

## FREE FRANCHISE FEE AND ROYALTY PAYMENT IN ISLAMIC FRANCHISE VIA *TA'AWUN* CONCEPT

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**Abstract:** *This paper is an exploratory study aims to offer the franchise industry with Islamic based franchise system through ta'awun (mutual cooperation) concept. The feature of Islamic franchise proposed is a free franchise fee and royalty payment basis. The paper used qualitative approach through in-depth interview of franchisors as purposive sampling respondents. The paper reveals that ta'awun (mutual cooperation) in Islamic franchise could be achieved through musharakah contract. This finding gives insight ideas on how free fee-based franchise could be implemented in the future which benefited the franchise industry, particularly the franchisor and franchisee which opt for an alternative in a franchise business.*

**Keywords:** *Franchise fee, royalty, Ta'awun, Musharakah, Islamic Franchise*

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### Introduction

Franchisor enjoys profit through initial franchise fee and royalty paid by the franchisee along with the bound contract. Initial franchise fee and royalty payment act as an income to the franchisor and in most cases, it is considered as a compulsory fee (Pandaa, K. Paswana, & Sailendra P. M, 2018; Frazer, 1998; Kotliarov, 2011). In other words, the franchisor in most cases will receive royalty, and in return, the franchisor assists the franchisee with supervision and training. On the other part, franchisee act as a financial provider in the form of payment on a particular cost and granted an authority to use franchisor's trademark, type and business system (M. Mendelsohn, 1995).

The relationship occurs between franchisor and franchisee seems much like a partnership where it encourages of cooperative behaviour, commitment and helping each other to aim for victory in the business as both partners are sharing the same business. The success of the franchise business depends on the quality of the relationship between franchisor and franchisee. Factors such as trust, genuine commitment, excellent communication and relationship satisfaction contribute to the success of franchise business (Adams Adeiza, Noor Azizi Ismail, & Marlin Marissa Malik, 2017; M. Victoria Bordonaba-Juste & Yolanda Polo-Redondo, 2002; Rahatullah & Raeside, 2015; M. Khairi Ishak, 2016). However, there was limited study on the concept of Musharakah in franchise. Only one study found in Indonesia. The concept is practised by Jarimatika Darussalam (Nurjannah MR & Nazaruddin A. Wahid, 2013). However, the practice is not purely reflect Musharakah contract as the practice of fee and late payment of royalty is still been imposed.

Thus, this paper aims to deliberate how the concept of *ta'awun* in a franchise can create a free fee and royalty-based franchise system through *musharakah* contract.

## Literature Review

This literature review will briefly discuss on the concept of Musharakah and *ta'awun* mutual cooperation).

### Musharakah

Musharakah is an Arabic word derived from “*syarika*” which denotes the meaning of partnership. The word *syarika* later forms *syirkah* and *syarikah*. In term of language, *syarikah* carries the meaning of to be allied or company. After the evolution of the word, *syirkah* or *syarikah* comprises the meaning of merger of members or partnerships or inclusion. This title also is the most accepted fluent designation (Ibn Manzur, 1956). *Syirkah* means mixing one of the usufructs with other usufructs until they are undistinguished between them (al-Jaziri ' .-R. , 1986). While *jumhur* scholars use the term “*syarikah*” to the contract designated to company even no shares were mixed, because the contract is the cause of to the mixing (al-Zuhaili, 1996).

Generally, *syarikah* is divided into two categories which is based on property (*syarikah al-amlak*) and contract (*syarikah al-'uqud*). *Syarikah al-amlak* is an ownership between two or more members without *syirkah* contract. It occurs mainly duet o inheritance of the estate, *hibah* or purchasing. While *syarikah al-'uqud* occurs between two or more members which involving capital and profit with the pronunciation of doing *syarikah* among them (Sarakhsi, 1978; Ibn al-Human, 1995). Generally, Shafi'i views that *syarikah* is divided into four parts namely *syarikah al-'inan*, *syarikah al-mufawadah*, *syarikah al-abdan* and *syarikah al-wujuh* (al-Nawawi, 1996; Syarbini, 1958). Among the four, Syafi'i only allowed *syarikah al-'inan* while the others denied it (al-Syirazi, 1959). This shows that Syafi'i scholar is vigilance in their view on the issue. The reason is majority of Syafi'i scholars tend to look on the concept of *syarikah* from *tasarruf* (management authority) on something clear and real rather than other aspects.

*Syarikah al-'inan* occurs between two or more members pronounced a contract with capital to form a *syarikah* in running a business. The profit distribution is according to the ratio of capital distributed with agreed conditions. Each member is conditionally required to pronounce pronunciation which shows the permission to conduct management (*tasarruf*) and if it is limited to *syarikah*, it is considered as invalid (Jaziri, 2001; Syarbini, 1958).

While according to Hanafi scholars, this similar *syirkah* concept known as *syarikah al-amwal*. It is an agreement occurs between two or more members contribute their aset as capital for investment purposes through work done by them. Each of the member will be rewarded from the future profit as been agreed and determined between them (Kasani, 1998; Sarakhsi, 1978). Generally, mutual consent between the two or more parties involve formed *syarikah al-amwal* through number of capitals invested to be traded, and the profit or loss therein is shared between them. *Syarikah al-amwal* in the form of *al-'inan* has been practised before Islam. It was recorded that the Quraish people shared their property and some rights or demands based on this *syarikah* (Kasani, 1998; Sarakhsi, 1978). However, the Maliki scholars disagree with the term *al-'inan*. According to Ibn Rusyd, majority of scholars agree with its validity but in different opinion on its rules (Ibn Rusyd, 2000).

In Musharakah context in Islamic franchise, the franchisor is required to contribute his business capital to start a franchise business together with the franchisee as his partner. The reason is due to the condition of a valid musharakah contract, each party is required to contribute a sum of capital in the form of a visible property. In this context, it is a currency that is used as a business capital. Loss and profit will be calculated based on the business capital. In applying the Musharakah contract in the franchise business, *Syirkah al-'inan* is considered to be suitable with the nature of franchise business. *Syirkah al-Inan* occurs when two or more parties agree to contribute capital or property to collectively run a business and its profits is divided among them (M. Nasri Md. Hussain, Nasri N., & M. Solehudin Shuib, 2013). Generally, *Syirkah al-Inan* is recognized by *fuqaha'* once the terms and conditions are fulfilled, namely, when all the capital between the partners has been mixed so that it can no longer be recognized and the profits between them are divided according to their respective capital ratio. Uniquely, the amount of capital contributed is not necessarily should be equal. Generally, the capital contributed by the partners is in the form of currency.

On contrary, *syirkah 'inan* is also valid if one of the parties contribute his capital in the form of intangible assets which is valued in the form of a currency. In this context, business names, corporate names, trademarks, literary expenditures, creations or inventions are considered as intangible asset which owes its financial value which can be buy and sold. These rights are recognized by the Shariah and should not be violated (Bouheraoua, Mohamad, Kasri, & Abdullah, 2015). For more clarity, one party (franchisor) can contribute his capital in the form of an intangible asset after the asset is valued in the form of currency value, while the franchisee contributes a certain amount of capital in the form of currency. In this state, the agreed division of profit between the parties is more just and transparent (mutual consent). Parties involved in *Syirkah al-'Inan* may agree to contribute an equal amount of capital but not on the profit distribution. The profit distribution ratio is based on the approval of parties involved, while for the loss is according to the ratio of contributed capital (al-Zuhaili, 1996).

### **Ta'awun (Mutual Cooperation)**

Collaboration and cooperation are developed through partnerships. Based on a study by Yliia Halynska (2017), collaboration is the most transparent form of interaction of economic entities compared to other forms of partnership. On the other hand, similar forms of interaction such as collaboration and cooperation have some differences in their formulation of objectives, form of communication and presence of competition (Yliia Halynska, 2017). Following that, good collaboration and cooperation will develop good teamwork. Good teamwork in partnerships inspires individuals within the group to boost the positive capability on an emotional level, confidence and the ability to plan and decide with others. In addition, it promotes a dynamic and healthy work environment with a workable agenda, creative activities, strategies and positive values (Mafizatun Nurhayati, Onggo Pramudito, & Ermawati Ermawati, 2018; Shouvik Sanyal & M. Wamique Hisam, 2018; Sheeba Khan & Layal Said Al Mashikhi, 2017).

Alternatively, the concept of *ta'awun* (mutual cooperation) implies the meaning of helping each other which encompasses to the concept of cooperation. The concept of cooperation also comprises the meaning of collaboration, group effort, support and mutual aid (Siddig Ahmad, 2012). The concept of *ta'awun* can be found in the holy Qur'an. All efforts that are meant to achieve goodness and piety as well as to avoid sin and enmity is considered as *ta'awun*. Allayh says in the Qur'an:

وَتَعَاوَنُوا عَلَى الْبِرِّ وَالتَّقْوَىٰ وَلَا تَعَاوَنُوا عَلَى الْإِثْمِ وَالْعُدْوَانِ وَاتَّقُوا اللَّهَ إِنَّ اللَّهَ شَدِيدُ الْعِقَابِ ٢

“...and help one another in goodness and piety, and do not help one another in sin and aggression; and be careful of (your duty to) Allah; surely Allah is severe in requiting (evil)”

(al-Maidah 5:2)

The above verse stressed on the importance of mutual help among each other to achieve goodness which benefits individual and society. The synergy of collective mutual help and cooperation in producing something within a group rather than individual resulting higher positive achievement (Ab. Aziz Yusof, 2010).

Further, the concept of *ta'awun* is associate with the element of *taqwa* which enhance strong moral and spiritual level of an individual to cooperate in goodness, consideration and justice in society. *Ta'awun* concept which is blended together with *taqwa* is the central key element to all forms of *'ibadah* which aims only to seek for Allah's blessing.

Similarly, the partnership concept of *musharakah* resembles the concept of *ta'awun*. It is common to see the practice of partnership in human life. It is very common when sharing occurs in the field of *Muamalat*. Humans are in the same order to facilitate the business of each other. In the context of *musharakah*, partnership and sharing practices are the central nerve which form *ta'awun*. The objective of *musharakah* which is based on justice and equality are urgently required to achieve mutual agreement which leads to goodness, not only to parties involved but benefits also to others. Allay says in the Qur'an:

وَإِنَّ كَثِيرًا مِّنَ الْخُلَطَاءِ لَيَبْغِي بَعْضُهُمْ عَلَىٰ بَعْضٍ إِلَّا الَّذِينَ ءَامَنُوا وَعَمِلُوا الصَّالِحَاتِ وَقَلِيلٌ مَّا هُمْ  
“and indeed, most of the partners act wrongfully towards one another, except for those who believe and do righteous deeds, and very few are they”

(Saad 38:24)

The above verse explains that the partnership is form when the parties involved combine their property or capital or labor or creditworthiness together to share for profit, while the loss is according to their contributed ratio. The mixing of the property between the parties is difficult to be distinguished from each other (M. Ayub, 2007). Therefore, *musharakah* contract applies the concept of *ta'awun* where there is a concept of mutual cooperation when the parties involve collectively share and combine their property to form *musharakah*. In franchise context, the franchisor and the franchisee collaboratively work together in conducting the franchise business by contributing their capital until it cannot be distinguished from each other to earn profits, while loss is accordance to the capital ratio contributed.

## Methodology

This study uses qualitative research due to the objective of the study to explore how the concept of *ta'awun* in a franchise can create a free fee and royalty-based franchise system through *musharakah* contract. The study interviews five experts (academician and experts in *muamalat* and franchise officer) and six franchisors as the purposive sampling respondents from various franchise sectors namely Islamic pawning, dialysis centre, food and beverage, education and health care sector. The respondents choose were based on religion, expert in the area and for franchisor, the duration of practicing franchising and availability were considered as the criterion. Each interview consumed between 30 minutes to 50 minutes with note-taking and the conversation was recorded, and later transcribed. The data was later analysed using thematic analysis.

## Result

Result obtained from the interview is arranged based on theme namely no fee and capital in *Musharakah*.

### *Fee in franchise Musharakah*

Franchise fee was paid to franchisors as a form of return from franchisees on the use of trademark, system, and others that belong to the franchisors. For further discussions, table 1 below shows the findings of the interview with franchisors on franchise fee in Musharakah.

**Table 1: Franchise fee from franchisor’s view**

<b>Respondent</b>	<b>Findings</b>
RF1	- Not in the interview dialogue.
RF2	- Not in the interview dialogue.
RF3	- Not in the interview dialogue.
RF4	- No fee as Musharakah concept applied. - Different franchise concept as no fee is imposed.
RF5	- Not in the interview dialogue.
RF6	- The fee concept is abolished when musharakah is utilized.

To bring forth the musharakah contract proposal in the franchise system, the first information obtained from RF6 is that the musharakah contract is feasible, but it is different from the existing franchise contracts as no fee is imposed. This is expressed in his opinion: *“It means that in the agreement, I do not impose a fee but later on when there is a profit, we will have the concept of Musharakah. To me, I think there is no problem.”*

This opinion is supported by RF4 and according to him, this concept is more similar to a partnership:

*“To me, this is not a franchise concept...no...which means no initial capital, to pay a fee of RM50,000...not required ...what is the point of paying a fee of RM50,000...”*

*“Menara provides a certain portion of capital, the other person also provides a portion of capital...we collaborate, using the name of Menara. That is a joint-venture...”*

### *Capital in Musharakah*

In the practice of musharakah context, franchisors and franchisee should contribute capital before starting the franchise business. This form of cooperation involves *ta’awun* (cooperation) concept. The findings from the interview with the experts and franchisors on the matter was shown in the table 2 and 3 below.

**Table 2: Capital in Musharakah from the experts’ view**

<b>Respondent</b>	<b>Findings</b>
RP1	- Each partner contribute capital. - Management has value.
RP2	- Capital can be tangible and intangible form where intangible capital is any consideration which is deemed as reasonable. - Franchisor may contribute capital in non-financial form.
RP3	- Brands and trademarks has value. - <i>Iktisas</i> (knowledge, expertise, capability, trust, and ability) are intangible assets that can be considered as capital. - Franchisor may contribute capital in non-financial form.

RP4	<ul style="list-style-type: none"> <li>- Goodwill can be considered as intangible capital.</li> <li>- Training provision and branding by a franchisor can also be considered as the franchisor’s capital.</li> </ul>
RP5	<ul style="list-style-type: none"> <li>- Intangible asset can be as capital.</li> </ul>

**Table 3: Capital in Musharakah from franchisors’ view**

Respondent	Findings
RF1	<ul style="list-style-type: none"> <li>- Capital in a form of volume.</li> </ul>
RF2	<ul style="list-style-type: none"> <li>- Not in the interview dialog.</li> </ul>
RF3	<ul style="list-style-type: none"> <li>- The value of goodwill is subjective.</li> <li>- Franchisor’s capital in non-financial form whereas franchisee in financial form.</li> </ul>
RF4	<ul style="list-style-type: none"> <li>- Franchisor’s capital in non-financial form whereas franchisee in financial form.</li> </ul>
RF5	<ul style="list-style-type: none"> <li>- Not in the interview dialog.</li> </ul>
RF6	<ul style="list-style-type: none"> <li>- Not in the interview dialog.</li> </ul>

In terms of capital contribution, RP1 is of the view that each partner should make a capital contribution. According to RP1: *“If it is a real musharakah, it would not be a problem if it is a real musharakah. It means a real musharakah, the responsibility is...based on capital. It means joint capital.”*

In RP2’s opinion, capital can be tangible and intangible as mentioned in RP2’s following statement: *“In terms of capital valuation, that’s right. It is even mentioned in the act, any consideration. Not necessarily in RM form. Whether in the form of labour man-hour, it’s up [to the parties].”*

RF1 stated that the capital contribution must be in the form of volume or something that can be quantified. RF1’s view is expressed as: *“His capital but it needs to be in the form of volume. Volume means quantity.”*

RP4 stated that goodwill or customer confidence in a person or a brand is an asset and can be used as intangible capital but must be appraised by a valuer to determine its volume or amount. RP4’s opinion is as follows: *“It is important to make a valuation of the intangible assets to derive their values before signing the musharakah-based franchise agreement.”*

This matter was also mentioned by RP5, as follows: *“It is possible, let say to create a franchise as a Musharakah, the person who did the branding will get the value of his brand appraised...and appraised by a certified valuer.”*

According to RP3, a partnership in brands and trademarks owned by a franchisor benefits the franchisee: *“So his copyright is used. So it is as if he gets the benefit. Since people would say the example of KFC, then KFC it is. So, he is going to benefit.”*

In addition to goodwill, RP3 is of the view that knowledge, expertise, capability, trust, and ability are intangible assets that can be appraised which RP3 referred to as *ikhtisas*. All of these items can be considered as the franchisor’s capital contribution. According to RP3: *“Because when we look at it, it is in the matter of ikhtisas. When it is ikhtisas, which are skills, expertise, then it is appreciated.”*

Meanwhile, RP1 is of the opinion that management has a value, as mentioned in the following statement by RP1: *“Management has a value, just as capital has a value.”*

RP4 gave an example that training provision and branding by a franchisor can also be considered as the franchisor’s capital. RP4’s opinion is as follows: *“In a conventional franchise model, the franchisor provides appropriate training and brands that can be considered as the franchisor's capital contribution in forming the partnership.”*

Meanwhile, RP2 stated that in the act, intangible capital is any consideration which is deemed as reasonable, as follows: *“In terms of capital valuation, that is right. It is even mentioned in the act, any consideration. Not necessarily in RM form. Whether in the form of labour man-hour, it is up [to the parties].”*

However, RF3 stated that the valuation of an intangible asset such as goodwill and expertise is quite difficult and subjective. According to RF3: *“so the valuation of goodwill is actually an opinion, his [the valuer’s] opinion and all, that’s why it is called creative accounting in the accounts, it is more on creativity, so that is my opinion, subjective, very subjective.”*

Meanwhile, RP2 agreed that it is not impossible to implement the Musharakah-based franchise as long as the franchisor does not contribute capital in the financial form. According to RP2: *“Theoretically, it is possible to implement it that way as long as the franchisor is not seen to invest directly in the franchise business.”*

RP3 also agreed for the franchisor to contribute only in non-financial forms in the franchise business:

*“But do not see it in physical terms only, but sometimes the non-physical, the intangible, has a great impact. So, the impact, ikhtisas, expertise. All are humans, but trust, abilities, capabilities and so forth. Therefore, we now accept that knowledge learning is the main asset. So, the expertise is already there.”*

RF4 agreed with RF3 on this matter through the following statement: *“I share without [contributing] capital, which means not in financial [terms]. Non-financial, material with non-material, you in material [form], me in non-material [form]. I agree if it is that way.”*

## **Discussion**

The implementation of Musyarakah in franchise context is unique and differs from the current franchise being practiced. This is because the possibility of several types of fees practiced now can be abolished or reduced as been stated by RF2 and RF6. Through the Musyarakah contract, the present fee will be translated in the form of profit and loss sharing. For example, if a joint agreement between franchisors franchisees has been established at the beginning of the Musyarakah such as the repeal of the initial fee and the advertising fee, the franchisees will no longer require to pay any fees to franchisors. This situation was replaced by the proportion of profits and losses in the partnership of the franchise business. The finding was also supported by the practice of the Musyarakah franchise in Indonesia by Jarimatika Darussalam. The concept of profit-sharing distribution is practiced as a mechanism to accommodate operating fees and royalties. Through Musyarakah contract, 15% from profit earned will be paid for operating cost and royalty, and the balance will be divided by a ratio of 40% to franchisors and 60% to franchisees (Nurjannah MR & Nazaruddin A. Wahid, 2013). The concept of *ta’awun*

between the franchisor and the franchisee can be seen where both parties agreed to mutually cooperate in the franchise business to share for profit and loss.

Further, despite of capital combination in Musharakah, *ta'awun* also comprises the element of mutual aid and assistance between franchisor and franchisee. As partners, franchisor will provide mutual assistance to franchisee as franchising involving both of them. A part from the mutual aid and assistance supported to franchisee are advertisement, promotion and training. All these considered as intangible capital contributed by franchisor to conduct the franchise business. Intangible form of capital in franchise such as trade name, corporate name, literature production, invention or discovery, are the properties own legally by its owner and has a financial value. These rights are recognized by the Shariah law (Bouheraoua, Mohamad, Kasri, & Abdullah, 2015). On the other hand, franchisee is required to contribute his capital in financial form. The matter is agreed by all respondents from the experts and few franchisors such as RP1, RP2, RP3, RP4 and RP5 and few franchisees such as RF1, RF3 and RF4. This situation seems to be fair and just to franchisors as they are more expert in the business area compared to franchisee. Besides, a successful franchise business which started from the bottom which is full of risk and challenges until the current state of victory was successfully managed by the franchisor. Hence, it is admissible to take into account all forms of cooperation such as advertising, promotion and training from the franchisors to the franchisees as his sole capital contribution as they can be evaluated in financial form. The volume of capital contributions in this form must be evaluated accurately and obtain the mutual consent from all parties involved to avoid any future dispute in determining the percentage of profits and losses proportion between them.

Furthermore, the practice of *syirkah 'inan* do not require for equality in terms of capital, management (*tasarruf*) and profit sharing as previously stated. Therefore, it is possible that the amount of capital contribute by the franchisor is greater than the franchisee. This is due to the franchisor who already has his own business and through franchising, the franchisor is able to grow its business with capital which is not 100% from him. As a result, the franchisor is not burdened with the financial matter in providing cash capital. This situation also indirectly coincides with the general characteristics of the franchise where the franchisor wants to grow its business without having to invest his own capital.

## Conclusion

This research concludes that *ta'awun* (mutual cooperation) in Musharakah franchise between franchisor and franchisee can be an alternative contract to those who opt for Islamic franchise contract. In Musharakah franchise contract, the fee-based structure is no longer applicable as it has been substituted with capital-based and loss sharing structure. Franchisor and franchisee as partners are required to help each other to conduct the business through *ta'awun* concept where capital contribution is the main central to validate musharakah contract. Besides, the concept of *ta'awun* in musharakah required each partner to form collaboration, group effort, support and mutual aid in order to sustain and achieve for the business victory and the pleasure of Allah.



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