the proposed name will be rejected by the authority.388 Nevertheless, the Ministry has not yet set the criteria on how an officer can identify the proposed name is well known and has an international recognition.389 These cause registration of internationally well-known trade name by a domestic businessperson.390 In Chapter four of this work, we will discuss the process of trade name registration and its impact on franchise development in a more detailed manner.

386 Pro.No.686/2010, Art. 26(1)
381 id., 22(2)
382 id., Art.24 (3) A up to O
383 id., Art.24 (2)
384 id., Art. 24 (2)
385 id., Art. 26(1)
386 id., Art. 23
387 ibid
388 id., Art. 24(3)
389 Interview with Amelework Mule, Registration and licensing business process team leader, on the Impact of Commercial Registration and Licensing Franchise Business in Ethiopia, April 19, 2016. [Here in After, Interview with Amelework]
390 ibid
Ethiopia regulates registration of foreign trade name in two scenarios. One is in cases where a foreign company wants to establish business by itself. Two, when a domestic businessperson wants to use a trade name of a business organization registered in another country. For foreign company, submitting properly authenticated commercial registration and trade name registration certificate issued by the country in which it was registered or any evidence, which testifies the same, is prerequisite for application.³⁹¹ Domestic business must have obtained authorization from a foreign company to use its trade name and such authorization should be authenticated in Ethiopia.³⁹² Therefore, one can conclude foreign franchisor who wants to open company owned outlet and a domestic franchisee that plans to use other company name should pass through the above procedure. One can say that Ethiopia regulates foreign and domestic franchisor trade name and gives necessary protection for well-known trade names.

3. 4. Franchisor’s Tax Liability and Franchisee Tax Obligation under Ethiopian Tax Law

Withholding tax regime is one of the prominent taxes that apply to franchise in all African countries³⁹³ and it is true under Ethiopian tax laws.³⁹⁴ In Ethiopia, Income tax law schedule D clearly stipulates royalty payment be subject to 5% withholding tax.³⁹⁵ Services provides by nonresident to Ethiopian customer is subject to 15% VAT.³⁹⁶ If a foreign franchisor gives technical services for domestic franchisee outside Ethiopia, his payment is subject to withholding tax of 10% under income tax law.³⁹⁷ The following paragraphs discuss the tax liabilities of franchisor.

Based on article 31(1) of the income tax proclamation³⁹⁸ and standard definitions that Ethiopia signed for avoidance of double taxation royalty means,

A payment of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work, including computer software cinematograph films, or films or tapes used

³⁹¹Pro.No 686/2010, Art. 24(2)
³⁹²Id., Art. 24(3)M
³⁹³Babette, Franchising in Africa, P. 131
³⁹⁵Id., Art. 31(1)
³⁹⁶Value added tax proclamation, 2002, Federal Negarit Gazetta, Proc. No. 285, 8 th year, No. 33, Article 7(1) C.
³⁹⁷Id., Art. 31(1)
³⁹⁸Double Taxation Avoidance Agreement between Saudi Arabia and Ethiopia, at <http://www.capitaletopia.com>
³⁹⁹, [last accessed April 30,2016]. [Here in after, Ethio-Saudi DTT]
for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process, or for the use or for the right to use of any industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience or the rendering of any services or assistance of a technical or consultancy nature. 399

Royalties paid by the franchisee to the franchisor for the use of the franchisor's intellectual property rights, would be subject to withholding tax. 400 In case of an international franchise agreement, royalties may be taxed on resident state rather than source state depending upon the provisions in any double taxation avoidance agreement. 401 For instance, Ethiopia has signed double taxation treaties (DTTs) with two dozen countries. 402 In relation to royalties, many of the DTTs of Ethiopia contain similar provisions. Based on the agreement royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State. 403 In some agreements, such royalties may also be taxed in the Contracting State in which they arise and according to the laws of that State, if the beneficial owner of the royalties is a resident of the other Contracting State, the tax so charged shall not exceed 5 per cent of the gross amount of the royalties. 404

The term "technical service" 405 means any kind of expert advice or technological service rendered by nonresident. 406 All payments made in consideration of any kind of technical services rendered outside Ethiopia to resident persons in any form shall be liable to tax at a flat rate of ten percent. 407 However, based on DTTs fees for technical services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State. 408 A

399 Pro.No. 286/2002, Article 31(5) and Double taxation avoidance agreement of Ethiopia with India, article 12(3) at <http://www.assenbriefing.com>, [last accessed April 30,2016], [Here in after, Ethiopia-India DTT]
400 Pro.No. 286/2002, schedule D
401 United Nations, "Model Double Taxation convention between Developed and Developing Countries", Department of economic and social affairs , United nation, New York, 2001, p. 190
403 Ethiopia-SAudi DTT
404 Double taxation avoidance agreement between Ethiopia and Netherlands , at <http://www.rijksoverheid.com>, [last accessed April 30,2016]
405 Ethiopia-India DTT Art. 12 (3) B
406 Define fees for technical services means payments of any kind as consideration for managerial or technical or consultancy services, including the provision of services of technical or other personnel.
407 Pro.No. 286/2002, Art. 32(2)
408 Id. Art. 32(1)
409 Ethiopia-India DTT, Art. 12(1)

57
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396 Pro.No. 286/2002, Article 31(5) and Double taxation avoidance agreement of Ethiopia with India, article 12(3) at <http://www.assemblybriefing.com>, [last accessed April 30, 2016]. [Here in after, Ethio-India DTT]
397 Pro.No. 286/2002, schedule D
398 United Nations, "Model Double Taxation convention between Developed and Developing Countries", Department of economic and social affairs, United nation, New York, 2001, p. 190
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