

## CONCEPT AND LEGALITY OF FRANCHISE BUSINESS MODEL IN FIQH MUAMALAH

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### Abstract

Franchising is one type of marketing in the modern era, where an individual businessman or business entity claims his business with certain characteristics and has special rights or the use of trademarks and business models. This research wants to see about the concept and legality of the franchise business model in the perspective of Islamic economic law. This research uses a literature approach, where the main data is obtained from secondary data sources, both from legal norms, relevant research and articles that have a relationship with this research. The results show that the concept of a business or venture using a franchise platform is permissible as long as it is in accordance with the principles allowed in Islam. Franchises are prohibited if they contain elements, such as businesses that aim to avoid various business irregularities (moral hazard), namely maysir (speculation), immorality, gharar (fraud), haram, usury, ikhtikar (hoarding/monopoly), and dharar (harmful).

**Keywords:** Business, Legality, Fikih Muamalah and Franchising

### INTRODUCTION

Franchising is a special right owned by individuals or business entities to a business system with the characteristics of a business in the marketing of a good and / or service that has proven successful and can be utilised and / or used by other parties<sup>1</sup> The utilisation of business expertise by other parties in the franchise agreement is in great demand by the people of Indonesia. This is as we all know that many KFC, Mc. Donald, Bakso

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<sup>1</sup> Mustofa Amirul Hadi, *Valuation of Franchise, A Study of Intangible Property Valuation in a Concept of Business Valuation Theory*. (Yogyakarta: CV Budi Utama, 2022), p. 26.

Kepala Sapi, supermarkets: Indomaret, Alfamaret, AlfaExpres, Giant, Carrefour, and so on.<sup>2</sup>

Franchising has several types, namely business format franchising and product and trademark franchising. Business format franchising is the granting of licence rights by the franchisor to the *franchisee* along with the entire package consisting of all elements. While product and trademark franchising is the simplest form of franchising by granting a trade licence to the *franchisee* to sell the *franchisor's* products along with granting permission to use the trademark.<sup>3</sup>

Indonesia is a developing country that requires innovations, one of which is innovation in the economic sector. economic development can also be a benchmark for the development of a country. In today's economic development, one of them is a franchise business. Franchise business has recently become a business that many people choose in the hope that the business can easily and quickly bring profits.

In the Regulation of the Minister of Trade of the Republic of Indonesia Number 12 of 2006, Franchise is an agreement between franchisees and franchisees. Franchisors get the right to run a franchise business and utilise intellectual property rights in the business owned by the franchisor. Franchisees are charged a fee based on conditions determined by the franchisor and the franchisor is obliged to provide ongoing operational consulting support to the franchisees.<sup>4</sup>

This type of franchise business was born in the United States about a century ago, when the Singer sewing machine company began introducing the concept of franchising as a way to expand its product distribution. Similarly, beer companies authorised small companies to distribute their products.<sup>5</sup> Businesses conducted under a franchise system allow small entrepreneurs in Indonesia to develop by using the recipes, technology,

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<sup>2</sup> Siti Rahayu, Supartini Supartini, and Sinarianda Kurnia Hartanti, "The Principle of Proportionality in Franchise Agreements," *Progressive Civics: Journal of Civic Thought and Research* 14, no. 1 (2019): 81, <https://doi.org/10.20961/pknp.v14i1.34789>.

<sup>3</sup> I Rachmayani, I Iswandi, and A A Fitri, "Implementation of Product Franchise and Trademark Business from the Perspective of Islamic Law (Case Study at Outlet Donat Bakar Haurgeulis Branch)," *Journal of Law and Human Rights Wara Sains* 1, no. 02 (2022): 84-99.

<sup>4</sup> Minister of Trade of the Republic of Indonesia, "Regulation of the Minister of Trade of the Republic of Indonesia Number 23 of 2020," *Temporary Export Ban on Antiseptics, Mask Raw Materials, Personal Protective Equipment and Masks* 23 (2020): 1-6.

<sup>5</sup> Sri Redjeki et al., "Franchising in Indonesia," *Franchising in Indonesia Lex Jurnalica* 8, no. 2 (2011): 127.

packaging, service management, trademarks/services of others by paying royalties based on the terms of the franchise business. In addition, the development of quality human resources is also part of the important thing, so through in-depth skills training to run a franchise business run by franchisees, small entrepreneurs do not need to bother to create their own business system, only need to provide business capital to partner using the franchise system through a business licence to use the same trademark in accordance with the agreed agreement.<sup>6</sup>

A franchise agreement is a legal act to create rights and obligations of the parties. Through a franchise agreement, the franchisor grants the franchisee the right to operate as a business partner in the same field where the trademark or trade name is used and other intellectual property rights while maintaining the quality standards and reputation of the franchisor regarding the use of the brand of goods and/or services received.<sup>7</sup> The franchisor shall grant permission to franchisees for a certain period of time to engage in the business of distribution of goods and services on behalf of the franchisor in a certain territory. The business must be run according to the procedures and methods specified by the franchisor, and then the franchisor provides assistance to the partner. In return, the franchisee pays a fee in the form of royalties.

Franchising is also well known in the concept of sharia law where the cooperation uses a syirkah contract, namely the purchase of intellectual property in the form of trademarks, inventions, and product characteristics as the rights of franchisees. From the perspective of the form of agreement that can be made by the franchisee and the franchisee, it can be stated that the agreement is actually a form of shirkah cooperation. this is one form of development of cooperation because the franchise agreement has automatically formed a cooperative relationship between the franchisee and the franchisee for a certain period of time according to the agreement. The cooperation aims to obtain benefits for both parties.<sup>8</sup>

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<sup>6</sup> Muhammad Achyar, Chairul Fahmi, and Riadhus Sholihin, "ISLAMIC LAW REVIEW OF MONOPOLY PRACTICES IN MODERN ECONOMICS," *Al-Mudharabah: Journal of Islamic Economics and Finance* 5, no. 2 (2024): 288-308.

<sup>7</sup> Salim H.S, *Development of Innominaat Contract Law in Indonesia*, (Jakarta: Sinar Grafika, 2003), p. 165. 165.

<sup>8</sup> Chairul Fahmi, "The Impact of Regulation on Islamic Financial Institutions Toward the Monopolistic Practices in the Banking Industry in Aceh, Indonesia,"

The rise of trade in goods and services with the franchise system, because the system is more profitable for both franchisees and franchisees. For franchisees, it is a fast way to expand the distribution system with minimum capital, the ability to grow without the cost of developing key managers internally, and receive income from franchisees. As for the franchisees themselves, it is a way to do business directly with enough capital without adequate skills.<sup>9</sup>

The more advanced the life of society in a country, the more problems that arise in human life. These problems arise in all aspects of life, ranging from problems of worship to problems in muamalah. Islamic economics is a business or activity carried out by individuals, groups of people, business entities incorporated in order to meet commercial needs according to sharia principles. According to Islamic law, franchise agreements are not contrary to Islamic law. As long as the object in the agreement is not something that is prohibited in Islamic sharia, and does not harm one or both parties who work together.<sup>10</sup>

This situation certainly deserves the attention of people in business because it is an opportunity. This business opportunity can be filled by collaborating with franchisors that are in demand by the public.<sup>11</sup>

## DATA AND METHODS

The research is a type of doctrinal or normative research with a literature review approach. Data is obtained from secondary sources, both primary materials from the law, as well as from secondary data, namely from related research or articles relevant to the title of this research. The data obtained is then analysed using a descriptive analysis approach to present and describe the findings, related to the concept of franchising in the perspective of muamalah fiqh.

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*Peuradeun Scientific Journal* 11, no. 2 (May 30, 2023): 667–86,  
<https://doi.org/10.26811/peuradeun.v11i2.923>.

<sup>9</sup> Iman Syahputra Tunggal, *Franchising: Concepts & Cases*, (Jakarta: Harvarindo, 2004), p. 18.

<sup>10</sup> Suhrawardi K Lubis, *Islamic Economic Law*, (Jakarta: Sinar Grafika, 2004), p. 169.

<sup>11</sup> By Indira Hastuti, "Legal Aspects of Franchise Agreements (FRANCHISE)," 1995, 27-38.

## RESULTS AND DISCUSSION

### A. Definition of Franchise

The term franchise in foreign languages is called a franchise. The origin of the word comes from old French which means free. Around medieval times, the government or nobility in England used franchises to grant special rights such as to operate ferries or hunt on land owned by the government or nobility.<sup>12</sup>

Franchise in Indonesia is called franchise. The word franchise itself comes from 2 (two) words, namely wara and profit. Wara means special and profit means profit. The word franchise was first introduced by LPPM (Lembaga Pembinaan dan Pengembangan Manajemen) as an equivalent of the word franchise.<sup>13</sup>

Franchising, according to Suhrawardi K. Lubis, is a franchise agreement that grants the franchisor the right to use business distinctiveness or business identifying characteristics in the field of trade or services, including the type of product and its form, as well as the time, hours, and hours of operation, clothing, and appearance of employees.<sup>14</sup>

According to the Regulation of the Minister of Trade of the Republic of Indonesia Number 12 of 2006, a franchise is an agreement between a franchisor and a franchisee in which the franchisee is granted the right to run a business by utilising and/or using the intellectual property rights or inventions or business characteristics owned by the franchisor in return for a fee based on the terms set by the franchisor with a number of obligations to provide continuous operational consulting support by the franchisor to the franchisee.<sup>15</sup>

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<sup>12</sup> Chairul Fahmi, "Analysis Of Legal Aspects On Capital Investment Fraud In Indonesia," *Proceeding of International Conference on Sharia Economic Law (ICoShEL)* 1, no. 1 (September 9, 2024): 79-95.

<sup>13</sup> Ahmad Luqman Hakim and Irfa Munandar, "THE LEGALITY OF MURABAHAH CONTRACTS SYSTEM IN ISLAMIC FINANCING INSTITUTIONS: An Analysis of Muḥammad Bin Ṣāliḥ Al-Uṣaimin's Thought," *JURISTA: Jurnal Hukum Dan Keadilan* 7, no. 1 (2023): 24-36, <https://doi.org/10.1234/jurista.v7i1.66>.

<sup>14</sup> Raudhatul Jannah, Chairul Fahmi, and Azka Amalia Jihad, "Financing Micro, Small and Medium Enterprises (MSMEs) After the Implementation of Qanun LKS in the Perspective of Maqashid Syariah," *AJIEL - Ar-Raniry Journal of Islamic Economic Law* 1, no. 1 (June 2, 2024): 1-25.

<sup>15</sup> Maratun Shalihah, "The Concept of Shirkah in Franchising," *Tahkim* XII, no. 2 (2016): 142-53.

As per Government Regulation No. 42 Year 2007, it defines franchising as: "A specific right owned by an individual or business group over a pattern of business using the special characteristics of the business in the framework of offering goods and services that have been tested successfully and can be used and utilised by other parties of the franchise agreement." Today, trading systems that use franchising, also known as franchising, have evolved in response to the challenges faced by modern society. To run a franchise system, businesses do not need to invest directly; instead, they can cooperate with other companies. Franchise is a type of business that is based on a favourable relationship or connection between parties.<sup>16</sup>

So the name or brand of the product being marketed usually helps the seller in the franchise business. New customers will come from communities that are already familiar with the brand or name of the item being sold. For example Pizza Hut, Kentucky Fried Chicken, or Indomart. Consumers must know these names. Because these brands are already known and recognised by the community, the franchisor does not need to do significant promotion. The franchisor and franchisee are the two parties involved in this business based on the above definition. To avoid losses, franchisees must be careful when starting a franchise outlet. Some things to note are as follows. The business format franchise consists of;

- a) Franchisor's overarching Business Concept.
- b) There is a start-up process and training on all aspects of business management, in accordance with the franchisor's concept.
- c) A process of continuous assistance and guidance from the franchisor.

In general, the components that make up a franchise agreement are as follows

- a) Franchisees, are parties who have certain systems or ways of doing business. Franchisees are business entities or individuals who grant rights to other parties to utilise and or use their intellectual property rights or inventions or business characteristics."

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<sup>16</sup> Kausar Rizqi Safrizal, "Analysis of Investment Implementation in Shari'ah Insurance Company According to Fiqh Muamalah," *AJIEL - Ar-Raniry Journal of Islamic Economic Law* 1, no. 2 (December 12, 2024): 133–47.



- b) Franchise, which is a party that receives a franchise or business system from franchisees so that it has the right to run a business in ways developed by franchisees.
- c) Franchise, which is the system and ways of the business itself, this is the knowledge or business specifications of the franchisees sold to the franchise, in a franchise agreement, the franchise is the object of the agreement.

According to Government Regulation 42/2007. Article 4 on franchising A Franchise Agreement must at least contain clauses on the following matters:

- a) Identity of each party;
- b) The identity and title of each party authorised to sign the Wara laba Agreement;
- c) A description of the intellectual property rights or inventions or characteristics of the products and/or services that are the object of the franchise;
- d) The rights and obligations of each party and the support and facilities provided to the franchisee;
- e) Marketing area. in this case, the franchisor can determine whether the marketing area covers all or part of Indonesia;
- f) The term of the Franchise Agreement (which shall be at least for a period of 5 (five) years and the procedures and requirements for renewal of the Agreement;
- g) Procedure for dispute resolution;
- h) Matters that may result in termination or expiration of the Franchise Agreement;
- i) Indemnification in the event of termination of the Franchise Agreement;
- j) Payment procedure;
- k) The use of domestically produced products or materials provided that they fulfil the requirements of established quality standards; and
- l) Coaching, training and guidance for Franchisees.<sup>17</sup>

It is generally recognised that there are two kinds or types of compensation that franchisors can demand from franchisees. First, direct

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<sup>17</sup> Tami Rusli, "Analysis of the Franchise Agreement of Alfa Mart Store," *Progressive Justice* 6, no. 1 (2015): 64-75.

monetary compensation is a lump sum payment and royalty. A lump sum payment is a pre-calculated amount of money that must be paid by the franchisee at the time the franchise agreement is concluded. Meanwhile, a royalty is an amount of payment that is linked to a certain percentage calculated from the amount of production and/or sales of goods and/or services produced or sold under the agreement, whether or not it is tied to a certain minimum or maximum amount of royalty.<sup>18</sup>

Second, indirect and non-monetary compensation. This includes, among others, profits as a result of the sale of capital goods or raw materials, which is a package with the granting of the franchise, payments in the form of dividends or interest on loans in the event that the franchisor also provides financial assistance, either in the form of equity or in the form of short-term or long-term loans, cost shifting or transfer of some of the costs that must be incurred by the franchisor, acquisition of market data from business activities carried out by the licensee and so on.<sup>19</sup>

## **B. Franchising in the Perspective of Islamic Law.**

Franchising is also well known in the concept of Sharia law where the cooperation uses a syirkah contract, namely the purchase of intellectual property in the form of trademarks, inventions, and product characteristics as the rights of franchisees. From the perspective of the form of agreement that can be made by the franchisee with the franchisee, it can be stated that the agreement is actually a form of shirkah cooperation. this is one form of development of cooperation because the franchise agreement has automatically formed a cooperative relationship between the franchisee and the franchisee for a certain period of time according to the agreement. The cooperation aims to obtain benefits for both parties.<sup>20</sup>

Seeing the above explanation about franchising, then according to the author, the concept of franchising includes the concept of musyarakah (syirkah) in fiqh muamalah. Musyarakah (shirkah) is definitively a

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<sup>18</sup> Chairul Fahmi and Peter-Tobias Stoll, "Measuring WTO Approaches in Resolving Palm Oil and Biofuel Trade Disputes from Indonesia," *BESTUUR* 12, no. 2 (December 31, 2024), <https://doi.org/10.20961/bestuur.v12i2.94203>.

<sup>19</sup> Riezka Eka Mayasari, "Franchise in the Islamic Legal System and Positive Law in Indonesia," *Al-Ishlah: Scientific Journal of Law* 21, no. 2 (2018): 108-14.

<sup>20</sup> J Beno, A.P Silen, and M Yanti, "Franchise Cooperation Practices in the Perspective of Sharia Economic Law (Case Study at Gopal Kebab Doro Pekalongan Regency)," *Braz Dent J.* 33, no. 1 (2022): 1-12.



cooperation between two or more people in terms of capital, skills, or trust in a particular business with profit sharing based on the ratio agreed upon by the parties to the union." Based on the above definition, shirkah is categorised as:

- a) Cooperation in capital;
- b) Franchising is done in writing, as commanded by QS. Al-Baqarah (2) 282.
- c) It must not conflict with Islamic law, for example, a business selling goods that are forbidden by Islamic law.
- d) The business is a business that contains maslahah/benefit.
- e) Does not contain elements prohibited by Islamic law, such as *matur* (gambling), immorality, usury, *ikhtikar* (hoarding goods/monopoly/damaging market prices).

*Franchisors* also earn revenue from royalty payments by *franchisees*. While franchising offers many advantages, it also comes with risks. One of them is losing control of the brand and reputation if the *franchisee* does not adhere to the set standards. Competition and high start-up costs can also be a challenge. In Islam, the concept of franchising can be seen through the principles contained in several propositions. One of the relevant propositions is the hadith of Prophet Muhammad (SAW) which states the principle of sharing profits and co-operation in business.

### C. The Concept of Franchise Business Agreement in Islamic Perspective

Agreement is one way to obtain something that is widely used in everyday life, especially in carrying out economic activities. This agreement must be made by both parties to the transaction and it is this agreement that determines whether a transaction is valid or not.

If we look at the form of the *franchising* agreement, it can be stated that the franchise agreement is actually a combination of three forms of contracts, namely a cooperation contract (*syirkah*), a debt and credit / borrowing contract, and a lease contract (*ijarah*).<sup>21</sup>

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<sup>21</sup> Ayla Natasya and Sayed Mohammad Reza Yamani, "THE VALIDITY OF TRANSACTIONS ON THE ACTION MOBILE APPLICATION OF BANK ACEH SYARIAH, INDONESIA," *JURISTA: Jurnal Hukum Dan Keadilan* 7, no. 1 (June 20, 2023): 37–63, <https://doi.org/10.1234/jurista.v7i1.68>.

*Franchise* agreement as a business partnership agreement, where the franchisor capitalises on Intellectual Property Rights and business experts, while the franchisee capitalises on assets and business experts. Each business partner agrees to share the results and risks of the business venture in accordance with the quantity and quality of their respective workloads or obligations. The combination of various types of capital and sharing various results and risks is an application of the *syirkah 'Inan* contract.

Prospective franchise users (*franchisees*) usually require a certain amount of money to be able to work with the franchisor. Franchise can get it through loans with other parties. However, it could be the *franchisor* who provides loans to him as business capital. This agreement regarding borrowing and lending is contained in a debt and credit agreement.<sup>22</sup>

In a *franchise* agreement, where the *franchisor* grants a licence (permission) to the franchisee to run a business by utilising or using Intellectual Property Rights in return for which the franchisee pays a *fee* (*franchise fee*) to the franchisor within a certain time limit, and sometimes the franchisor has its own standards and designs for each of its outlets. The *franchisees* are allowed to build their own outlets, but the *franchisor* still has the right to interfere in terms of standards and design, for example to match the characteristics of its business.

In the operation of franchise activities, the principles of openness, honesty and prudence are also applied. The basic principles of mu'amalah that must be fulfilled in the agreement are activities that contain maslahat, uphold the principles of justice, honesty, mutual assistance, not complicate, mutual consent and avoid all forms of usury.<sup>23</sup>

The construction of an agreement based on Islamic law, in addition to fulfilling the principles of mu'amalah, must also fulfil the pillars and conditions of the validity of the agreement. In addition, there are provisions regarding the obligation to fulfil the agreement and the prohibition of

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<sup>22</sup> Chairul Fahmi and Wira Afrina, "ANALYSIS OF LEGAL ASPECTS ON DEBT TRANSFER FROM CONVENTIONAL BANK TO SHARIA BANK POST THE APPLICATION OF QANUN ACEH NO. 11 OF 2018," *Al-Mudharabah: Jurnal Ekonomi Dan Keuangan Syariah* 4, no. 1 (July 23, 2023): 28-39.

<sup>23</sup> Nurul Maghfirah et al., "UNDERSTANDING INTELLECTUAL PROPERTY RIGHTS IN THE INDONESIAN TRADING BUSINESS," *Al-Mudharabah: Jurnal Ekonomi Dan Keuangan Syariah* 3, no. 2 (2022): 89-103, <https://doi.org/10.22373/al-mudharabah.v4i2.3384>.

cooperation to commit a sin, as well as the ability for the parties to perform legal acts.<sup>24</sup>

To create an Islamic franchise business system, a sharia value system is needed as a business moral filter that aims to avoid various business deviations (moral hazard), namely Maysir (speculation), Immorality, Gharar (fraud), Haram, Riba, Ikhtikar (hoarding/monopoly), Dharar (harmful).<sup>25</sup>

In Islamic Fiqh, there are two things that are assessed in the concept of Franchising, namely:

1. The purchase of Intellectual Property Rights (HAKI) in the form of trademarks, inventions and product characteristics or business management as a patent owned by the franchisor, Consequences of Islamic law views that copyright (ibtikar) is included in the category of property that results in the inventor or creator against the results of his work or creation into absolute property rights that are material. The inventor or creator is entitled to the value of the material or the right, when used or utilised by others with his permission. This right is like property and applies to the laws surrounding it.<sup>26</sup>
2. The concept of cooperation in franchising can be classified with Syirkah Uqud, which is two or more parties making an agreement or contract to combine assets to conduct a business / business, and the results are shared both in the form of profit and loss.<sup>27</sup>

The scholars of fiqh are generally of the opinion that cooperation in buying and selling is called shirkah. Shirkah is divided into 2 main classifications namely syirkah *al- amlak* and *syirkah al-uqud*. *Syirkah al-amlak* some call it *musyarakah* ownership, some call it a *union in ownership* and some call it a *property rights company*. While *syirkah al uqud* some call it *musyarakah aqad* (contract), some call it the *union of an aqad*.

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<sup>24</sup> Neilul Masyitah et al., "Factors of Exchange of Waqf Property According to Positive Law and Islamic Law in Indonesia: A Case Study in Pidie District of Aceh Province," *AJIEL - Ar-Raniry Journal of Islamic Economic Law* 1, no. 2 (December 1, 2024): 97-118.

<sup>25</sup> Anwar, *Law*, p. 70.

<sup>26</sup> Djuwaini, Dimyauddin. *Introduction to Fiqh Muamalah*. Student Library. Yogyakarta. 2008. Page. 298.

<sup>27</sup> "Development of Musyarakah Agreements," n.d.

1. Syirkah amlak (ownership), namely: partnership between two or more people to own an object, syirkah amlak is divided into 2, namely syirkah ikhyar and syirkah jabbar.
2. Shirkah contract, which is a partnership between two or more people that arises from an agreement. Imam Taqyuddin An-Nabhani called shirkah contract as a transaction company, which is a company whose object is the development of property rights Shirkah contract, divided into four (4), namely:
  - a) Shirkah amwal, which is a partnership between two or more people in capital / assets.
  - b) Shirkah a'mal, which is an agreement between two or more people to accept work from a third party to be done together with the provision that the wages are divided in half.
  - c) Shirkah wujuh, which is a partnership between two or more people with capital from an outside party.
  - d) Shirkah mudharabah, which is an agreement between the owner of the capital and the worker as the manager of the business to manage the money from the owner of the capital in a certain trade, whose profits are divided according to mutual agreement.

Shirkah mudharabah is a partnership (alliance) between labour and wealth, which is managed for business, with the stipulation that the profit (profit) obtained will be shared according to the agreement of both parties. The basic form of mudharabah is lending money for business purposes. Shirkah mudharabah is divided into 2 forms, namely:

- a) mudharabah muthlaqah in this case the investor gives his property to the executor for mudharabahkan with no specify the type of work, place and time and person.
- b) Mudharabah muqayyadah (bound by a condition), is where the owner of the capital specifies one of the above types.

If considered from the angle of the form of agreement held franchising (franchising) can be argued that the franchise agreement is actually a development of the form of cooperation (syirkah). It can be understood that with the franchising agreement, then automatically between the franchisor and franchisee formed a cooperative relationship for a certain time (in accordance with the agreement). The cooperation is

intended to obtain benefits for both parties by way of cooperation either in the form of granting permission to use certain trademarks and trade recipes, or cooperation in fostering labour expertise. There is also cooperation where one party expends labour and the other party only expends business capital with an agreement that profits will be shared according to the agreement. In the operation of franchise activities, the principles of openness, honesty and prudence are also applied. The basic principles of mu'amalah that must be fulfilled in the agreement are activities that contain maslahat, uphold the principles of justice, honesty, mutual assistance, not complicate, mutual consent and avoid all forms of usury. The construction of agreements based on Islamic law, in addition to fulfilling the principles of mu'amalah, must also fulfil the pillars and conditions of the validity of the agreement. In addition, there are provisions regarding the obligation to fulfil the agreement and the prohibition of cooperation to commit a sin, as well as the ability for the parties to perform legal acts.<sup>28</sup>

According to contemporary Islamic jurists, the pillars that make up a contract are four, namely:

- a) The parties making the contract (*al-'aqidain*)
- b) Statement of the parties' will (*shigatul-'aqad*)
- c) The object of the contract (*mahallul-'aqad*)
- d) The purpose of the contract (*maudhu' al-'aqad*).

The 4 (four) pillars of the contract are in principle the same as the conditions for the validity of the agreement stipulated in Article 1320 of the Civil Code. The subject of the engagement relates to the parties who make the engagement, both individuals and legal entities. In this case, it relates to the competence of the parties, including (1) competence (*al-ahliyyah*), which is divided into the ability to accept the law (*ahliyyatul wujub*) and the ability to act legally (*ahliyyatul ada*), (2) authority (*wilayah*), and representation (*wakalah*). The expression of will consists of *ijab* and *kabul*, which represent an agreement (*arridha, toestemming*). *Ijab* (offer) is the first statement of will in the form of an offer made by one party to another party to create a legal action. *Kabul* (acceptance) is a statement of will from the other party to accept the *ijab* conveyed by the offering party, thus creating a contract. The object of the contract can be in the form of objects (both movable and

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<sup>28</sup> Linda Firdawati, "Franchise Agreement According to Islamic Law," *Asas* 3, no. 5 (2011): 40-49.

immovable objects, as well as tangible and intangible objects), the benefits of objects, services or work, or something else that is not contrary to sharia.<sup>29</sup>

The condition for the validity of a contract/agreement is the fulfilment of the purpose of the contract as the main effect of a contract. The conditions that must be fulfilled for the purpose of the contract to be considered valid and have legal consequences are:

- a) The purpose of the contract is not an obligation that would have been incurred by the parties without the contract.
- b) The purpose must continue to exist until the end of the execution of the contract
- c) The purpose of the contract must be justified by Shara'

Looking at the technical operations applied to the franchise business, it can be understood that in the franchise agreement there are no obstacles or prohibitions in Islamic business. Thus, it can be argued that the franchise agreement is not contrary to Islamic law.

Of course, with a note that the object of the franchise agreement is not something that is prohibited in Islamic law, and in the franchise agreement the pillars, conditions and basic principles of muamalah have been fulfilled. This means that this agreement is permissible and valid if it fulfils the pillars and conditions of the agreement in general. If the object of the franchise is something that is prohibited in Islamic law (for example, haram food and drink), then the agreement is automatically contrary to Islamic law. Requirements to become a Franchisee:

- a) The term of the franchise agreement is not less than ten years;
- b) How to resolve disputes;
- c) The procedure for payment of rewards; and
- d) Franchisee coaching, guidance and training. Once the agreement is finalised, the franchisee must register with the director general of domestic trade of the Ministry of Trade of the Republic of Indonesia to obtain a franchise business registration certificate (STPUW).

Applications must be accompanied by the following documents:

- a) A copy of the personal identity of the company owner or manager;

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<sup>29</sup> Norman Syahdar Idrus, "Legal Aspects of Franchise Agreements in the Perspective of Civil Law and Islamic Law," *Yuridis Journal* 4, no. 1 (2017): 28, <https://doi.org/10.35586/.v4i1.125>.



- b) A copy of the business licence of the ministry or technical agency;
- c) A copy of the company registration mark (TDP);
- d) A copy of the franchise agreement;
- e) A copy of the franchisor's business prospectus.
- f) A copy of the franchisor's business legality letter.
- g) The term of the STPUW is 5 years and can be extended as long as the franchise agreement is valid.

#### **D. Rights and Obligations of Parties in Franchising**

The obligations of *franchisees* who become *franchise* rights are as follows:

- 1) Brand, Name which includes logo, landing and others.
- 2) Systems and business operation manuals.
- 3) Support in operations, because after all, franchisees have more extensive experience,
- 4) Monitoring which aims to ensure that the system provided is carried out properly and correctly on a consistent basis,
- 5) Combination of promoss/joint promotion, because it is related to the brand name,
- 6) Supply that applies to certain franchisees, for example for franchisees who are food/beverage ingredient suppliers. Sometimes franchisees also supply certain necessary machinery or equipment.<sup>30</sup>

Meanwhile, the obligations of franchisers which are the rights of franchisees can be divided into two types, namely:

- 1) Direct monetary compensation can be realised in two forms: (a) Lampsuns payment, which is an amount of money that has been calculated in advance and must be paid by the franchisee at the time the franchise agreement is concluded. This payment can be made in cash or in several instalments. And (h) royalty, which is a payment amount linked to a presentation and calculated from the amount of production and/or sales of goods and/or services produced or sold under the agreement, whether or not accompanied by a bond of a certain minimum or maximum amount of royalty.

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<sup>30</sup> Asiva Noor Rachmayani, "The Concept of Franchise Business Agreement in Islamic Perspective," 2015, 6.

- 2) Indirect compensation in the form of monetary value (indirect and non monetary compensation). This compensation usually includes: (a) profits as a result of the sale of capital goods or raw materials that come with the franchise. Usually this agreement is made in the form of an exclusive purchase arrangement. (b) Payment of compensation can also be realised in the form of dividend distribution as a result of equity participation or realised in the form of short-term or long-term loans.
- 3) The transfer of some of the costs incurred by the franchisor (cost shifting) to the franchisee in order to prevent infringement or as an effort to protect intellectual property rights.

The *Franchisor* also earns revenue from royalty payments by *franchisees*. While franchising offers many advantages, it also comes with risks. One of them is losing control of the brand and reputation if the *franchisee* does not comply with the set standards. Competition and high start-up costs can also be a challenge. In Islam, the concept of franchising can be seen through the principles contained in several propositions. One of the relevant propositions is the hadith of Prophet Muhammad (SAW) which states the principle of sharing profits and co-operation in business.

#### **E. Types of Franchises**

Franchising can be done either in the form of products franchise (brand), business format (sales system) or manufacturing plant franchising (secret formula of an item product).

##### **1. Product and Trade Franchise**

Franchising can be divided into two forms, namely trademark and product franchising, where the franchisor grants the franchisee the right to sell products developed by the franchisor and is accompanied by permission to use its trademark. For granting permission to use the trademark, the franchisor gets a form of royalty payment in advance, and then he also gets profits from the sale of his

products. For example, a petrol station that uses the Pertamina name/trademark.<sup>31</sup>

## 2. Business Format Franchise

A business format franchise is the granting of a licence by one person to another, the licence entitles the franchisee to do business using the franchisor's trademark or trade name and to use the whole package, consisting of all the elements necessary to make a previously untrained person skilled in the business and to run it with continuous assistance on a predetermined basis. This type of franchise is like the minimarket retail business of Alfamart, Indomart and the like.

Business format franchises consist of:

- a. Franchisor's overarching business concept
- b. There is a start-up process and training on all aspects of business management, in accordance with the franchisor's concept.
- c. A process of constant help and guidance from the franchisor.

## 3. Manufacturing Plant Francising (the secret formula of an item production)

In this kind of franchise, the franchisor gives the secret formula of a production which then produces the goods and also distributes them according to the same production standards and brands owned by the franchisor. This form of franchise is used by Coca Cola Production which has a secret formula for making coca cola and other soft drinks.<sup>32</sup>

## F. Franchise Profit Sharing System

Profit Sharing Islam interprets interest as usury which is forbidden by sharia. So that interest is not established in a sharia-based economy and

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<sup>31</sup> Linda Firdawaty, "Franchise Agreement According to Islamic Law," *ASAS: Journal of Sharia Economic Law* 3, no. 1 (2011).

<sup>32</sup> An Iiiuiauan and H T Kiim, "Business Law: The Legal, Ethical, and International Environment, Prentice Hill, Englewood, New Jersey" 431997, no. 7 (n.d.).

instead a profit-sharing system is applied. Profit sharing according to the term is a system that includes procedures for sharing business results between fund providers and fund managers. In a sharia-compliant franchise agreement, the main objective is the benefit or welfare of the parties that by doing business through the agreement there is a benefit between the two, namely the *shāhibul māl* (franchisee / capital provider) can benefit from the capital provided to the *muḍarrib* (franchisor), while the *muḍarrib* / franchisor can run his business through the capital.

The profit should be shared proportionately between the *shāhibul māl* and the *muḍarrib*. Thus, all regular expenses related to the *muḍārabah* business, not for the personal benefit of the *mudharib*, can be included in the operating expenses. The net profit should be shared between the *shāhibul māl* and the *muḍarrib* according to the proportion agreed upon in advance and explicitly mentioned in the initial agreement. There is no profit sharing until all losses have been covered and the *shahibul maal's* equity has been repaid. If there is any profit sharing before the end of the agreement period, it will be considered as advance profit sharing. The method of calculating profit sharing can be done with two approaches, namely:

- a. Profit sharing approach, is a profit sharing calculation based on the profit of the fund manager, which is the business income minus the business expenses to obtain the income.
- b. The revenue sharing approach, is the calculation of profit based on the income earned from fund managers, namely business income before deducting business costs to obtain that income.

Therefore, Sharia Economics outlines the concept of profit sharing as follows:

- a) Fund owners invest their funds through financial institutions that act as fund managers.
- b) The manager manages the funds with a system known as the fund collection system, then the fund manager invests the funds in a business that is profitable and that meets the provisions of sharia aspects.
- c) Both parties make an agreement (*akad*) that contains the scope of cooperation, the nominal amount of funds, the ratio, and the period of validity of the agreement.

Thus, the core of the profit-sharing investment mechanism basically lies in good co-operation between the shahibul maal and mudharib. Cooperation or partnership is a character in Islamic economic society. Economic co-operation must be carried out in all lines of economic activity, namely: production, distribution of goods and services. One form of co-operation in business or Islamic economics is qiraḍ or muḍārabah. Qiraḍ or muḍārabah is a cooperation between the owner of capital or money and the entrepreneur who has the expertise or skills or labour in the implementation of economic units or business projects. Through qiraḍ or muḍārabah, both partnering parties will not earn interest, but get profit and loss sharing from the mutually agreed economic project.

### **Example of a business**

#### **1. Baba Rafi Turkey Kebab**

Baba Rafi Turkey is one of the franchises based on the sharia system. This is as explained by Hendy Setiono (franchisor), that Kebab Turki Baba Rafi is one of the franchise businesses that apply Sharia system in which the franchisee (franchisee) invests its capital to the franchisor (franchisor) to manage Kebab Turki Baba Rafi outlet with profit sharing system of 50:50. According to the franchisor, the franchisee is exempted from royalty fee every month but the royalty fee is charged on net profit of 3%, profit sharing is also charged on net profit from kebab sales turnover.

Investment or initial capital of Rp 65,000,000 submitted by the Baba Rafi Turkey Kebab franchisee to the franchisor to then with that capital open a Turkey Kebab outlet managed by the franchisor with the aim of obtaining profit. The profit (net profit) obtained is divided in half with a profit ratio of 50:50. Example of profit sharing for example, in August obtained a profit of Rp 3,000,000 then the nominal profit sharing is the franchisor / franchisor Rp 1,500,000 and franchisee / franchisee of Rp 1,500,000, if in July obtained a profit of Rp 2,000,000 then the franchisor and franchisee each received Rp 1,000,000. In detail, the benefits and conditions of the Baba Rafi Turkey Kebab franchise can be described as follows:

1. The benefits for franchisees are free royalty fees every month; outlets are fully managed by the franchisor; profits are more guaranteed; and a 50:50 profit sharing system every month.

2. Provided that, all outlet management costs (BPO) are charged to the total turnover; and the outlet management costs include: a) use of raw materials (including packaging); b) employee commissions and salaries; c) rent of premises; d) transportation of approximately Rp 10,000/day; e) operational costs, such as LPG gas, repair or addition of outlet equipment; f) net profit is obtained from total turnover minus BPO; g) franchisee provides motorbike facilities for outlet operator operations; and h) the franchise period is 4 years and can be extended. From these provisions, it can be concluded that if there is debt, the debt includes BPO which can be deducted from the total turnover.

Looking at the system applied by Kebab Turki Baba Rafi, the profit sharing in the franchise agreement uses the *muḍārabah* system, where the management power is fully vested in the franchisor, who also doubles as the capital manager (*muḍarrib*).<sup>33</sup>

## CONCLUSIONS

Franchise is an agreement between the franchisor and the franchisee in which the franchisee is granted the right to run a business by utilising and/or using the intellectual property rights or inventions or business characteristics owned by the franchisor in return for a fee based on the terms set by the franchisor with a number of obligations to provide continuous operational consulting support by the franchisor to the franchisee.

Franchisors also earn revenue from royalty payments by *franchisees*. While franchising offers many advantages, it also comes with risks. One of them is losing control of the brand and reputation if the *franchisee* does not adhere to the set standards. Competition and high start-up costs can also be a challenge. In Islam, the concept of franchising can be seen through the principles contained in several propositions. One of the relevant propositions is the hadith of Prophet Muhammad (SAW) which states the principle of sharing profits and co-operation in business.

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<sup>33</sup> Puji Sulistyaningsih, Heniyatun Heniyatun, and Heni Hendrawati, "Profit Sharing System in Franchise Agreement from Islamic Law Perspective," *Novelty Law Journal* 8, no. 1 (2017): 137.



Franchise agreement as a business partnership agreement, where the franchisor capitalises on Intellectual Property Rights and business experts, while the franchisee capitalises on assets and business experts. Each business partner agrees to share the results and risks of the business venture in accordance with the quantity and quality of their respective workloads or obligations. The combination of various types of capital and sharing various results and risks is an application of the *syirkah 'Inan* contract.

To create an Islamic franchise business system, a sharia value system is needed as a business moral filter that aims to avoid various business deviations (moral hazard), namely Maysir (speculation), Immorality, Gharar (fraud), Haram, Riba, Ikhtikar (hoarding/monopoly), Dharar (harmful). Of course, with a note that the object of the franchise agreement is not something that is prohibited in Islamic law, and in the franchise agreement the pillars, conditions and basic principles of muamalah have been fulfilled. This means that this agreement is permissible and valid if it fulfils the pillars and conditions of the agreement in general. If the object of the franchise is something that is prohibited in Islamic law (for example, haram food and drink), then the agreement is automatically contrary to Islamic law.

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