

THE FRANCHISE LAW  
REVIEW

EIGHTH EDITION

Editor  
Mark Abell

THE LAWREVIEWS

THE  
FRANCHISE LAW  
REVIEW

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# CONTENTS

PREFACE.....	vii
<i>Mark Abell</i>	
Chapter 1      WHAT IS FRANCHISING? .....	1
<i>Mark Abell</i>	
Chapter 2      FRANCHISING AS PART OF AN INTERNATIONAL MULTICHANNEL STRATEGY .....	3
<i>Mark Abell</i>	
Chapter 3      THE REGULATION OF FRANCHISING AROUND THE WORLD.....	8
<i>Mark Abell</i>	
Chapter 4      INTELLECTUAL PROPERTY.....	27
<i>Allan Poulter and Robert Williams</i>	
Chapter 5      DATA PROTECTION.....	33
<i>Ruth Boardman, Francis Aldhouse and Elizabeth Upton</i>	
Chapter 6      TAX CONSIDERATIONS.....	40
<i>Zoe Feller and Caroline Brown</i>	
Chapter 7      TRADE SECRETS AND FRANCHISING.....	93
<i>Mark Abell and Jonathan Goldsworthy</i>	
Chapter 8      FRANCHISEES AS CONSUMERS.....	101
<i>Jiri Jaeger and Frederik Born</i>	
Chapter 9      RESOLVING INTERNATIONAL FRANCHISE DISPUTES.....	110
<i>Victoria Hobbs</i>	
Chapter 10     E-COMMERCE AND FRANCHISING.....	123
<i>Ben Hughes and Francesca Longworth</i>	

Chapter 11	THE COMPETITION LAW OF THE EUROPEAN UNION .....	131
	<i>Mark Abell</i>	
Chapter 12	THE IMPACT OF COVID-19 AND BREXIT ON FRANCHISING .....	138
	<i>Mark Abell</i>	
Chapter 13	EDITOR'S GLOBAL OVERVIEW .....	145
	<i>Mark Abell</i>	
Chapter 14	AFRICA OVERVIEW .....	152
	<i>Nick Green</i>	
Chapter 15	GCC OVERVIEW .....	157
	<i>Melissa Murray</i>	
Chapter 16	AUSTRIA.....	169
	<i>Eckhard Flohr and Alfons Umschaden</i>	
Chapter 17	BRAZIL.....	185
	<i>José Carlos Vaz e Dias and Bruna Valois</i>	
Chapter 18	CHILE.....	200
	<i>Cristóbal Porzio</i>	
Chapter 19	CHINA.....	213
	<i>Sven-Michael Werner</i>	
Chapter 20	CZECH REPUBLIC .....	226
	<i>Vojtěch Chloupek</i>	
Chapter 21	DENMARK .....	238
	<i>Jacob Ørskov Rasmussen</i>	
Chapter 22	FRANCE.....	252
	<i>Raphaël Mellerio</i>	
Chapter 23	GEORGIA .....	263
	<i>Mikheil Gogeshvili</i>	
Chapter 24	GERMANY.....	274
	<i>Stefan Münch, Alexander Duisberg, Markus Körner and Michael Gafßner</i>	

## Contents

---

Chapter 25	HONG KONG .....	284
	<i>Michelle Chan and Hank Leung</i>	
Chapter 26	HUNGARY.....	296
	<i>Péter Rippel-Szabó, Bettina Kövecses and Péter Sziládi</i>	
Chapter 27	INDIA.....	312
	<i>Nipun Gupta and Divya Sharma</i>	
Chapter 28	IRAN.....	326
	<i>Shelley Nadler and Farid Kani</i>	
Chapter 29	ITALY.....	336
	<i>Claudia Ricciardi</i>	
Chapter 30	JAPAN.....	350
	<i>Kentaro Tanaka</i>	
Chapter 31	KAZAKHSTAN.....	365
	<i>Nick Green and Saule Akhmetova</i>	
Chapter 32	MALAYSIA.....	376
	<i>Lee Lin Li and Chong Kah Yee</i>	
Chapter 33	NEW ZEALAND.....	401
	<i>Stewart Germann</i>	
Chapter 34	POLAND.....	416
	<i>Kuba Ruiz</i>	
Chapter 35	RUSSIA.....	430
	<i>Sergey Medvedev</i>	
Chapter 36	SAUDI ARABIA.....	447
	<i>Melissa Murray</i>	
Chapter 37	SINGAPORE.....	457
	<i>Lorraine Anne Tay and Just Wang</i>	
Chapter 38	SWITZERLAND.....	473
	<i>Christophe Rapin and Vincent Jäggi</i>	

## Contents

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Chapter 39	TAIWAN.....	488
	<i>Wen-Yueh Chung, Jane Wang and Charles Chen</i>	
Chapter 40	UKRAINE.....	500
	<i>Volodymyr Yakubovskyy and Graeme Payne</i>	
Chapter 41	UNITED KINGDOM.....	510
	<i>Graeme Payne</i>	
Chapter 42	UNITED STATES.....	534
	<i>Steven Feirman, Daniel Deane, Keri McWilliams, Brad Steinbrecher, Kendal Tyre and Nathan Warecki</i>	
Chapter 43	DISPUTE RESOLUTION APPENDIX.....	556
	<i>Pablo Berenguer and María Fuentes</i>	
Appendix 1	ABOUT THE AUTHORS.....	559
Appendix 2	CONTRIBUTORS' CONTACT DETAILS.....	583

# PREFACE

Since the publication of the seventh edition of *The Franchise Law Review*, the major economic and geopolitical developments that we would expect to have a significant impact on world trade have been dwarfed by the impact of the coronavirus pandemic. Covid-19 has had a devastating effect on the global economy and despite the advent of vaccines and the roll-out of national vaccination programmes, it is likely to continue to do so for some time to come. Through all this, however, the apparently inexorable march towards the globalisation of commerce has continued unabated. While there have been some economic bright spots, the global economy continues to underperform and concerns persist about the stability of the US economy.

As a consequence, businesses are often presented with little choice but to look to more vibrant markets in Asia, the Middle East and Africa for their future growth. At the same time, South–South trade is on the increase, perhaps at the expense of its North–South counterpart. All of this, coupled with the unstable wider geopolitical landscape, presents business with only one near certainty: there will be continued deleveraging of businesses in the coming years and, thus, growing barriers to international growth for many of them. All but the most substantial and well-structured of such businesses may find themselves facing not only significant difficulties through reduced access to funding for investment in their foreign ventures, but also challenges arising from their lack of managerial experience and bandwidth.

Franchising, in its various forms, continues to present businesses with one way of achieving profitable and successful international growth without the need for either substantial capital investment or a broad managerial infrastructure. In sectors as diverse as food and beverages, retail, hospitality, education, healthcare and financial services, franchising continues to be a popular catalyst for international commerce and makes a strong and effective contribution to world trade. We are even seeing governments turning to it as an effective strategy for the future of the welfare state as social franchising gains still more traction as a way of achieving key social objectives.

Given the positive role that franchising can play in the world economy, it is important that legal practitioners have an appropriate understanding of how it is regulated around the globe. This book provides an introduction to the basic elements of international franchising and an overview of the way that it is regulated in 29 jurisdictions.

As will be apparent from the chapters of this book, there continues to be no homogenous approach to the regulation of franchising around the world. Some countries specifically regulate particular aspects of the franchising relationship. Of these, a number try to ensure an appropriate level of pre-contractual hygiene, while others focus instead on imposing mandatory terms upon the franchise relationship. Some do both. In certain countries, there is a requirement to register certain documents in a public register. Others restrict the manner

in which third parties can be involved in helping franchisors meet potential franchisees. No two countries regulate franchising in the same way. Even those countries that have a well-developed regulatory environment seem unable to resist the temptation to continually develop and change their approaches – as was well illustrated by changes to the Australian regulations in the recent past. The unstoppable march towards franchise regulation continues, with countries such as Argentina, which previously had not specifically regulated franchising, adopting franchise-specific laws in the past year or so.

Many countries do not have franchise-specific legislation but nevertheless strictly regulate certain aspects of the franchise relationship through the complex interplay of more general legal concepts such as antitrust law, intellectual property rights and the doctrine of good faith. This heterogeneous approach to the regulation of franchising presents yet another barrier to the use of franchising as a catalyst for international growth.

While this book certainly does not present readers with the complete answer to all the questions they may have about franchising in all the countries covered – that would require far more pages than it is possible to include in this one volume – it does seek to provide the reader with a high-level understanding of the challenges involved in international franchising in the first section, and then, in the second section, explains how these basic themes are reflected in the regulatory environment within each of the countries covered. I should extend my thanks to all of those who have helped with the preparation of this book, in particular Caroline Flambard and Nick Green, who have invested a great deal of time and effort in making it a work of which all those involved can be proud. It is hoped that this publication will prove to be a useful and often-consulted guide to all those involved in international franchising, but needless to say it is not a substitute for taking expert advice from practitioners qualified in the relevant jurisdiction.

**Mark Abell**

Bird & Bird LLP

London

January 2021

# MALAYSIA

*Lee Lin Li and Chong Kah Yee<sup>1</sup>*

## I INTRODUCTION

The Malaysian government has been an active proponent of franchising as a business model. Despite the covid-19 pandemic and its impact on the global economy, Malaysia's economy continues to recover and is set to continue improving.<sup>2</sup> With the speedy implementation of various stimulus and recovery measures to boost and strengthen the economy, Malaysia had posted the best recovery among major ASEAN countries in the third quarter of 2020, with a much slower pace of contraction, 2.7 per cent, than the double digit decline of 17.1 per cent in the second quarter.<sup>3</sup> While Malaysia's gross domestic product is expected to register a contraction of 4.5 per cent for 2020, it is also expected to grow between 6.5 per cent and 7.5 per cent in 2021.<sup>4</sup>

The Ministry of Domestic Trade and Consumer Affairs (MDTCA) has been charged with monitoring the continued growth of the franchising sector in Malaysia. These efforts have culminated in the enactment of the Franchise Act 1998 (amended in 2012) (the Act) and the establishment of the Franchise Registry.

Foreign franchisors, particularly those with unique franchise models and concepts, are actively encouraged to enter into the Malaysian market. Between January 2000 and February 2020, the number of registered franchise businesses from various sectors in Malaysia increased to 1,019, up from 1,003 in June last year, and of which 610 are local brands and 409 are foreign brands.<sup>5</sup> This represents an increase in registered franchise businesses in Malaysia of approximately 1.57 per cent.

The Malaysian government, in recognition of the revenue streams that franchising models offer, has actively promoted the growth of domestic franchises. This support has been in the form of state grants, soft loans and business education programmes organised by the MDTCA and Perbadanan Nasional Berhad (PNS). PNS falls within the joint purview of the Ministry of Finance and the MDTCA. PNS is charged with spearheading the growth of the local franchise industry and assisting its expansion abroad, allocating and managing

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1 Lee Lin Li is a partner and Chong Kah Yee is an associate at Tay & Partners.

2 <https://www.nst.com.my/news/nation/2020/11/641356/budget-2021-malaysia-path-economic-recovery>.

3 See <https://www.treasury.gov.my/index.php/en/gallery-activities/press-release/item/7366-media-release-commentary-on-q3,-2020-gdp-growth.html> and <https://www.nst.com.my/news/nation/2020/11/641356/budget-2021-malaysia-path-economic-recovery>.

4 *ibid.*

5 See <https://www.kpdnhep.gov.my/kpdnkk/wp-content/uploads/2019/10/STATISTIK-UTAMA-KPDNHEP-JUN-2019.pdf>.

grants and offering business support in the form of franchise consultation and other advisory services. These efforts have led to significant growth in the number of local franchisors in the past decade.

The government has introduced various schemes and incentives to assist and support franchisors and franchisees in developing their brands and expanding their franchise businesses, such as the Franchise Financing Scheme, Franchise Development Assistance Fund, Small Franchise Financing Scheme, Franchise Development Programme, and Local Franchise Product Development Programme.

The Malaysian Franchise Association (MFA) was formed in 1994. It has a wide membership base that includes representatives from the franchising industry, service providers such as accountants, franchise consultants and bankers, and government bodies. All members are required to abide by the MFA's Code of Ethics of a Professional Conduct of Franchise Practitioners.<sup>6</sup> The MFA maintains professional and ethical standards by enforcing this code of practice among its members.

The MFA serves as a resource centre for franchisors and franchisees, the media and the public. It also acts as a networking and discussion forum between the private sector, franchise industry and government agencies.

## II MARKET ENTRY

### i Restrictions

Prior to the introduction of the Act, parties were free to negotiate their own terms and were governed by contract and common law. This allowed for a higher degree of flexibility. The franchising industry is now regulated by the Act, which places greater restrictions on foreign franchisors and introduces criminal liability for certain acts.

Section 54 of the Act requires that all foreign franchisors intending to set up franchises or enter into franchise agreements with any Malaysian citizen obtain prior approval from the Franchise Registry. Applications for registration are required to be supported by documents that include:<sup>7</sup>

- a* a sample franchise agreement;
- b* a certified true copy of the applicant's certificate of incorporation;
- c* document evidencing changes in shareholding of the company, if applicable;
- d* details of the franchise concept, including the uniqueness of the brand's franchise system and franchise experience;
- e* official declaration from the Insolvency Department that the board of directors are free from bankruptcy;
- f* a certified true copy of the registration certificate of the franchise's trademarks issued by the intellectual property office of the brand's country of origin and the Intellectual Property Corporation of Malaysia (MyIPO) (or proof of an application for such a registration);
- g* the company's brochure or profile;
- h* pictures of a prototype outlet; and

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6 See <http://www.mfa.org.my/newmfa/background/>.

7 See <https://myfex.kpdnhep.gov.my/>.

- i* a certified true copy of the latest three years' audited accounts that have been notarised by a notary public.

Decisions are communicated by the Registrar of Franchise in writing and the approval remain in place until the Registrar issues an order suspending, terminating, prohibiting or refusing the sale and registration of the franchise as permitted under the Act or where an applicant or franchisor seeks a cancellation of the approval.

Apart from Section 54 of the Act, there are no restrictions placed on foreign franchisors with regard to granting a master franchise or development rights to a local franchisee. The appointed master franchisee or a franchisee of the foreign franchisor is required to register its franchise with the Franchise Registry before making an offer to sell the franchise to any person or commencing the franchise business, respectively.<sup>8</sup>

Foreign franchisors are permitted to acquire equity in local businesses and real property subject to certain conditions.

Franchises with foreign equity must be incorporated locally, either as a subsidiary, a representative or branch office to carry on business in Malaysia.

All distributive trades, which includes retailers, wholesalers, franchise practitioners and direct-selling businesses, are required to obtain approval from the MDTCA before they are able to operate in Malaysia and are required to comply with the MDTCA's Guidelines on Foreign Participation in the Distributive Trade Services (the MDTCA Guidelines).<sup>9</sup>

These Guidelines are extensive and cover the following:

- a* acquisitions, mergers or takeovers by foreign participation;
- b* the opening, relocation, expansion of branches or outlets or chain stores;
- c* buying over or taking over of outlets of other operators; and
- d* real property transactions relating to distributive trade activities (prior to obtaining other necessary approvals or licences from local authorities and other government agencies).

In addition, all distributive trades with foreign equity are required to:

- a* appoint a *bumiputra* or Malay director or directors (*bumiputra* is a local term that refers to the indigenous peoples of Malaysia encompassing ethnic Malaysia and other minority indigenous ethnic groups);
- b* hire local (Malaysian) personnel at all levels, particularly for management positions and above;
- c* have low-skilled foreign workers comprise only 15 per cent of the total workforce;
- d* develop and provide transparent standard operating procedures for local suppliers to market their goods;
- e* encourage *bumiputra* or Malay participation in the distributive trade sector;
- f* hire at least 1 per cent of the total workforce from among persons with significant disabilities;
- g* increase the utilisation of local airports and ports in the export and import of goods;
- h* encourage utilisation of local professional services available in Malaysia;

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<sup>8</sup> A master franchisee is required to obtain approval under Section 6 of the Franchise Act 1998, whereas a franchisee of a foreign franchisor is required to obtain approval under Section 6A of the Franchise Act 1998.

<sup>9</sup> Guidelines on Foreign Participation in the Distributive Trade Services Malaysia, by the MDTCA; see [https://www.kpdnhep.gov.my/images/FINAL\\_GP\\_2020.pdf](https://www.kpdnhep.gov.my/images/FINAL_GP_2020.pdf).

- i* submit audited annual financial reports to the MDTCA;
- j* support the initiatives and agenda for sustainable development as provided in the Sustainable Development Goals by the Malaysian government; and
- k* comply with all local authority by-laws and regulations.

The MDTCA Guidelines also impose specific conditions on franchises operating in certain industry sectors. These include:

- a* for businesses operating in the hypermarket sector, a minimum capital requirement of 50 million ringgit and a requirement for a minimum 30 per cent of equity to be held by *bumiputra* or Malay ownership
- b* in the department store sector, a minimum capital requirement of 20 million ringgit;
- c* for superstores operating as self-service distribution stores retailing mainly consumer goods that comprise of a mix of food and non-food products, a minimum capital requirement of 25 million ringgit; and
- d* for specialty stores serving an exclusive brand name, product or line of goods, a minimum capital requirement of 1 million ringgit.
- e* for convenience stores qualifying as distribution stores operating 24 hours a day and selling fast-moving items, a minimum capital requirement of 1 million ringgit and a requirement for a minimum 30 per cent of equity to be held by *bumiputra* or Malay ownership with a maximum foreign interest of 30 per cent; and
- f* for distribution centres (i.e., specialised buildings designed to store goods temporarily prior to redistribution to another location), a minimum capital requirement of 1 million ringgit.

Generally, in an effort to promote local participation, government agencies are actively tasked with encouraging the formation of joint ventures between Malaysians and foreign investors instead of allowing wholly foreign-owned corporations to operate independently.

Pursuant to the National Land Code, a foreigner is required to obtain prior approval from the relevant state authority for transactions regarding real property. Any property transactions without this formal approval are rendered void.<sup>10</sup> In addition to the requirements of the National Land Code, there are further restrictions in place and these are, broadly, as follows:<sup>11</sup>

- a* foreigners are generally prohibited from purchasing properties valued at below 1 million ringgit; and
- b* where the property is valued at or above 1 million ringgit, there are generally no restrictions, but where a property is valued at over 20 million ringgit and the purchase results in the dilution in the ownership of property held by *bumiputra* interest or government agency, prior approval will be required from the Economic Planning Unit.

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10 Sections 433A, 433B and 433C of the National Land Code 1965.

11 Guidelines on the Acquisition of Properties (2014), by the Malaysian Economic Planning Unit; see <http://103.8.145.121/en/en/sites/default/files/GP%2520EPUJPM%2520-%2520English%25202014.pdf>.

## ii Foreign exchange and tax

### *Foreign exchange*

Foreign exchange issues are governed by the Foreign Exchange Administrative Rules issued by the Central Bank of Malaysia and the Financial Services Act 2013 (FSA).

Residents<sup>12</sup> and non-residents<sup>13</sup> are defined within Section 213 of the FSA. The Malaysian market is generally accessible by foreign investors. Payment for investments can be made in a foreign currency or in Malaysian ringgit. Non-residents are free to remit divestment proceeds, profits, dividends or any income arising from investments in Malaysia abroad. Any repatriation of funds must, however, be made in foreign currency. Non-residents are also free to:

- a open ringgit or foreign currency accounts in Malaysia;
- b obtain credit facilities in Malaysia in ringgit or foreign currency;
- c obtain loans of any amount from Malaysian residents to finance the purchase of immovable properties in Malaysia; and
- d enter into foreign exchange contracts on a spot or forward basis with onshore licensed banks to hedge investments in Malaysia.<sup>14</sup>

Non-resident travellers may:

- a bring in or take with them, Malaysian currency up to the value of US\$10,000; and
- b bring in any amount of foreign currency, including traveller's cheques.<sup>15</sup>

### **Tax**

The imposition of tax is governed by the Income Tax Act 1976. Non-resident companies are subject to withholding tax on royalty payments derived from within Malaysia. This imposes a legal obligation on the party or franchisee making the payment to a non-resident to withhold tax at source and remit it to the Inland Revenue Board of Malaysia within a specified period (usually within a month of the date of the payment or royalties).<sup>16</sup>

## III INTELLECTUAL PROPERTY

### i Brand search

Registration of intellectual property rights (IPRs) such as, trademarks, patents, industrial designs and geographical indications is administered by MyIPO. Prior to filing an application to register marks, it is prudent for franchisors seeking to enter into the Malaysian market

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12 Section 213 of the Financial Services Act 2013. Residents include Malaysian citizens, foreign citizens who have been accorded permanent residence status and who reside in Malaysia and companies incorporated in Malaysia.

13 Section 213 of the Financial Services Act 2013. Non-residents include foreign citizens, foreign embassies or high commissions, supranational Malaysian citizens who have acquired permanent residence status abroad and who reside abroad and foreign corporate entities.

14 Foreign Exchange Administration Rules of the Central Bank of Malaysia; see [http://www.bnm.gov.my/files/doc/fea/archive/FEA\\_rules\\_Part\\_2\\_Non-residents%202019.pdf](http://www.bnm.gov.my/files/doc/fea/archive/FEA_rules_Part_2_Non-residents%202019.pdf).

15 *ibid.*

16 Section 109(1) of the Income Tax Act 1967.

to undertake trademark searches against the databases maintained by MyIPO to ascertain whether there are any conflicts, potential or otherwise. Similar searches may be conducted with regard to other IPRs, such as industrial designs and patents.

Following the launch of an online search portal by MyIPO in 2010, all trademark searches are now conducted online.<sup>17</sup> However, as the online search portal is limited in its field of searches, the search results may not be comprehensive. It is, therefore, advisable to conduct searches using the online facilities provided at the Registry of Trademarks. Such searches will be subject to official fees but will provide more comprehensive search results.

MyIPO also maintains databases for granted patents and registered industrial designs, which are open to public search and inspection and which may similarly be searched using the MyIPO online search portal.<sup>18</sup> As with trademarks, however, it is advisable to conduct searches at the Registry of Patents and the Industrial Designs Registration Office to obtain more comprehensive search results.

Franchisors should also perform further searches against the database for registered companies and businesses maintained by the Companies Commission of Malaysia (CCM).<sup>19</sup> The CCM is charged with approving applications for, and maintaining the registration of, companies and businesses in Malaysia. As the CCM does not, as a matter of practice, conduct any cross-reference searches with MyIPO, a registered trademark may well be registered by a third party as a company name. In such an instance, and in the absence of any direct settlement with the company or business concerned, the only recourse available to a trademark owner is to commence court proceedings for the alteration of the registered company or business name.

## ii Brand protection

Section 24 of the Act requires a franchisor to register any trademarks relevant to his or her franchise prior to applying for registration with the Franchise Registry. Trademark applications take time to mature to registration. Hence, it is important to file the applications for registration of the marks early, before the franchise commences operation and, wherever possible, as soon as practicable after the franchisor has made a decision to expand its franchise in Malaysia. The Franchise Registry usually accepts proof of filing for registration in place of a certificate of registration of the marks.

The trademark filing process involves two main stages. After the trademark application is filed, it will be examined for compliance with formalities and substantive requirements. If the requirements were met, the Registrar would accept and publish the application in the Intellectual Property Official Journal for opposition purposes by third parties. If there are no oppositions, a sealed notification of registration will be issued. The entire process takes between nine and 12 months from the filing date to registration. If the requirements were not met, the Registrar would issue a provisional refusal of the application based on absolute grounds (inherent registrability) or relative grounds (conflict with earlier or well-known marks), or a combination of these. The applicant would be given an opportunity to submit a response to the objection by filing written submissions or by applying for a hearing to

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17 See <https://iponlineext.myipo.gov.my/SPHI/Extra/IP/TM/Qbe.aspx?sid=637102816544748876>.

18 See database of the Registry of Patents at <https://iponlineext.myipo.gov.my/SPHI/Extra/IP/PT/Qbe.aspx?sid=637102817725493492> and database of the Industrial Design Registration Office at <http://onlineip.myipo.gov.my/index.cfm/search/id/index>.

19 See <https://www.ssm-einfo.my/page.php>.

submit oral arguments. If the applicant is successful, the application would be accepted and the steps indicated above are followed until the sealed notification of registration is issued. If the applicant is unsuccessful, a total provisional refusal would be issued whereupon the applicant may appeal to the High Court within one month of the date of the Registrar's decision to refuse the application.

The initial period of registration is 10 years from the date of application, which is deemed to be the date of registration.<sup>20</sup> The trademark may be renewed every 10 years before the expiry date. If it is not renewed before the expiry date, late renewal may be filed within six months of the expiry date. If late renewal is not filed, the application will be deemed removed and an application to restore the registration may be filed within six months of the date of removal. Failure to do either of these will result in the cessation of the registration.

A registered trademark is also vulnerable to cancellation on the grounds that: (1) the trademark has not been used in good faith for a period of three years from its registration and there are no proper reasons for non-use; (2) the use of the goods or services for which the trademark is registered has been suspended for an uninterrupted period of three years and there are no proper reasons for non-use; (3) the trademark has become a common name in the trade because of the registered proprietor's acts or inactivity; or (4) the use of the trademark by the registered proprietor would mislead the public.<sup>21</sup>

### **iii Enforcement**

The main IPRs applicable to a franchise are trademarks, confidential information or trade secrets, know-how and copyright. In certain businesses, other IPRs such as industrial designs and patents may also be applicable.

A registered proprietor has recourse under the relevant legislation or common law to seek relief for the infringement of any of its IPRs. Infringement actions in respect of trademarks, copyright, industrial designs and patents are generally initiated in the High Court. Other rights such as breach of confidentiality or trade secrets or passing off may also be initiated in the Sessions Court (a subordinate court) if the claim for damages does not exceed 1 million ringgit.<sup>22</sup> Both the High Court and the Sessions Court have jurisdiction to grant interim or permanent injunctive and specific reliefs.<sup>23</sup> The reliefs ordinarily sought in civil actions for infringement are permanent injunctive orders prohibiting further infringing acts, orders for the delivery of the infringing articles, damages or an account of profits and legal costs.

Where a trademark is infringed, a registered proprietor or an exclusive licensee of the trademark may commence a civil action pursuant to the Trademarks Act 2019 (TMA),<sup>24</sup> and where the mark has been used in Malaysia such that there is goodwill and reputation associated with it, there is additional recourse under common law for passing off. The standard reliefs are usually available in such actions and these have been codified under the TMA.

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20 Section 39(1) of the Trademarks Act 2019.

21 Section 46(1) of the Trademarks Act 2019.

22 Section 65(1)(b) of the Subordinate Courts Act 1948.

23 Sections 65(1)(c) and (5)(a) of the Subordinate Courts Act 1948 and Section 25(2) of the Courts of Judicature Act 1964.

24 Sections 56 and 71 of the Trademarks Act 2019.

A registered proprietor may also have recourse to administrative relief in the form of border protection measures to prevent the importation of counterfeit goods, and to criminal remedies under the TMA<sup>25</sup> whereby the Enforcement Division of the MDTCA may be moved to initiate a raid, seize infringing or counterfeit goods and prosecute the persons responsible.

Know-how, trade secrets and confidential information are protected through contract law and under the common law tort of breach of confidential information. In the case of a franchise business model, Section 26 of the Act provides that a franchisee is required to provide the franchisor with a guarantee that the franchisee, including its directors, their spouses and immediate family, and its employees, may not disclose any information contained in the training or operation manual or information obtained from the franchisor during the term of the franchise agreement. Failure to provide such a guarantee is tantamount to an offence under the Act.

Where these obligations of confidence are set out in the franchise agreement or a confidentiality agreement or undertaking, a franchisor will also have recourse to a civil action for breach of confidentiality under contract and common law.

While there is no compulsory registration system for copyright in Malaysia, it is possible to provide voluntary notification of copyright ownership to the MyIPO. A work is eligible for copyright protection upon the fulfilment of certain conditions, which include labour, skill and judgement to make the work original, where the work is reduced in material form, written down or recorded and the author is a Malaysian or the work is produced or made in Malaysia. Works that are protected under copyright include literary, musical artistic or dramatic works.<sup>26</sup>

When a copyright work is infringed, the proprietor of the copyrighted work may initiate a civil action and seek injunctive reliefs similar to the standard reliefs and, in addition, may seek statutory damages of not less than 25,000 ringgit for each work and not more than 500,000 ringgit on aggregate.<sup>27</sup> The copyright owner may also have recourse to criminal remedies provided under the Copyright Act 1987<sup>28</sup> by lodging a complaint with the Enforcement Division of the MDTCA to request that a seizure action be carried out in respect of the infringing activities.

Similarly, if other IPRs, such as patents<sup>29</sup> or industrial designs,<sup>30</sup> registered in Malaysia are concerned, the registered proprietor will have similar recourse to the civil remedies discussed above for such infringements.

#### **iv Data protection, cybercrime, social media and e-commerce**

The Personal Data Protection Act 2010 (PDPA) and regulations made thereunder, including the Personal Data Protection Regulations 2013, regulate personal data that is processed and maintained in relation to commercial transactions.

Personal data encompasses information in relation to commercial transactions that relates directly or indirectly to a data subject who is identified or identifiable from that

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25 Part XIII and Sections 99, 100, 101 and 102 of the Trademarks Act 2019.

26 Section 7 of the Copyright Act 1987.

27 Section 37 of the Copyright Act 1987.

28 Section 41 and Part VII of the Copyright Act 1987.

29 Section 60 of the Patents Act 1983.

30 Section 35 of the Industrial Designs Act 1996.

information or other information in the possession of the data user, and includes any expressions of opinion relating to the data subject. 'Data subject' refers to an individual who is the subject of the personal data.

Commercial transactions are defined as any transaction of a commercial nature, whether contractual or otherwise, which includes any matter relating to the supply or exchange of goods or services, agency, investments, financing, banking and insurance. The PDPA applies to the operation of a franchise, as personal information of the franchisor's employees, customers, clients, suppliers and contractors that is collected will be in relation to a commercial transaction.

'Processing', in relation to personal data, means collecting, recording, holding or storing personal data or carrying out any operation or set of operations on personal data, including organisation, adaptation or alteration; retrieval, consultation or use; disclosure by transmission, transfer, dissemination, or otherwise making available; and alignment, combination, correction, erasure or destruction of personal data.

Although the personal data may be processed outside Malaysia, the PDPA will apply to such processing if the personal data is intended to be further processed in Malaysia.<sup>31</sup> Accordingly, the PDPA may also apply to the foreign franchisor as a joint data user if it is involved in and has some form of control over the processing of such data by its Malaysian franchisee.

A data user who belongs to any of the following class of data users as specified in the Schedule to the Personal Data Protection (Class of Data Users) Order 2013 is required to be registered under the PDPA:<sup>32</sup>

- a* communications;
- b* banking and financial institutions;
- c* insurance;
- d* health;
- e* tourism and hospitality;
- f* transportation;
- g* education;
- h* direct selling;
- i* services;
- j* real estate;
- k* utilities;
- l* pawnbroker; and
- m* moneylender.

To process personal data, a data user must comply with the following Personal Data Protection Principles (collectively, the PDP Principles):<sup>33</sup>

- a* General Principle;
- b* Notice and Choice Principle;
- c* Disclosure Principle;
- d* Security Principle;
- e* Retention Principle;

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31 Section 3(2) of the Personal Data Protection Act 2010.

32 Section 14(1) of the Personal Data Protection Act 2010.

33 Section 5(1) of the Personal Data Protection Act 2010.

- f* Data Integrity Principle; and
- g* Access Principle.

The General Principle requires a data user to obtain the consent of its data subjects, which in this case would include the franchisor's employees, customers, clients, suppliers and contractors, prior to processing their personal data.<sup>34</sup> There is no specific form in which the consent must be obtained as long as the consent is capable of being recorded and maintained properly by the franchisor.<sup>35</sup>

Under the Notice and Choice Principle, franchisors must give written notice in Malay and English to the data subjects with the following information when they first collect, or before they use, personal data:<sup>36</sup>

- a* a statement that personal data of the data subject are being processed by or on behalf of the franchisor and a description of the personal data;
- b* the purposes for which the personal data are being or is to be collected and further processed;
- c* the sources of the personal data;
- d* the data subject's right to request access to and correction of the personal data, and how to contact the franchisor with any enquiries or complaints in respect of the personal data (i.e., by providing the designation of the contact person, phone number, fax number (if any), email address (if any) and such other related information);<sup>37</sup>
- e* the class of third parties to whom the franchisor discloses or may disclose the personal data;
- f* the choices and means the franchisor offers the data subject for limiting the processing of personal data;
- g* whether it is obligatory or voluntary for the data subject to supply the personal data; and
- h* where it is obligatory for the data subject to supply the personal data, the consequences for the data subject if he or she fails to supply the personal data.

Under the Disclosure Principle, franchisors are prohibited from disclosing the personal data of their employees, customers, clients, suppliers and contractors for any purpose or to any party other than for the purposes that were made known to the data subjects at the time the personal data were collected, unless further consent is obtained.<sup>38</sup>

The Security Principle requires franchisors to take practical steps to protect personal data from any loss, misuse, modification, unauthorised or accidental access or disclosure, alteration or destruction.<sup>39</sup> Franchisors must develop and implement a security policy that complies with the security standard set out in the Personal Data Protection Standard 2015 (the Standard). If the franchisor engages a third party (data processor) to process the personal

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34 Section 6(1) of the Personal Data Protection Act 2010.

35 Regulation 3(1) of the Personal Data Protection Regulations 2013.

36 Section 7 of the Personal Data Protection Act 2010.

37 Regulation 4 of the Personal Data Protection Regulations 2013.

38 Section 8 of the Personal Data Protection Act 2010.

39 Section 9(1) of the Personal Data Protection Act 2010.

data on its behalf, it must ensure that the data processor provides sufficient guarantees in respect of the technical and organisational security measures governing the processing to be carried out, and takes reasonable steps to ensure compliance with those measures.<sup>40</sup>

Under the Retention Principle, franchisors must not keep personal data longer than is necessary for the fulfilment of the purposes for which they were collected. If the personal data are no longer required, the franchisor must take reasonable steps to ensure that the personal data are permanently deleted.<sup>41</sup> There is no specific retention period or destruction timeline under the PDPA for the storage of personal data and this may be subject to requirements of other legislation, such as employment laws, company laws and tax laws, which may require personal data to be retained for a specific period. The data retention must comply with the Standard.

The Data Integrity Principle requires franchisors to take reasonable steps to ensure that the personal data of their employees, customers, clients, suppliers and contractors are accurate, complete, not misleading and kept up to date, and this must be carried out in accordance with the Standard.

The Access Principle gives data subjects the right to access and correct their personal data where the personal data are inaccurate, incomplete, misleading or not up to date.<sup>42</sup> Franchisors should implement a system that allows their employees, customers, clients, suppliers and contractors controlled access to their personal data for purposes of updating the personal data.

The PDPA allows a data subject to withdraw his or her consent to the processing of personal data by written notice to the data user. Accordingly, data users must, upon receiving such notice, cease processing the personal data. Failure to comply is an offence and, on conviction, the data user is liable to a fine of up to 100,000 ringgit or imprisonment for a term not exceeding one year, or both.<sup>43</sup> In view of the fact that processing includes storage, a request to delete arguably amounts to a withdrawal of consent to process personal data. Therefore, a request to delete must be complied with.

Franchisors are prohibited from transferring any personal data to places outside Malaysia except to places specified by the Minister of Communications and Multimedia and notified in the Gazette or unless it meets one of the conditions set out below:<sup>44</sup>

- a* the data subject has given consent;
- b* the transfer is necessary for the performance of a contract between the data subject and the franchisor;
- c* the transfer is necessary for the conclusion or performance of a contract between the franchisor and a third party that:
  - is entered into at the request of the data subject; or
  - is in the interests of the data subject;
- d* the transfer is for the purpose of any legal proceedings, for obtaining legal advice, or exercising or defending legal rights;
- e* the franchisor has reasonable grounds to believe that in all circumstances of the case:

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40 Section 9(2) of the Personal Data Protection Act 2010.

41 Section 10 of the Personal Data Protection Act 2010.

42 Section 12 of the Personal Data Protection Act 2010.

43 Sections 38(1), 38(2) and 38(4) of the Personal Data Protection Act 2010.

44 Sections 129(1) and 129(3) of the Personal Data Protection Act 2010.

- the transfer is for the avoidance or mitigation of adverse action against the data subject;
  - it is not practicable to obtain the consent in writing of the data subject to that transfer; and
  - if it were practicable to obtain that consent, the data subject would have given his or her consent;
- f* the franchisor has taken all reasonable precautions and exercised due diligence to ensure that the personal data will not, in that place, be processed in any manner that, if that place is Malaysia, would be a contravention of the PDPA;
- g* the transfer is necessary to protect the vital interests of the data subject; and
- h* the transfer is necessary in the public interest.

In addition to obtaining the general consent for the processing of personal data, franchisors should also obtain consent from their employees, customers, clients, suppliers and contractors to transfer the personal data to places outside Malaysia. Alternatively, franchisors may transfer the personal data if they are able to show that they have taken all reasonable precautions and exercised all due diligence to ensure that the personal data of the data subjects will not, in that place outside Malaysia, be processed in any manner that, if that place were Malaysia, would contravene the PDPA. In this connection, data users may consider entering into an agreement with the recipient of the personal data outside Malaysia and conducting regular audits to ensure that the recipient complies with the PDPA.

A data user who transfers personal data outside Malaysia in breach of the PDPA commits an offence that carries a fine of up to 300,000 ringgit or imprisonment of up to two years, or both.<sup>45</sup>

There is no requirement under the PDPA to appoint a designated data protection officer to oversee compliance and administration of the PDPA within the organisation. However, under the Notice and Choice Principle, the written notice must specify how the data subject can contact the data user with any inquiries or complaints in respect of the personal data. For this purpose, franchisors must provide in the written notice at least the designation of the contact person, with phone number and fax number, if any; email address, if any; and such other related information.

In addition to the PDPA, franchisors should generally be aware of other Malaysian legislation that regulates matters relating to cybercrime, e-commerce and social media. In brief:

- a* the Computer Crimes Act 1997 sets out offences relating to the misuse of computers, including unauthorised access to a computer, unauthorised access with intent to commit other crime and also the communication of information, such as passwords, to unauthorised persons;
- b* the Electronic Commerce Act 2006 provides a legal framework for and recognises the use of electronic messages in commercial transactions and the use of such messages to fulfil legal requirements and to enable and facilitate legal transactions; and
- c* the Communications and Multimedia Act 1998 and the Malaysian Content Code regulate the provision of content, including online content, and apply to persons within

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<sup>45</sup> Section 129(5) of the Personal Data Protection Act 2010.

and outside Malaysia if the content is made available in Malaysia. Compliance with the Content Code is generally voluntary unless the Communications and Multimedia Commission issues mandatory compliance directions.

## IV FRANCHISE LAW

### i Legislation

The Act provides a dedicated legislative framework relating to the franchising industry. It provides for the registration of franchises and regulates franchises, including setting out mandatory terms and conditions that have to be contained within a franchise agreement. Contravention of the Act may render a franchise agreement void or expose a franchisor or franchisee to criminal penalties.

Apart from complying with the Act, franchisors and franchisees should also be aware of other relevant legislation such as the Contracts Act 1950, the TMA (and legislation relating to the protection of other IPRs as set out above), the Employment Act 1955 and the Competition Act 2010.

### ii Pre-contractual disclosure

Specific pre-contractual disclosure is covered within the Act and it may also generally fall within the scope of the Contracts Act 1950 and common law.

The Act requires a franchisor to provide disclosure documents to a prospective franchisee at least 10 days before the franchisee signs the franchise agreement.<sup>46</sup> The information required to be disclosed to the franchisee includes:

- a* description of the franchise business;
- b* details of intellectual property rights, fees and payments required from the franchisee;
- c* financial obligations;
- d* whether the franchisee is required to purchase or obtain supplies or materials from a designated source;
- e* territorial rights;
- f* franchise terms, including terms for renewal and termination, obligations upon termination; and
- g* audited accounts of the franchisor's business (at present, the Franchise Registry requires a minimum of the latest three years' audited accounts).

In the event that the information within the disclosure documents is false or misleading, the franchisor may be liable to both criminal and civil action under the Act. It is a criminal offence under the Act to make false statements or omissions that render the information within the disclosure documents misleading.<sup>47</sup>

Section 39 of the Act sets out the applicable penalties if a person is found guilty of an offence under the Act where no express penalties have been specified. Upon conviction, a person will be liable:<sup>48</sup>

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46 Section 15(1) of the Franchise Act 1998.

47 Section 37 of the Franchise Act 1998.

48 Section 39(1)(b) of the Franchise Act 1998.

- a* for the first offence under the Act, to pay a fine of not less than 5,000 ringgit and no more than 25,000 ringgit or to imprisonment of no more than six months; and
- b* for the second or any subsequent offences, a fine of not less than 10,000 ringgit and no more than 50,000 ringgit or imprisonment of no more than one year.

If the alleged offender is a body corporate, it will, upon conviction, attract:<sup>49</sup>

- a* for the first offence under the Act, a fine of not less than 10,000 ringgit and no more than 50,000 ringgit; and
- b* for the second or any subsequent offence, a fine of not less than 20,000 ringgit and no more than 100,000 ringgit.

Further, the court has the power to declare the franchise agreement null and void and may order the franchisor to refund any payments made by the franchisee, and the court may further prohibit the franchisor from entering into any new franchise agreements or from appointing any new franchisees.<sup>50</sup>

In addition to the Act, an aggrieved party may also bring an action for damages for misrepresentation under tort law and, if proven, the court may rescind the franchise agreement. The Contracts Act 1950 also expressly provides for misrepresentation, which potentially renders the contract or agreement voidable at the option of the franchisee.<sup>51</sup>

The franchisor should therefore seek to expressly protect its position within the franchise agreement by ensuring that all projections of profits and revenue and pre-contractual information, where provided to the franchisee pursuant to the disclosure documents under the Act or during the course of negotiations leading to the franchise agreement, do not amount to legally binding representations, guarantees or warranties, to avoid any potential action for misrepresentation or a criminal prosecution under the Act.

### **iii Registration**

There are four categories of registration under the Act, namely registration by:

- a* a local franchisor or master franchisee of a foreign franchisor before offering to sell its franchise to any party;
- b* a foreign franchisor intending to sell its franchise in Malaysia or to Malaysian citizens;
- c* the franchisee of a local franchisor; and
- d* the franchisee of a foreign franchisor.

#### ***Local franchisor or master franchisee***

Section 6 of the Act requires a local franchisor or a master franchisee of a foreign franchisor to register its franchise with the Franchise Registry before operating a franchise business or offering to sell its franchise to any party. A breach of this Section is an offence under the Act and a person will upon conviction, be liable:<sup>52</sup>

- a* for the first offence under the Act, to pay a fine not exceeding 100,000 ringgit or to imprisonment of no more than one year; and

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49 Section 39(1)(a) of the Franchise Act 1998.

50 Section 39(2) of the Franchise Act 1998.

51 Section 19(1) of the Contracts Act 1950.

52 Section 6(2)(b) of the Franchise Act 1998.

- b* for the second or any subsequent offence, to pay a fine not exceeding 250,000 ringgit or to imprisonment of no more than three years.

If the alleged offender is a body corporate, it will, upon conviction, attract:<sup>53</sup>

- a* for the first offence under the Act, a fine not exceeding 250,000 ringgit; and
- b* for the second or any subsequent offence, a fine not exceeding 500,000 ringgit.

The local franchisor is required to submit its application for registration together with all supporting documents, which include the disclosure documents, a sample of the franchise agreement, operation manual, the training manual, its latest audited accounts,<sup>54</sup> financial statements and the auditors' or directors' reports and any other information required by the Registrar.<sup>55</sup>

The Registrar may approve, impose conditions or reject the application, and all such decisions are communicated in writing to the applicant. In the case of an adverse decision, the applicant may submit an appeal to the Minister within one month of the date of communication of the decision. The Minister's decision is final.<sup>56</sup>

### ***Foreign franchisor***

Section 54 (read together with Section 6) of the Act requires a foreign franchisor to apply for prior approval before making an offer to sell its franchise in Malaysia or to any Malaysian citizen. The Registrar may approve, impose conditions on or refuse such an application, and the rights of appeal are set out above.<sup>57</sup>

### ***Franchisee of a local franchisor***

Pursuant to Section 6B of the Act, a franchisee who is granted a franchise by a local franchisor is required to register the franchise with the Registrar within 14 days of the date of signing of the franchise agreement between the franchisor and the franchisee.

### ***Franchisee of a foreign franchisor***

Upon entering into a franchise agreement with a local franchisee and prior to the commencement of operations, the franchisee of a foreign franchisor is required to make an application to register its franchise with the Registrar pursuant to Section 6A of the Act.

## **iv Mandatory clauses**

The Act provides for the inclusion of certain mandatory clauses in a franchise agreement pursuant to Section 18 of the Act, failing which a franchise agreement will be void. Section 18 provides that a franchise agreement will include:

- a* the name and description of the product and business of the franchise;
- b* the territorial rights granted to the franchise;

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53 Section 6(2)(a) of the Franchise Act 1998.

54 The Franchise Registry presently requires a minimum of the latest three years' audited accounts to be submitted in support of such applications.

55 Section 7 of the Franchise Act 1998.

56 Section 17 of the Franchise Act 1998.

57 *ibid.*

- c* the franchise fee, promotion fee, royalties, or any other related payment that may be imposed on the franchisee;
- d* the obligations of both the franchisor and franchisee;
- e* the franchisee's right to use the intellectual properties belonging to the franchisor;
- f* the conditions under which the franchisee may assign the rights given under the franchise;
- g* a statement confirming a cooling-off period of at least seven working days during which the franchisee may terminate the agreement and seek the refund of any franchise fee paid to the franchisor subject to reasonable expenses incurred in the preparation of the franchise agreement that may not be refundable;
- h* a description pertaining to the mark or any other intellectual property owned or related to the franchisor that is used in the franchise;
- i* if the agreement is related to a master franchisee, the franchisor's identity and the rights obtained by the master franchisee from the franchisor;
- j* the type of assistance to be provided by the franchisor to the franchisee;
- k* the duration of the franchise (minimum five years) and the terms of renewal; and
- l* the effect of termination or expiration of the franchise agreement.

Further, the franchisor is required to set up a promotion fund, managed under a separate account, if the franchisee is required to make any payment for the promotion of the franchise.<sup>58</sup>

#### **v Guarantees and protection**

The Act provides for the following written guarantees to be provided by a franchisee:

- a* the franchisee, including its directors, their spouses and immediate family, and its employees must not disclose any information contained in the operation manual or any information obtained while undergoing training organised by the franchisor during the whole of the franchise term and for a period of two years after the expiration of the agreement;<sup>59</sup> and
- b* the franchisee, including its directors, their spouses and immediate family, and its employees must not carry out any other business similar to the franchised business for the whole of the franchise term and for a period of two years after the expiration of the agreement.<sup>60</sup>

Failure to provide the above guarantees amounts to an offence under the Act and the penalties are set out above (see Section IV.ii).

In addition, any written guarantees given by a party will also be enforceable under contract and common law. In the event of failure to provide the guarantees, the franchisor or the aggrieved party may have the option of terminating the agreement and suing for damages for breach of the guarantees given. Alternatively, depending on the nature and extent of the guarantees, the aggrieved party may choose instead to continue with the contractual relationship and claim for damages to put them in such a position as if the guarantees had been performed and fulfilled.

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58 Section 22 of the Franchise Act 1998.

59 Section 26 of the Franchise Act 1998.

60 Section 27 of the Franchise Act 1998.

## V TAX

### i Franchisor tax liabilities

Tax liabilities generally arise in relation to any income derived within Malaysia. For a franchisor, this would include income arising from royalties, financial gains arising from dividends or profits paid. Capital payments, such as lump-sum payments for the grant or acquisition of a franchise, are normally not taxable. 'Capital payment' represents a payment made for the purchase of a capital asset for the enduring benefit of the business of the franchisee. Taxable income is defined within Section 4 of the Income Tax Act 1967.<sup>61</sup>

Different tax rates will apply depending on whether the franchise business is managed and owned through a company (thus attracting corporate tax rates) or if it is being managed as a sole proprietorship (which attracts rates payable by individuals).

Royalty payments and interest arising from within Malaysia and payable to non-residents will be subjected to withholding tax at the rate of 10 per cent and 15 per cent, respectively, and must be paid within one month of paying or crediting the royalty.<sup>62</sup>

Apart from income taxes, the franchisor may also be subject to other general tax liabilities such as stamp duties arising from the execution of the franchise agreement, real property gains tax, excise duty and sales and services tax (SST).

SST was introduced by the Sales Tax Act 2018 and the Services Tax Act 2018, which came into force on 1 September 2018, replacing the current goods and services tax. SST is charged and levied at the rate of between 5 and 10 per cent on taxable goods<sup>63</sup> manufactured in Malaysia by a taxable person and sold, used or disposed of by that taxable person, and on taxable goods imported into Malaysia.<sup>64</sup> Any person who manufactures taxable goods must be registered if the annual turnover has exceeded the 500,000-ringgit threshold.<sup>65</sup> SST is charged and levied at the rate of 6 per cent of the price and value of the taxable services on any taxable services<sup>66</sup> provided in Malaysia by a registered person in carrying on his or her business.<sup>67</sup> Any person specified in the First Schedule of the Service Tax Regulations 2018 providing any taxable service that exceeds the specified threshold for the total value of the taxable service must be registered under the Services Tax Act 2018.<sup>68</sup>

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61 Classes of income on which tax is chargeable pursuant to Section 4 of the Income Tax Act 1976 are gains or profits from a business; gains or profits from an employment; dividends, interest or discounts; rents, royalties or premiums; pensions, annuities or other periodical payment not mentioned and other gains and profits not mentioned under Section 4.

62 Section 109 of the Income Tax Act 1976.

63 'Taxable goods' is defined under Section 2(1) of the Sales Tax Act 2018 as 'goods of a class or kind not exempted from sales tax'.

64 Section 8(1) of the Sales Tax Act 2018 and Order 2 of the Sales Tax (Rates of Tax) Order 2018.

65 Sections 12 and 13 of the Sales Tax Act 2018 and Order 2 of the Sales Tax (Total Sale Value of Taxable Goods) Order 2018.

66 'Taxable services' refer to the services specified in the First Schedule of the Service Tax Regulations 2018.

67 Section 7 of the Service Tax Act 2018 and Order 3 of the Service Tax (Rate of Tax) Order 2018.

68 Sections 12 and 13 of the Service Tax Act 2018.

## ii Franchisee tax liabilities

Franchisees are similarly required to pay tax on taxable income;<sup>69</sup> apart from income tax, the franchisee may also be subject to other general tax liabilities, such as SST as explained above (see Section V.i).

The expenses incurred by a franchisee in undertaking the franchise business – royalty payments, promotion fees, advertising costs, training fees and services fees – are tax deductible. Any franchise fee paid to a foreign franchisor is, however, not tax deductible. Franchise fees paid to a local franchisor, on the other hand, are tax deductible pursuant to the Income Tax (Deduction for Expenditure on Franchise Fee) Rules 2012.

## VI IMPACT OF GENERAL LAW

### i Good faith and guarantees

Section 29(1) of the Act requires both franchisor and franchisee to act in an honest and lawful manner and requires them to endeavour to pursue the best franchise practice of the time and place. However, the Act does not expressly stipulate any penalties for non-compliance. For the aggrieved party to bring an action for the breach of this statutory provision or duty, they must prove that the alleged breach has resulted in actual damage and that the damage was a type contemplated as a foreseeable consequence of the breach.

The Malaysian courts do not recognise any duty of honesty or good faith in a contract where both parties are free to negotiate terms at arm's length. The courts will recognise the principle of freedom of contract and uphold the terms in an agreement unless there are vitiating factors such as coercion, undue influence, misrepresentation or mistake. This was recently confirmed in *Aseambankers Malaysia Berhad & Ors v. Shencourt Sdn Bhd & Anor*<sup>70</sup> and was subsequently adopted in *SCOMI Transit Projects Sdn Bhd v. Prasarana Malaysia Berhad*.<sup>71</sup> In *Aseambankers*, the court held that if it were to allow the defendant's counterclaim on the grounds that there is a general duty of good faith, the court would effectively be creating new law.

### ii Agency distributor model

Section 29(3) of the Act requires the franchisee to operate its business separately from the franchisor and specifies that the relationship between the franchisee and the franchisor will not at any time be regarded as a partnership, service contract or agency. Thus, the agency model has no role to play in a franchise system in Malaysia. A franchisee may, however, distribute a franchisor's products as this is not prohibited under the Act, and such an arrangement may be subject to a separate distribution agreement.

### iii Employment law

The Employment Act 1955 applies to employees whose wages do not exceed 2,000 ringgit a month and to all manual labourers (irrespective of wages).<sup>72</sup> All other employees are governed by their employment contracts and common law principles developed through case

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69 *ibid.* at 63 and 66.

70 [2014] 4 MLJ 619.

71 [2016] MLJU 622.

72 Section 2(1) of the Employment Act 1955.

law. Given the express provision within the Act that franchises are not regarded as service contracts, there will be no presumption of an employer–employee relationship between a franchisor and a franchisee.

#### **iv Consumer protection**

Franchisees are not treated as consumers under existing laws in Malaysia or pursuant to the Consumer Protection Act 1999, which principally governs consumer rights and protection.

#### **v Competition law**

Franchise agreements commonly incorporate provisions that restrict or prevent competition; for instance, selective or exclusive distribution provisions and restrictions on the use of IPRs licensed under the franchise agreement. These provisions are permissible if they can be justified as proportionate and can be shown to be necessary to safeguard the goodwill that has been built up into a brand by the franchisor.

The Competition Act 2010 expressly prohibits anticompetitive agreements, which include horizontal and vertical agreements, between enterprises that have the object or effect of significantly preventing, restricting or distorting competition in any market for goods or services.<sup>73</sup> The franchise agreement, being a form of vertical agreement, is prohibited if it has an anticompetitive object or effect that is significant in the relevant market unless:

- a* the parties to the agreement are competitors who are in the same market and their combined market share does not amount to more than 20 per cent; or
- b* the parties to the agreement are not competitors and, individually, each party has less than 25 per cent of shares in any relevant market.<sup>74</sup>

The Competition Commission of Malaysia (MyCC) will generally take a strong stance against resale price maintenance and will deem any form of maximum pricing or recommended retail pricing that serves as a focal point for price determination to be anticompetitive.<sup>75</sup>

As the Competition Act 2010 has only come into force relatively recently, MyCC has, as yet, not issued any guidelines to address the competing tensions between the IPRs or franchise agreements on the one hand and free competition on the other. Resale price maintenance is one area of potential conflict. If a recommended price sought to be provided in a franchise agreement is a genuine recommendation and does not become a focal point for price determination, it is likely that it will be permitted.

#### **vi Restrictive covenants**

Non-compete clauses and restrictive covenants are generally upheld as contractual terms and enforceable for the duration of the agreement. Breach of these covenants entitles the aggrieved party to sue for damages and specific reliefs and may also form the grounds of a complaint to the Franchise Registry. Breach of restrictive covenants set out in the Act is tantamount to an offence under the Act.<sup>76</sup>

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73 Section 4 of the Competition Act 2010.

74 Guidelines on Chapter 1 Prohibition: Anti-competitive Agreements (2012) by the MyCC; see [https://www.myc.gov.my/sites/default/files/pdf/newsroom/MYCC-4-Guidelines-Booklet-BOOK1-10-FA-copy\\_chapter-1-prohibition001\\_1.pdf](https://www.myc.gov.my/sites/default/files/pdf/newsroom/MYCC-4-Guidelines-Booklet-BOOK1-10-FA-copy_chapter-1-prohibition001_1.pdf).

75 *ibid.*

76 Section 27 of the Franchise Act 1998.

### **vii Termination**

When introduced in 1998, the Act prohibited only the franchisee from terminating a franchise agreement before expiration of the franchise term. Following amendments made in 2012, a similar a similar prohibition now applies to franchisors.<sup>77</sup>

In any event, either party may not terminate a franchise agreement before the expiration date except for good cause as stipulated in the Act. 'Good cause' is defined to include failure of the franchisee or franchisor to comply with the terms of the franchise agreement or any other relevant agreement between the parties and their failure to remedy the breach within a specified period, which may not be less than 14 days.<sup>78</sup>

Termination without the requirement of notice and the opportunity to remedy the breach is also permissible in certain specified circumstances such as bankruptcy or insolvency, voluntary abandonment of franchised business, assignment of franchise rights for the benefit of creditors or a similar disposition of the assets to any other persons, conviction of a criminal offence that substantially impairs the goodwill associated with the franchisor's mark or other IPRs, and repeated failure to comply with the terms of the agreement.<sup>79</sup>

Non-compete clauses are expressly permitted under the Act for a period of two years post-termination of the franchise<sup>80</sup> and they form an exception to contract law principles, which generally hold a restraint of trade clause post-contract as void.<sup>81</sup>

Apart from pursuing a civil action for a breach, the covenant may also be enforced by the franchisor by lodging a complaint with the Franchise Registrar, and this may potentially lead to a criminal prosecution.<sup>82</sup>

Nothing in the Act prevents the franchisor from taking over the franchise business granted to the franchisee upon termination of the franchise term; however, in a non-renewal of the franchise agreement, the franchisor is under an obligation to compensate the franchisee either by a repurchase or other means of compensation at a price agreed between the franchisor and franchisee in consideration of the diminution in value of the franchised business caused by the expiration of the franchise where:

- a the franchisee is barred by the franchise agreement or by the refusal of the franchisor to waive any portion of the franchise agreement that prohibits the franchisee from continuing with the business; or
- b the franchisee has not been given written notice of the franchisor's intent not to renew the agreement at least six months prior to the expiration date.<sup>83</sup>

### **viii Anti-corruption and anti-terrorism regulation**

The Anti-Money Laundering and Anti-Terrorism Financing Act 2001 (AMLA) is the primary legislative framework combating money laundering and terrorist financing. The AMLA not only criminalises money laundering and financing of terrorism, but also imposes various obligations on reporting institutions. Any person who engages in, or attempts to engage in or abets the commission of money laundering, commits an offence under the AMLA.

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77 Section 19 of the Franchise (Amendment) Act 2012 and Section 31 of the Franchise Act 1998.

78 Section 31(2) of the Franchise Act 1998.

79 Section 31(3) of the Franchise Act 1998.

80 Section 27 of the Franchise Act 1998.

81 Section 28 of the Contracts Act 1950.

82 Section 27(3) of the Franchise Act 1998.

83 Section 32 of the Franchise Act 1998.

Anti-corruption is governed by the Malaysian Anti-Corruption Commission Act 2009, which was enacted to provide for the establishment of the Malaysian Anti-Corruption Commission and to make further and better provision for the prevention of corruption.

In addition, in the absence of any specific legislation, regard must also be had to the Malaysian Penal Code, which covers fraudulent and dishonest acts such as criminal breach of trust,<sup>84</sup> cheating<sup>85</sup> and criminal misappropriation of property.<sup>86</sup>

## **ix Dispute resolution**

Litigation can be an expensive, lengthy and complex process especially where foreign law is applied within a franchise agreement. Civil proceedings may be initiated in the Sessions or High Court depending on the proposed cause of action and quantum of damages sought.

It is a usual practice for parties, particularly where a foreign party is involved, to include a law and jurisdiction clause within their franchise agreement. Generally, the local courts will recognise and uphold a choice of foreign law or jurisdiction clause; however, the choice of foreign law may only cover the interpretation of the terms and conditions of the franchise agreement and may not exclude compliance with other Malaysian laws, such as the Act, which may still continue to apply and which may, in some instances take precedence over the terms of the franchise agreement.

Parties may also opt for arbitration or mediation as the preferred method of resolving disputes. Arbitration is governed by the Arbitration Act 2005 and mediation is governed by the Mediation Act 2012. Mediation is, however, not a mandatory form of alternate dispute resolution and there are no costs or other penalties that can or may be imposed if a party refuses to pursue mediation and decides instead to initiate a court action.

Parties are generally encouraged by the Franchise Registry to resolve disputes informally, through good faith negotiations or mediation. The Franchise Registry may, at the request of the parties, act as a mediator. Mediation is, however, not a mandatory form of dispute resolution.

Where informal dispute resolution mechanisms fail, the court process remains the primary means of enforcement.

Injunctive relief, both interim and permanent, is available to restrain the infringement of any IPRs or a breach of a restraint of trade covenant.

Where a contract is breached, the injured party is entitled to initiate a civil action for damages. Calculation of damages in a breach of contract action (including misrepresentation) depends on whether the injured party is claiming for expectation loss or reliance loss. Expectation loss aims to put the injured party in such a position as if the contract had been fully performed and where the injured party would have made certain profits or earnings; any such losses will have to be proven on a standard of balance of probabilities. If the injured party is claiming for reliance loss, the injured party must prove the expenses incurred arising from his or her reliance on the contract. In any event, the loss must not be too remote such that it must arise as a natural consequence of the breach or the parties must be aware of the loss.<sup>87</sup>

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84 Sections 405-409 of the Malaysian Penal Code.

85 Sections 415-424 of the Malaysian Penal Code.

86 Sections 403-404 of the Malaysian Penal Code.

87 Section 74 of the Contracts Act 1950.

Under the Contracts Act 1950, the parties must also restore or compensate for any advantage received where the injured party rescinds a contract that is void or has become voidable as a consequence of the breach.<sup>88</sup> The Contracts Act 1950 also requires that an injured party takes all reasonable steps to mitigate the loss and must not incur unreasonable expenses in the act of doing so.<sup>89</sup>

An injured party may also seek to pursue a claim under tort. Damages under tort are calculated to place the claimant in such a position as if the breach or tort had not taken place. They are generally quantified under two headings, namely general and special damages.

To successfully recover any damages, a claimant must prove on a balance of probabilities that the losses were caused by the defendant's actions or breach and there has been no break in the chain of causation leading to the losses suffered. Losses that are too remote are not recoverable.

Litigation costs usually follow the event and are awarded to the successful party. There are no capped costs and in the absence of agreement between parties, the quantum of costs will be determined by the court through taxation proceedings.

The registration and enforcement of foreign court judgments is governed by the Reciprocal Enforcement of Judgments Act 1958 (REJA). REJA is limited to final judgments<sup>90</sup> awarded by a superior court from a country listed in its First Schedule, and they are Brunei, Hong Kong, India, New Zealand, Singapore, Sri Lanka and the United Kingdom. If the foreign judgment is from another jurisdiction, the only method of enforcement would be to initiate fresh proceedings and secure a Malaysian court judgment.

Malaysia is a signatory to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention) and therefore Malaysian courts will recognise foreign arbitral awards made in a New York Convention contracting state unless any of the grounds for refusal of recognition stated under Section 39(1) of the Arbitration Act 2005 are successfully established.

## VII CURRENT DEVELOPMENTS

### i Amendments to the Act

Malaysia has introduced various amendments to the Act via the Franchise (Amendment) Act 2020 (the Amending Act) to ensure conformity with current developments in franchise business in Malaysia. The Amending Act was published in the Gazette on 6 March 2020 after receiving royal assent on 20 February 2020. It has yet to come into force but is anticipated to do so at the end of this year or early next year.

One of the major changes under the Amending Act is the new requirement under Section 6 of the Act for a foreign franchisor to register its franchise separately after obtaining the Registrar of Franchise's approval to sell its franchise in Malaysia or to a Malaysian citizen pursuant to Section 54 of the Act (at present this requirement only applies to local franchisors). This requirement was introduced by extending the scope of application of Section 6 of the Act to foreign franchisors. It is relevant to note that the additional registration requirement

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88 Section 66 of the Contracts Act 1950.

89 Explanation to Section 74 of the Contracts Act 1950.

90 Section 2 of the Reciprocal Enforcement of Judgments Act 1958. Judgments capable of registration are judgments or orders given or made by a court in any civil or criminal proceedings for the payment of a sum of money in respect of compensation or damages.

for foreign franchisors gives effect to the High Court's judgment in *Dr HK Fong BrainBuilder Pte Ltd v. SG-Maths Sdn Bhd & Ors*,<sup>91</sup> which gave Section 6(1) of the Act a more liberal interpretation, requiring foreign franchisors to be subject to the same registration requirements as local franchisors, to promote fairness and consistency in the regulation of local and foreign franchises. To enable a smooth transition to the new Act, the Amending Act allows all foreign franchisors who had previously obtained the Registrar's approval under Section 54 of the Act to be automatically registered under Section 6 of the Act. It is anticipated that the Registrar may provide partial exemptions for foreign franchisors in respect of the Section 6 application given that the information required for the Section 6 application is almost identical to that for the Section 54 application. The only difference is that the Section 6 application requires additional information and documents such as training manuals, operational manuals and the franchisee's profit and loss projection.

Because of the expansion of the scope of Section 6, foreign franchisors are likely to be bound by the post-registration obligations under the Act (which currently only apply to local franchisors), namely the pre-contractual disclosure of the franchise agreement and supporting documents approved by the Registrar, including the amendments thereto,<sup>92</sup> the submission of the annual report within six months of the end of the financial year of the franchise business<sup>93</sup> and the submission of the financial statement of the promotion fund, endorsed by a registered public accountant within 30 days of the conclusion of the most recent financial term.<sup>94</sup> This amendment should serve as a wake-up call for foreign franchisors to take steps to comply with the post-registration obligations.

Under the Amending Act, a franchise registration will have a prescribed period of validity. A franchisor may apply to the Registrar to renew its registration within 30 days of the expiry date upon payment of the prescribed renewal fee. The approval is subject to terms and conditions imposed by the Registrar. The period of validity and renewal fee have yet to be made known.

Following the amendments, a franchisor or a franchisee will be required to display the franchise registrations (i.e., certificate of registration) in a conspicuous position at the place where the franchisor or franchisee carries on its business.

The Amending Act also explicitly requires terms of extension to be included in a franchise agreement. It follows that franchisors are required to provide a separate extension term, which is usually shorter than a renewal term, for franchisees to recoup on their investments. However, this amendment is unlikely to affect franchises registered prior to the Amending Act as it has always been the Registrar's practice to require terms of extension to be provided in a franchise agreement.

The Amending Act extends the requirement to obtain the Registrar's approval for material changes to the supporting documents for franchise registration, to franchise agreements, operation manuals and training manuals. Similarly, in view of the Registrar's current practice, this amendment is unlikely to affect franchises registered prior to the Amending Act.

Pursuant to the Amending Act, non-registration of franchisees (namely franchisees of a foreign franchisor and franchisees of a local franchisor or local master franchisee) will be

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91 *Dr HK Fong BrainBuilder Pte Ltd v. SG-Maths Sdn Bhd & Ors* [2018] 11 MLJ 701.

92 Section 15 of the Act.

93 Section 16 of the Act.

94 Section 22 of the Act.

made an offence under the Act. Therefore, it is important for franchisees to register their franchises after execution of the franchise agreement but before the commencement of business operations to avoid being penalised under the Act.

**ii Dr H K Fong Brainbuilder Pte Ltd v. SG-Maths Sdn Bhd & Ors [2020] MLJU 1211 (CA)**

This was an appeal by the plaintiff against the decision of the High Court in dismissing its claims, among others, that (1) the first defendant had breached the master licence agreement by granting a sub-licence to a third party; (2) the second and third defendants (who were the shareholders and the only directors of the first plaintiff) were liable to the plaintiff under the guarantee for the first defendant's breaches of the agreement; and (3) the fifth and sixth defendants (which were set up by the second and third defendants) had wrongfully utilised the plaintiff's confidential information, and the defendants' counterclaim for, among other things, a declaration of the invalidity of the agreement and the guarantee and a refund of all money paid to the plaintiff.

The Court of Appeal agreed with the High Court in finding the master licence agreement to be a franchise as it satisfied all the elements required under Section 4 the Act.

In determining whether Section 6(1) of the Act applies to foreign franchisors, the Court of Appeal further agreed with the purposive approach adopted by the High Court in interpreting Section 6(1), together with the wide definition of 'franchisor' under Section 4 of the Act that Section 6(1) should apply to all franchisors, both local and foreign. It was acknowledged that if Section 6(1) were to apply only to local franchisors as submitted by the plaintiff, it would create an absurdity whereby local franchisors would have to register their franchises under Section 6(1) while foreign franchisors remained exempt from this requirement (in the absence of the Minister exercising power to grant the local franchisor exemption), and would cause injustice to franchisees of foreign franchisors, who, through non-registration under Section 6(1), might wriggle out of compliance with mandatory provisions intended for the protection of their franchisees. Therefore, the Court of Appeal upheld the High Court's decision that non-registration by the plaintiff under Section 6(1) amounted to a contravention of the Act.

Further, it was held that the High Court did not err in holding that non-registration rendered the agreement void, as it is forbidden by the Act or is of such a nature that, if permitted, would defeat the Act within the meaning of Section 24(a) or 24(b), or both, of the Contracts Act 1950. As a result, the agreement together with the guarantee and the power of attorney, which together constitute a single composite transaction, were declared void in their entirety.

It is noteworthy that the Court of Appeal's decision serves as a renewed reminder to all franchisors and franchisees of the importance of abiding by the registration requirements under the Act. Be that as it may, the Court of Appeal again failed to consider Section 54 of the Act, which applies specifically to foreign franchisors, who are required to obtain the Registrar of Franchise's approval for the sale of franchises in Malaysia or to any Malaysian citizen.

**iii Proposed amendments to the PDPA**

On 14 February 2020, the Malaysian Personal Data Protection Commissioner released the much anticipated proposed amendments to the PDPA for public consultation, which closed on 10 March 2020. The proposed amendments are aimed at strengthening the effectiveness and practical implementation of the PDPA while aligning it to the European Union's General Data Protection Regulation. The proposed amendments are set out briefly below:

- a* imposing direct obligations and responsibilities on data processors;
- b* introducing the right of data portability for data subjects;
- c* requiring data users to appoint a data protection officer;
- d* introducing a data breach notification requirement;
- e* providing clarity on the consent requirement;
- f* providing clarity on the conditions for transferring personal data to places outside Malaysia;
- g* requiring data users to implement privacy by design;
- h* introducing a do-not-call registry;
- i* introducing the right for data subjects to know which third parties personal data is disclosed to;
- j* introducing the right for data subjects to take civil action against a data user who breaches the PDPA;
- k* addressing privacy issues arising from data collection endpoints;
- l* extending the application of the PDPA to the Malaysian government;
- m* addressing cross-border data transfer for data users with entities located outside Malaysia;
- n* clarifying the status of business contact information;
- o* providing clarity on the disclosure of personal data to government regulatory agencies;
- p* reclassifying data users on the basis of business activity;
- q* introducing voluntary registration by data users;
- r* extending the application of the PDPA to non-commercial transactions;
- s* extending the application of the PDPA to data users outside Malaysia who monitor and actively profile Malaysians;
- t* addressing digital and electronic marketing including mechanisms to unsubscribe from online services;
- u* addressing direct marketing with permission for data users to make the first direct marketing call to data subject with an option to opt out; and
- v* addressing processing of personal data in cloud computing.

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