

Client Update: Malaysia

2018 AUGUST

Dispute Resolution

Bubble Yet To Burst: Chatime vs Tealive, Round 2

Introduction

On 16 July 2018, the Chatime-Tealive battle reached the apex court of Malaysia, the Federal Court. The Federal Court granted an application to stay of the Court of Appeal order dated 27 June 2018, which had granted a prohibitory injunction against Tealive – in effect requiring all Tealive stores to close down. In order to understand what the Federal Court’s decision means for this dispute, and what will happen next, we travel back in time to late 2016, when trouble between both sides first started to brew.

The Dispute

La Kaffa International Co. Ltd. (“**La Kaffa**”), a Taiwanese company, is the owner of the Chatime franchise. It entered into a Regional Exclusive Representation Agreement (“**RERA**”) with Loob Holding Sdn Bhd (“**Loob**”) where it was agreed that Loob would be the Master Franchisee of Chatime franchise in Malaysia.

However, in October 2016 La Kaffa commenced arbitration proceedings against Loob in Singapore (“**Singapore Arbitral Proceedings**”) in accordance with the dispute resolution mechanism under the RERA, alleging that:

- (a) Loob failed to purchase all raw materials from La Kaffa as required by Article 7 of the RERA;
- (b) Loob failed to allow La Kaffa to inspect and/or audit, among others, Loob's accounts, books and records; and
- (c) Loob failed to pay for raw materials purchased from La Kaffa.

La Kaffa would terminate the RERA on 5 January 2017. Shortly after, Loob started its Tealive business, and 161 Chatime outlets “transformed” into Tealive outlets.

Pending the disposal of the arbitral proceedings in Singapore, La Kaffa filed a suit in the Malaysian High Court, requesting, among others:

- (a) a mandatory injunction to compel Loob to return materials related to Chatime’s trade marks and La Kaffa’s proprietary information to La Kaffa; and
- (b) a prohibitory injunction to prohibit Loob from carrying on a business which is identical or similar to the Chatime franchise business.

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If the above requests were granted in full, the injunctions would have lasted until the end of the arbitral proceedings in Singapore.

Meanwhile Loob also filed a suit in the Malaysian High Court, requesting an interim injunction to restrain La Kaffa from taking any action which had the effect of interfering with the Tealive franchise business.

This article will focus on the prohibitory injunctions requested by La Kaffa, as they were the primary focus of the Court of Appeal's judgment on 27 June 2018.

High Court Decision

The High Court set out 2 main points in its approach to this case:

- (a) first, the High Court would only grant interim measures which may support, assist, aid or facilitate the Singapore Arbitral Proceedings;
- (b) secondly, the High Court would not decide on the merits of La Kaffa and Loob's claims in the Singapore Arbitral Proceedings. Nothing in the High Court judgment would affect the integrity of the Singapore Arbitral Proceedings.

In deciding how the High Court would exercise its discretion to grant an interim prohibitory injunction, the following considerations were to be taken into account:

- whether there was any bona fide and serious question to be tried in respect of La Kaffa's cause of action against Loob; and if yes;
- whether damages constituted an adequate remedy for La Kaffa; and
- if damages did not constitute an adequate remedy for La Kaffa, whether the "balance of convenience" lied in favour of granting or refusing an interim prohibitory injunction.

It was La Kaffa's argument that Section 27(1) of the Franchise Act 1998 ("FA") restrained Loob from carrying on a business similar to the Chatime franchise business, while Section 26(1) of the Franchise Act restrained Loob from disclosing, using and converting La Kaffa's confidential information, both for two years after the expiration or earlier termination of the franchise agreement. Additionally, Article 15(1) of the RERA prohibited La Kaffa and Loob from carrying out competing businesses, and it was agreed that this provision would survive the invalidity, expiration or termination of the RERA.

However, the High Court rejected these arguments, stating that the said Section 26(1) and 27(1) of the FA provide that a franchisee "shall" give written guarantees as provided in those statutory provisions to a franchisor. In this case, Loob did not provide the guarantees to La Kaffa. Accordingly, the said guarantees were not incorporated into the RERA and there was no serious question to be tried in respect of whether Loob had breached Section 26(1) and 27(1) of the FA. Even if the guarantees were deemed

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to be incorporated into the RERA, the High Court held that it had the discretion to refuse or allow La Kaffa's application for interim injunctions.

In that regard, the High Court took the position that in the circumstances, damages were an adequate remedy for La Kaffa, citing the various provisions in the RERA which stipulate a monetary remedy in the event of any breach of the RERA by Loob. Hence, Loob was ordered by the High Court to serve on La Kaffa's solicitors an affidavit containing Loob's gross monthly sales and an account of profits from the Tealive franchise business on the tenth day of every calendar month from the date of the High Court order until the disposal of the Singapore Arbitral Proceedings.

The High Court also held that La Kaffa had been guilty of inequitable conducts which disentitled La Kaffa from applying for interim prohibitory injunctions – these amongst others, included La Kaffa sending a notice dated 5 January 2017 to shopping mall owners stating that all the agreements between Loob and the shopping mall owners regarding the Chatime franchise business "shall be null and void".

The Court of Appeal

On 27 June 2018, the Court of Appeal unanimously reversed the decision of the High Court and allowed La Kaffa's application for an interim prohibitory injunction. In brief, the reasons given by the Court of Appeal were:

- (a) a simple construction of Article 15 of the RERA as well as Section 27 of the FA demonstrates that there is an obligation for Loob not to compete with La Kaffa's business even after the termination of the RERA;
- (b) when parties have agreed not to do certain acts and a statute (in this case the FA) also provides for such protection, the court is obliged to give effect to ensure the salient terms of the agreement as well as the statute is not breached;
- (c) the possibility that the Tealive business consisting of 161 outlets and the livelihood of 800 employees of Loob will be affected is not a justifiable reason to refuse the prohibitory injunction when the complaint of La Kaffa in crude terms is that Loob has changed the name of the business of 'Chatime' overnight and is now running the business under 'Tealive'.

The Court of Appeal went on to say that the conduct of Loob on the face of the record is not only in breach of its legal obligations related to restraint of trade but also a breach of franchise law which does not encourage criminal or tortious conduct of business, goodwill, etc.

The Stay Application

Loob first filed an application to stay (i.e. suspend) the Court of Appeal order dated 27 June 2018, pending the disposal of Loob's application for leave to appeal to the Federal Court. This application was rejected by the Court of Appeal on a 2-1 majority basis on 5 July 2018. However, on 16 July 2018, Loob's stay application was allowed by the Federal Court.

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What Happens Next

The next step will be the hearing of Loob's application for leave (i.e. permission) to appeal to the Federal Court. The test for determining whether leave will be granted is that:

- (a) the applicant must have raised a question of general importance not previously decided by the Federal Court; or
- (b) such decision requires further argument and a decision of the Federal Court is to the public's advantage.

Loob will also need to create a "first impression view" that the appeal might succeed.

(We refer to the case of *Terengganu Forest Products Sdn Bhd v. COSCO Container Lines Co Ltd & Anor & Other Applications* [2011] 1 CLJ 51 FC.)

Conclusion

The La Kaffa-Loob battle is just heating up. In the event that the Federal Court dismisses Loob's application for leave to appeal, or if the Federal Court allows the leave application but dismisses the appeal itself, then Tealive would have to close down until the conclusion of the Singapore Arbitral Proceedings.

We trust that the above provides you with a succinct update on this dispute as well as a general overview of injunctive relief. Should you require any assistance or clarification in respect of the above or in relation to any other aspect of injunctive relief, please do not hesitate to contact us.

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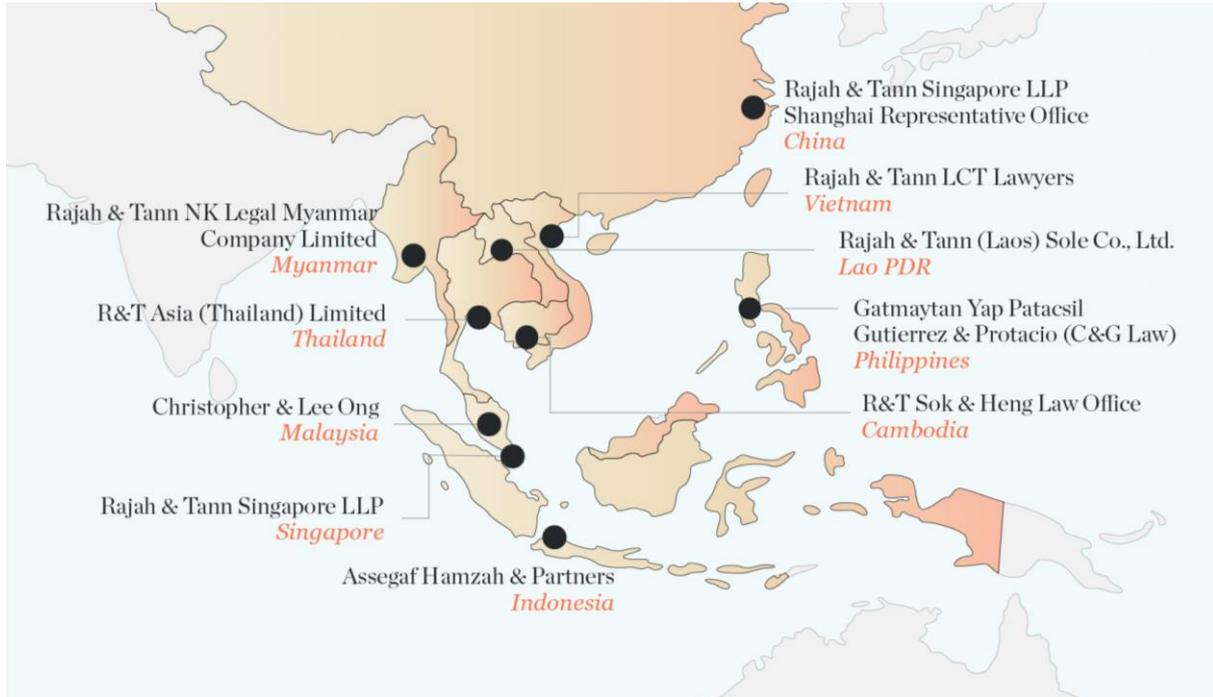
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