



# Franchise

in 33 jurisdictions worldwide

Contributing editor: Philip F Zeidman

# 2010



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<b>Introduction</b> Philip F Zeidman <i>DLA Piper LLP (US)</i>	<b>3</b>
<b>Australia</b> John Sier and Philip Colman <i>Mason Sier Turnbull</i>	<b>5</b>
<b>Austria</b> Sylvia Freygnier and Dzemila Beganovic <i>Freygnier Rechtsanwälte GmbH</i>	<b>12</b>
<b>Belgium</b> Jan Ravelingien <i>Marx Van Ranst Vermeersch &amp; Partners</i>	<b>18</b>
<b>Canada</b> Bruno Floriani and Marvin Liebman <i>Lapointe Rosenstein LLP</i>	<b>25</b>
<b>China</b> Janet Jie Tang and Ning Lu <i>Akin Gump Strauss Hauer &amp; Feld LLP</i>	<b>33</b>
<b>Cyprus</b> Yiannos G Georgiades and Rebecca E Howarth <i>Georgiades &amp; Mylonas, Advocates &amp; Legal Consultants</i>	<b>40</b>
<b>El Salvador</b> José Roberto Romero <i>Romero Pineda &amp; Asociados</i>	<b>45</b>
<b>Finland</b> Hanna-Maija Elo <i>Attorneys-at-Law Juridia Ltd</i>	<b>50</b>
<b>France</b> Emmanuel Schulte <i>Bersay &amp; Associés</i>	<b>55</b>
<b>Germany</b> Karsten Metzlauff <i>Nörr Stiefenhofer Lutz Partnerschaft</i>	<b>61</b>
<b>Greece</b> Andreas Bagias <i>Andreas Bagias Law Office</i>	<b>67</b>
<b>Guatemala</b> Marco Antonio Palacios López <i>Palacios &amp; Asociados</i>	<b>72</b>
<b>Hungary</b> Peter Lukácsi <i>SBG &amp; K Patent and Law Offices</i>	<b>77</b>
<b>India</b> Manish Kumar Sharma <i>FoxMandal Little</i>	<b>82</b>
<b>Indonesia</b> Galinar R Kartakusuma <i>Makarim &amp; Taira S</i>	<b>88</b>
<b>Italy</b> Roberto Pera <i>Rödl &amp; Partner</i>	<b>94</b>
<b>Japan</b> Etsuko Hara <i>Anderson Mōri &amp; Tomotsune</i>	<b>101</b>
<b>Korea</b> Jae Hoon Kim and Sun Chang <i>Lee &amp; Ko</i>	<b>107</b>
<b>Kuwait</b> Sam Habbas and David Walker <i>Al Sarraf &amp; Al Ruwayeh (in association with Stephenson Harwood)</i>	<b>115</b>
<b>Luxembourg</b> Claude Geiben and Marie-Eve Delpech <i>Schaeffer Hengel Geiben &amp; Associés</i>	<b>121</b>
<b>Malaysia</b> Jin Nee Wong <i>Wong Jin Nee &amp; Teo</i>	<b>126</b>
<b>Mexico</b> Jorge Mondragón and Miguel Valle <i>González Calvillo, SC</i>	<b>133</b>
<b>New Zealand</b> Stewart Germann <i>Stewart Germann Law Office</i>	<b>139</b>
<b>Romania</b> Adrian Roseti and Andra Filatov <i>Drakopoulos Law Firm</i>	<b>144</b>
<b>Russia</b> Elena Frolovskaya and Natalya Babenkova <i>Nörr Stiefenhofer Lutz OOO</i>	<b>150</b>
<b>South Africa</b> Eugene Honey <i>Bowman Gilfillan Inc</i>	<b>157</b>
<b>Spain</b> Rocío Belda de Mergelina and Roldán García Pereda <i>Garrigues</i>	<b>164</b>
<b>Sweden</b> Peter Orander and Mikael von Schedvin <i>Advokatfirma Lindhs DLA Nordic</i>	<b>171</b>
<b>Switzerland</b> Walter H Boss and Thomas G Albert <i>Poledna Boss Kurer AG</i>	<b>178</b>
<b>Thailand</b> Chanvitaya Suvarnapunya and Athistha Chitranukroh <i>DLA Piper (Thailand) Limited</i>	<b>183</b>
<b>United Kingdom</b> Andrew Johnston and Andrew Chandler <i>Eversheds LLP</i>	<b>188</b>
<b>United States</b> Michael G Brennan and Philip F Zeidman <i>DLA Piper LLP (US)</i>	<b>194</b>
<b>Venezuela</b> Rafael de Lemos, Andres Halvorssen and Andrea Rondón <i>Raffalli de Lemos Halvorssen Ortega y Ortiz</i>	<b>203</b>

# New Zealand

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### Overview

#### 1 What forms of business entities are relevant to the typical franchisor?

Most franchisors conduct business in New Zealand by way of an incorporated company. Sole traders and partnerships are used and occasionally a franchisor may be a trading trust. Joint ventures are uncommon in New Zealand. The relevant agency is the Ministry of Commerce.

#### 2 What laws and agencies govern the formation of business entities?

The Companies Act 1993 applies to all companies incorporated in New Zealand. It also applies to a company with overseas shareholding. It does not apply to a company incorporated in another country. If a trading trust is used, the Trustee Act 1956 would apply.

#### 3 Provide an overview of the requirements for forming and maintaining a business entity.

A new company can be incorporated online and the relevant website is at [www.companies.govt.nz](http://www.companies.govt.nz). The first step is to obtain name approval. Then an application to incorporate must be completed naming all of the directors and shareholders of the company who must sign written consents both to act as directors and to become shareholders. An address of the registered office of the company and an address for service must be provided and both must be New Zealand addresses.

Please note that all new companies must be incorporated online and the fee is NZ\$160. Once an overseas shareholder holds 25 per cent or more of the shares of the company then a company must file financial accounts and be audited. Otherwise, if the shareholders pass a unanimous resolution that no auditor need be appointed then the company does not have to be audited. The Financial Reporting Act 1993 applies to all companies. Also, when incorporating a new company it is wise to have a separate constitution (also known overseas as articles of association) otherwise the provisions in the Companies Act 1993 will apply. For example, any pre-emptive rights will only exist by way of a separate constitution and not in reliance upon the Companies Act 1993.

#### 4 What restrictions apply to foreign business entities and foreign investment?

If a foreign business entity holds 25 per cent or more of the shareholding in a company then the company must be audited and must file financial statements pursuant to the Financial Reporting Act 1993. In relation to foreign investment, there are no barriers for funds coming into New Zealand. If a foreign entity wishes to buy land in New Zealand, if the land is greater than five hectares in area, application to the relevant government agency must be made for consent to purchase.

#### 5 Briefly describe the aspects of the tax system relevant to franchisors. How are foreign businesses and individuals taxed?

The corporate tax rate for both resident and non-resident companies is 30 per cent. New Zealand has tax treaties with many countries, for example, Australia, the UK and the US, where non-resident withholding tax at 10 per cent must be deducted from all interest and royalty income before funds are repatriated. The overseas entity will be able to claim a tax deduction in the relevant country because a non-resident withholding tax certificate will be provided. If dividends are repatriated, non-resident withholding tax at 15 per cent must be deducted.

#### 6 Are there any relevant labour and employment considerations for typical franchisors? What is the risk that a franchisee or employees of a franchisee could be deemed employees of the franchisor? What can be done to reduce this risk?

The Employment Relations Act 2000 applies in New Zealand. Membership of unions is voluntary but there must be a written employment contract in relation to every employee. Strict procedures must be followed before employment can be terminated and if the procedures are breached, this would give rise to a personal grievance action which may cost the employer many thousands of dollars. There is no risk that a franchisee or employees of a franchisee could be deemed employees of a franchisor so nothing needs to be done to reduce that risk.

#### 7 How are trademarks and know-how protected?

The Trademarks Act 2002 is the relevant statute and all trademarks must be registered in New Zealand. The relevant body to deal with is the Intellectual Property Office of New Zealand (IPONZ) and its website is at [www.iponz.govt.nz](http://www.iponz.govt.nz). Trademark registrations last for 10 years and then must be renewed. Know-how is protected by normal intellectual property laws and would be deemed to be included in what are called trade secrets.

#### 8 What are the relevant aspects of the real estate market and real estate law?

All real estate in New Zealand is recorded by Land Information New Zealand (LINZ), which provides a registered title for each piece of land. Titles can be freehold, leasehold, strata, cross-lease or some combination. An overseas franchisor can own land subject to discussion in question 4. Franchisors can lease commercial buildings without restriction. If real estate agents are engaged, they must comply with the Real Estate Agents Act 1976. Franchisors who request real estate agents to find them premises will have to pay commission to the relevant agents. There is a new Real Estate Agents Act 2008 which comes into force on 1 October 2009. The Property Law Act 2007 is also relevant in relation to real estate and must be consulted.

Laws and agencies that regulate the offer and sale of franchises

9 What is the legal definition of a franchise?

There is no franchise-specific legislation in New Zealand so there is no legal definition of a franchise.

However, the Franchise Association of New Zealand Incorporated (FANZ) was formed in July 1996 and all members must comply with the Code of Practice. This Code of Practice, in section 2.1, defines a 'franchise' as meaning a business operated as a franchise, and that term is further defined in the rules. The rules of the FANZ contain the following definition for franchise:

*Franchise means the method of conducting business under which the right to engage in the offering, selling or distributing of goods or services within New Zealand includes or is subject to at least the following features:*

- *the grant by a Franchisor to a Franchisee of the right to the use of a Mark, in such a manner that the business carried on by the Franchisee is or is capable of being identified by the public as being substantially associated with a Mark identifying, commonly connected with or controlled by the Franchisor; and*
- *the requirement that the Franchisee conducts the business, or that part of the business subject to the Franchise Agreement, in accordance with the marketing, business or technical plan or system specified by the Franchisor; and*
- *the provision by the Franchisor of ongoing marketing, business or technical assistance during the term of the Franchise Agreement.*

10 Which laws and government agencies regulate the offer and sale of franchises?

No government agencies regulate the offer and sale of franchises. However, there are a number of laws that must be complied with including the Commerce Act 1986 and the Fair Trading Act 1986. If a broker is used by a franchisor to assist with the sale of franchises, the discussion in question 8 will be relevant.

As mentioned in question 9, there is no franchise-specific legislation in New Zealand so there is no legal definition of a franchise. In 2008 the government published a discussion document with a view to seeing whether franchise legislation should be introduced. However, on 11 June 2009 the Honourable Simon Power, minister of justice, announced that in the opinion of the government:

*I do not believe that there is a need for the introduction of franchise-specific regulation at this time. There is little evidence of widespread problems within the sector and it is difficult to argue that franchising is unique enough from other types of businesses or contracts to necessitate specific regulation. There is also insufficient evidence to indicate that current processes are inadequate to address any issues and it is unclear that regulation would be the answer to any perceived problems.*

11 Describe the relevant requirements of these laws and agencies.

The Commerce Act 1986 is concerned with anti-competitive behaviour and restrictive trade practices. The Fair Trading Act 1986 is concerned with representations made by any party that amount to misrepresentations, which may be innocent, negligent or fraudulent. There are monetary penalties in relation to breaches of both Acts.

12 What are the exemptions and exclusions from any franchise laws and regulations?

Not applicable.

13 Does any law or regulation create a requirement that must be met before a franchisor may offer franchises?

There is no law in New Zealand which would create such a requirement.

14 In the case of a sub-franchising structure, who must make pre-sale disclosures to sub-franchisees? If the sub-franchisor must provide disclosure, what must be disclosed concerning the franchisor and the contractual or other relationship between the franchisor and the sub-franchisor?

Legally, the answer to the question is that none is required. However, if a franchisor belongs to the FANZ, it must comply with the Code of Practice and publish a disclosure document. A sub-franchisor would have to provide a disclosure document to a potential sub-franchisee if that sub-franchisor was a member of the FANZ.

15 What is the compliance procedure for making pre-contractual disclosure in your country? How often must the disclosures be updated?

Again, there are no franchising laws requiring pre-contractual disclosure but great care must be taken to ensure that all representations are true and do not amount to misrepresentations which will fall foul of the Fair Trading Act 1986. A member of the FANZ must provide a potential franchisee with its disclosure document at least 14 days before the franchise agreement is executed and the disclosure document must be updated annually by the franchisor.

16 What information must the disclosure document contain?

The disclosure document must provide:

- details of the franchisor and its directors including experience, a viability statement with key financial information of the franchisor;
- details of any bankruptcies, receiverships, liquidations or materially relevant debt recovery;
- criminal, civil or administrative proceedings within the past five years;
- a summary of the main particulars and features of the franchise;
- a list of components making up the franchise purchase;
- details of any financial requirements by the franchisor of the franchisee; and
- other information listed in the code.

17 How do the relevant government agencies enforce the disclosure requirements?

There is no enforcement by government agencies in relation to disclosure requirements. However, please note what has been stated in question 10. If a franchisor is a member of the FANZ and it does not comply with the Code of Practice in relation to disclosure requirements, that franchisor can be ousted from the FANZ. If any franchisee suffers a loss at the hands of such a franchisor then the franchisee's remedies would be according to normal contractual laws and the franchisor would be vulnerable from an action for damages by the franchisee. As stated above, if there are any misrepresentations, the person suffering a loss may make a complaint to the Fair Trading Division of the Commerce Commission pursuant to the Fair Trading Act 1986.

**18** What actions can franchisees take to obtain relief for violations of disclosure requirements? What are the legal remedies for such violations? How are damages calculated? If the franchisee can cancel or rescind the franchise contract, is the franchisee also entitled to reimbursement or damages?

Franchisees could make an official complaint to the Fair Trading Commission if information contained in any disclosure document was false or misleading. Furthermore, a franchisee could sue the franchisor for misleading conduct pursuant to the Fair Trading Act 1986. Damages are normally calculated from the date of loss. A franchisee may be entitled to cancel or rescind the franchise agreement pursuant to the Contractual Remedies Act 1979 and may be entitled to reimbursement or damages, or both.

**19** In the case of sub-franchising, how is liability for disclosure violations shared between franchisor and sub-franchisor? Are individual officers, directors and employees of the franchisor or the sub-franchisor exposed to liability? If so, what liability?

If a sub-franchisor misrepresented the position without recourse to a franchisor, the franchisor should not be liable in any way. If a representation is made by a director or employee of the franchisor or the sub-franchisor, the protection of a limited liability company would not protect that individual, who would be personally liable pursuant to New Zealand legislation.

**20** In addition to any laws or government agencies that specifically regulate offering and selling franchises, what are the general principles of law that affect the offer and sale of franchises? What other regulations or government agencies or industry codes of conduct may affect the offer and sale of franchises?

The answer to the first question is not applicable. The answer to the second question is not applicable except if the franchisor was a member of the FANZ in which case both the Code of Practice and the Code of Ethics would apply.

**21** What other actions may franchisees take if a franchisor engages in fraudulent or deceptive practices in connection with the offer and sale of franchises? How does this protection differ from the protection provided under the franchise sales disclosure laws?

Franchisees could make a complaint to the Commerce Commission and request an investigation in relation to such activity. Such protection differs in that there is fraudulent or deceptive conduct that should not occur in relation to franchise sales. Also, such franchisees could bring a civil action against the franchisor and it may be possible to join the directors of the franchisor company as separate defendants as they could be personally liable for damages if the franchisor company had no assets. This protection does not differ from the protection provided pursuant to existing civil laws in New Zealand.

Legal restrictions on the terms of franchise contracts and the relationship between parties involved in a franchise relationship

**22** Are there specific laws regulating the ongoing relationship between franchisor and franchisee after the franchise contract comes into effect?

There are no specific laws regulating the ongoing relationship between franchisor and franchisee after the franchise contract comes into effect.

**23** Do other laws affect the franchise relationship?

There are no other laws affecting the franchise relationship in New Zealand.

**24** Do other government or trade association policies affect the franchise relationship?

There are no other government or trade association policies affecting the franchise relationship.

**25** In what circumstances may a franchisor terminate a franchise relationship? What are the specific legal restrictions on a franchisor's ability to terminate a franchise relationship?

Any events of termination must be specified in the franchise agreement. There must be some fault or misdemeanour on the part of the franchisee for a valid termination to be confirmed. If a termination is unlawful, a franchisor would be able to seek redress from a court with the remedies being either damages or an order from the court that the franchise be reinstated to the franchisee which may continue to conduct business pursuant to the franchise agreement.

**26** In what circumstances may a franchisee terminate a franchise relationship?

A franchisee may terminate a franchise relationship only if the franchisor has engaged in misrepresentations or fraudulent conduct as an inducement for the franchisee to enter the franchise agreement in the first place. Termination would be pursuant to specific sections as set out in the Contractual Remedies Act 1979. Further, if a franchise agreement specifically allows a franchisee a right to terminate on, for example, six months' notice, a franchisee would be able to give such notice if required to exit the franchise but would lose the right to sell its business and recoup the upfront franchise fee together with any goodwill paid to the franchisor.

**27** May a franchisor refuse to renew the franchise agreement with a franchisee? If yes, in what circumstances may a franchisor refuse to renew?

A franchisor may refuse to renew the franchise agreement with a franchisee if some provisions in the franchise agreement allow it to do so. If a franchisee has breached the franchise agreement in a material way during the term, or if two or more breach notices have been issued within a 12-month period then the franchisor may be able to block any renewal provided the franchise agreement contains such a relevant clause. Further, if a franchisee is in default at the time of purporting to renew a franchise agreement, the franchisor could prevent such renewal.

**28** May a franchisor restrict a franchisee's ability to transfer its franchise or restrict transfers of ownership interests in a franchisee entity?

A franchisor may restrict a franchisee's ability to transfer its franchise or restrict transfers of ownership interests in a franchisee entity provided the franchise agreement contains a right of first refusal clause in favour of the franchisor. Further, any transfer or sale of a franchise by a franchisee is always subject to the consent of a franchisor, who should be able to say no without giving any reasons.

**29** Are there laws or regulations affecting the nature, amount or payment of fees?

There are no laws or regulations affecting the nature, amount or payment of fees, but should an unfair interest rate be imposed, for example, 30 per cent or 40 per cent then the equitable doctrine

## Update and trends

The hot topic which was recently confirmed by the New Zealand government is that it has no intention to introduce any franchise-specific legislation at this time.

Also, the time is getting closer where a judge of the New Zealand High Court may imply a duty of good faith into franchise agreements and this duty of good faith will expand globally in the future as it is now doing in some countries.

of unjust enrichment may be available to assist a disgruntled and unfairly treated franchisee.

**30** Are there restrictions on the amount of interest that can be charged on overdue payments?

There are no restrictions on the amount of interest that can be charged on overdue payments but any ridiculous or oppressive amount is likely to be challenged by a franchisee or a franchisee's lawyer.

**31** Are there laws or regulations restricting a franchisee's ability to make payments to a foreign franchisor in the franchisor's domestic currency?

Laws and regulations exist restricting a franchisee's ability to make payments to a foreign franchisor in the franchisor's domestic country. As discussed in question 5, in all cases non-resident withholding tax would have to be deducted. In relation to many countries, New Zealand has double taxation treaties so any tax paid in New Zealand by an overseas franchisor in relation to the repatriation of income should be able to be claimed as a tax credit in the franchisor's foreign country.

**32** Are confidentiality covenants in franchise agreements enforceable?

Confidentiality covenants in franchise agreements are enforceable.

**33** Is there a general legal obligation on parties to deal with each other in good faith? If so, how does it affect franchise relationships?

There is a general legal obligation on parties to deal with each other in good faith and a good faith clause should always be included in franchise agreements. The courts in New Zealand are moving towards implying a duty of good faith into franchise agreements if no such duty is expressly stated (but it has not happened yet). Both parties should act loyally and faithfully towards each other at all times as that is the essence of any franchise relationship.

**34** Does any law treat franchisees as consumers for the purposes of consumer protection or other legislation?

There is the Consumer Guarantees Act 1993 but this does not apply to a franchisee who purchases products from a franchisor because both parties are in business.

**35** Must disclosure documents and franchise agreements be in the language of your country?

There is no legal requirement for disclosure documents and franchise agreements to be written in English, but since the major language of New Zealand is English, all parties would insist that the English language is used.

**36** What restrictions are there on provisions in franchise contracts?

There are no restrictions on provisions in franchise contracts except that there must be compliance with the Commerce Act 1986 as mentioned earlier, with the main thrust being that there must be no price-fixing, anti-competitive behaviour or other restrictive trade practices. Obviously, all provisions must comply with New Zealand law.

**37** Describe the aspects of competition law in your country that are relevant to the typical franchisor. How are they enforced?

See question 36. The Commerce Commission enforces the Commerce Act 1986 and its wide powers include declaring a transaction void together with monetary penalties, and there is a current trend for the courts to award higher penalties if the gravity of the offence demands that the public should be protected. At present, it has no power to imprison a guilty party.

**38** Describe the court system. What types of dispute resolution procedures are available relevant to franchising?

The lowest level court in New Zealand is the district court. For claims exceeding NZ\$200,000, the High Court of New Zealand is the relevant body. Appeals from the High Court of New Zealand go to the Court of Appeal of New Zealand, which sits in Wellington. Appeals from the Court of Appeal go to the Supreme Court of New Zealand, which also sits in Wellington.

Up until a few years ago, appeals from the New Zealand Court of Appeal went to the Privy Council in London but that right has now been abolished.

If a franchisor belongs to the FANZ, the franchise agreement must contain a dispute resolution clause. The Code of Practice prescribes that mediation is mandatory and it has a high chance of success. There is also the Arbitration Act 1996. A domestic franchisor

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who is not a member of the FANZ can resort to court action but the courts usually require an attempt to resolve the dispute by way of mediation. A foreign franchisor could issue proceedings in New Zealand and sue a particular franchisee. But again, the courts may require an attempt to settle any dispute by way of mediation. The governing law in any franchise agreement is important and most foreign franchisors require the governing law to be that of their home country. However, it is recommended that foreign franchisors should stipulate that the governing law should be the laws of New Zealand as it is far easier to take swift action in relation to a defaulting master franchisee or a franchisee through the New Zealand courts and to apply New Zealand law.

39 In what respects, if at all, are foreign franchisors treated differently from domestic franchisors?

Foreign franchisors still need to comply with the laws of New Zealand so far as they affect them. The only way they would be treated differently from domestic franchisors may be in the area of taxation where income of any sort which is to be repatriated from New Zealand to an overseas jurisdiction will be subject to non-resident withholding tax.

