1. Introduction

Minter Ellison welcomes the opportunity to provide submissions to the Review of the Franchising Code of Conduct (**Review**).

These submissions respond to certain issues identified in the Discussion Paper: Review of the Franchising Code of Conduct[1] (**Discussion Paper**).

Although these submissions only deal with some of the issues identified in the Discussion Paper, it is acknowledged that all of the issues raised are important issues facing the franchising sector and are worthy of detailed consideration by the Review.

However, it also must be kept in mind that the Review is a scheduled review of the Code. Its purpose is to assess the recent batch of changes made to the Code. Given the recent amendments, combined with the comprehensive recent changes to the *Competition and Consumer Act 2010* (Cth) (**CCA**), further changes should only be recommended where a clear and compelling reason is identified – we caution against adopting a 'change for change's sake' approach.

For this reason, the overall tenor of our submission is that, on the whole (and with the exception of the foreign franchise exemption and certain interpretational issues), we advocate for the status quo of franchising regulation to be maintained.

2. Executive summary

Minter Ellison submits that:

(a) an express obligation to act in good faith should not be inserted into the Code;

(b) the current enforcement regime is adequate and we oppose extending the application of any fine-based remedy to a breach of the Code;

(c) the foreign franchisor exemption should be reinstated. However, if the exemption is not reinstated, the disclosure requirements for foreign franchisors should be streamlined;

(d) the Code in its current form adequately addresses concerns about end of term arrangements, in particular non-renewal of franchise agreements and whether compensation should be paid for goodwill;

(e) the level of disclosure made by franchisors is sufficient and should not be increased; and

(f) the ongoing interpretational issues associated with the Code need to be addressed.

[1] Department of Industry, Innovation, Science, Research and Tertiary Education (Cth), *Discussion Paper: Review of the Franchising Code of Conduct* (January 2013) (*Discussion Paper*).

3. An express obligation to act in good faith should not be inserted into the Code.

3.1 Imposing an 'overarching obligation to act in good faith' creates inconsistencies with the current state of the law.

It is submitted that, given the state of uncertainty about the law of the implied duty of good faith, now is not the time to be seeking to create new, quasi-statutory good faith rights and obligations.

The nature and extent of the implied duty of good faith was recently described by the Attorney-General's Department in the discussion paper titled *Improving Australia's Law and Justice Framework*[2] as being *'controversial'*[3]. We agree with this description.

A major area of uncertainty is that of the contractual basis for the duty.

One of the earliest key decisions in Australia to deal with this issue was that of *Renard Constructions (ME) Pty Ltd v Minister for Public Works*.[4] In *Renard*, Justice Preistley, after commenting on international developments in the area,[5] stated that:

> *The result is that people generally, including judges and other lawyers, from all strands of the community, have grown used to the courts applying standards of fairness to contract which are wholly consistent with the existence in all contracts of a duty upon the parties of good faith and fair dealing in its performance. In my view this is in these days the expected standard, and anything less is contrary to prevailing community expectations.* [6]

Cases subsequent to *Renard* have attempted to deal with not only the circumstances in which a duty of good faith will be implied into agreements, but also the scope of any such duty.

In certain decisions, the duty has been implied on the basis of the parties' presumed intention; that is, an implication in fact. Such an approach requires a court to examine the agreement in question to determine whether, in all the circumstances, it is appropriate and was intended by the parties that a duty be imposed.

In *Esso Australia Resources Pty Ltd v Southern Pacific Petroleum NL (recs and mgrs apptd) (admins apptd),*[7] Justice Buchanan commented that the application of the duty of good faith is *'perhaps [an] ad hoc implication... rather than implication as a matter of law creating a legal incident of contracts of a certain type'*.[8] Importantly, his Honour noted that in some contracts, it *'may be appropriate... to import such an obligation to protect a vulnerable party from exploitive conduct which subverts the original purpose for which the contract was made'*.[9] However, his Honour observed there may also be contracts where such a term would be inappropriate. Justice Buchanan was therefore reluctant to conclude that *'an obligation of good faith applies indiscriminately to all the rights and powers conferred by a commercial contract'*.[10]

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[2] Attorney-General's Department (Cth), *Improving Australia's Law and Justice Framework: A discussion paper to explore the scope for reforming Australian contract law* (2012) (*Improving Australia's Law and Justice Framework*)
[3] *Improving Australia's Law and Justice Framework,* 24.
[4] (1992) 26 NSWLR 234 (*Renard*).
[5] *Renard*, 263 – 286.
[6] *Renard*, 269.
[7] [2005] VSCA 228 (*Esso*).
[8] *Esso*, 27 (Buchanan J). His Honour held it was not necessary to determine if there was an implied term of good faith in that case, as even if there were such an obligation, it had not been breached: see 27.
[9] *Esso*, 24 (Buchanan J).
[10] *Esso*, 25 (Buchanan J).

In the same case, Chief Justice Warren noted that *'where commercial leviathans are contractually engaged, it is difficult to see that a duty of good faith will arise'*.[11] Her Honour relevantly held that there was no vulnerable party and therefore there was no implied term in the case before her.[12]

Other decisions resolved the basis for the implication as being an implication by law into all 'commercial' contracts (if not all contracts).[13] Such an implication does not depend upon determining the presumed intention of the parties; rather it, in effect and as a matter of policy, involves the imposition of legal duties on contracting parties.[14] Although certain decisions resolve the issue as one of an implication of law, it is submitted that recent decisions evidence a trend towards the view that the duty must be implied in fact (and on a case by case basis).[15] At a minimum, it cannot be said that there is consensus for either approach across all jurisdictions in Australia.

It is submitted that implication in fact is the more preferable approach. This approach ensures that the bargain struck between the parties is preserved and given effect to.

In the franchise context, courts have been prepared to imply a term to act in good faith in franchise agreements, whether in fact or in law (as a class of commercial contracts).[16] As these decisions make clear, the nature of a franchise agreement is such that a court is more likely than in other circumstances to imply a duty to act in good faith, principally because of the typical disparity in bargaining position between the parties to a franchise agreement. However, it cannot be said that in *all* cases there will be such a disparity. Many franchisees are sophisticated and well resourced. Given the advice certification requirements in the Code,[17] many franchisees will have had the benefit of legal advice prior to entry into the agreement.

It is submitted that it cannot be said that in every instance, a franchisee is vulnerable to exploitative conduct such that the duty must be *'indiscriminately'* implied (to use Justice Buchanan's language in *Esso*). Given the sometimes nebulous nature of the duty, this flexibility is an important limitation and proper acknowledgment that a 'one size fits all' approach is inappropriate. Moreover, reference is made to the comments of Gleeson CJ in *Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd,*[18] who observed that:

> *One thing is clear ... [a] person is not in a position of relevant disadvantage, constitutional, situational, or otherwise, simply because of inequality of bargaining power. Many, perhaps even most, contracts are made between parties of unequal bargaining power, and good conscience does not require parties to contractual negotiations to forfeit their advantages, or neglect their own interests.*

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[11] *Esso*, 4 (Warren CJ).
[12] *Esso*, 5 (Warren CJ).
[13] See, for example, *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349 at 368-369; *Burger King Corporation v Hungry Jacks Pty Ltd* [2001] NSWCA 187, 163 – 164 and *Garry Rogers Motors (Aust) Pty Ltd v Suburu (Australia) Pty Limited* [1999] FCA 903.
[14] see *Australis Media Holdings Pty Ltd v Telstra Corporation Ltd* (1998) 43 NSWLR 104 at 123.
[15] See, for example, *Vodafone Pacific Ltd v Mobile Innovations Ltd* [2004] NSWCA 15 at [191], *Esso*, *Tote Tasmania Pty Ltd v Garrott* (2008) 17 Tas R 320 at [16], *Driveforce Pty Ltd v Gunns Ltd (No 3)* [2010] TASSC 38 at [12], *Starlink International Group Pty Ltd v Coles Supermarkets Australia Pty Ltd* [2011] NSWSC 1154 at [18].
[16] See, for example, *Burger King*, *Garry Rogers*, *Far Horizons* [2000] VSC 310, *Bamco Villa Pty Ltd v Montedeen Pty Ltd; Delta Car Rentals Aust Pty Ltd v Bamco Villa Pty Ltd* [2001] VSC 192, *J F Keir Pty Ltd v Priority Management Systems Pty Ltd (Administrators Appointed)* [2007] NSWSC 789, *Meridian Retail v Australian Unity Retail Network* [2006] VSC 223 (although, because no breach could be established, Dodds-Streeton J elected not to decide whether the implication should be made).
[17] see section 11 of the Code.
[18] (2003) 214 CLR 51 at [11]

Although made in the context of unconscionable conduct, his Honour's comments are relevant here – the mere fact that there will, in many cases, be an inequality of bargaining position between a franchisor and franchisee does not justify the mandatory implication of the duty into all franchise agreements. Rather, it is submitted that the more preferable approach is for the existence, scope and application of the duty be determined on a case by case basis.

It might be argued that by drafting a right into the Code, the uncertainty in the common law position as outlined above would be clarified. Four points are made in response:

(a) firstly, the development of this area of law is best left to the common law and the courts which, in the usual way, will provide the flexibility to develop to meet changing business practices and circumstances;

(b) secondly, the imposition of the duty in every franchise agreement would amount to, in effect, an imposition at law. Such an approach is contrary to, it is submitted, the trend of common law development, namely, that the duty to act in good faith is treated as an 'ad hoc' or factual implication (although it is accepted that there is no settled approach, one way or another). In this regard, the comments of Justice Gummow (sitting in the Federal Court) remain relevant:

> *The implication of a term by operation of law, applicable across the whole spectrum of the law of contract, is a major step. Further, in deciding to take any such step it is now idle to speak to 'the law of contract' without a real appreciation of the deep impact in Australia of various statutory regimes, one of which, of course, gives rise to a most substantial body of work in this court, and has done so now for many years;*[19]

(c) thirdly, the fact that there is uncertainty does not justify the mandatory imposition of the duty in all franchise agreements, in circumstances where there is little empirical evidence that the uncertainty causes any tangible problems in the franchising sector; and

(d) fourthly, as noted in the Discussion Paper, enshrining the duty in the Code may address the uncertainty as to the basis for the implication, but it is unlikely to (nor should it attempt to) address the uncertainty as to the scope of the duty. Parties will still need to have recourse to the courts to determine whether the conduct in question breaches the duty to act in good faith.

In our view, section 23A of the Code is sufficient and effective at addressing concerns regarding conduct that would breach an obligation of good faith. As it is intended, section 23A highlights to franchisors and franchisees that there is an obligation at common law of good faith that could apply. It also operates to alert parties to their ability to seek redress should they consider there has been a breach. However, it does not state (quite correctly) that good faith will apply equally in all cases or encourage parties to act without considering their commercial position, their legal rights or seeking appropriate advice.

3.2 An express obligation of good faith would increase confusion regarding the obligations of members of the franchising industry.

As outlined above, the application of an implied term of good faith will differ depending on the facts of the case. A codified term or duty of good faith may actually increase confusion in the franchising industry about its application and scope.

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[19] *Service Station Association Ltd v Berg Bennett & Associates Pty Ltd* (1993) 117 ALR 393, 407.

In the *Commonwealth Government Response*[20] to the report *Opportunity not opportunism: improving conduct in Australian franchising,*[21] the Commonwealth government rejected the recommendation that a standalone good faith obligation be introduced into the Code as this would increase uncertainty:

> *The law on good faith is still evolving. The scope of the requirement is unclear. From a commercial perspective, uncertainty would be increased by an express statement of the requirement in the Franchising Code. Neither franchisors nor franchisees would be certain of the occurrence of a breach. Indeed it would require court proceedings to establish that.*[22]

Given this uncertainty, an express obligation of good faith is likely to become fertile ground for disputes and, in many cases, will inevitably result in increased litigation. In such cases, any imbalance of power between franchisors and franchisees could actually be exacerbated by litigation.

In addition, a statutory obligation of good faith is likely to add to the sentiment of over regulation in the franchising industry, particularly from the perspective of overseas investors. It may also lead would-be franchisors deciding to pursue a different business model, which would have the effect of decreasing participation in the sector.

To the extent that that the inclusion of good faith in the Code is likely to involve a list of examples, indicia or be expressly defined, the recent comments regarding the codification of unconscionable conduct is relevant. We refer to the report, *Strengthening statutory unconscionable conduct and the Franchising Code of Conduct.*[23] In that report the potential ramifications of codifying unconscionable conduct, including the introduction of a list of examples of such conduct, was noted. It was found that statutory unconscionable conduct can be *'difficult for stakeholders to understand and for the courts to apply, which contributes to a lack of certainty and confidence surrounding the effect of the provisions'.*[24]

In particular, the report cautioned against providing a list of examples of what would constitute unconscionable conduct.[25] It was noted that the possible ramifications of such a list included:

(a) creating a false expectation of those who read the section;

(b) parties could incorrectly believe there has been unconscionable conduct, leading them to invest significant resources in pursuing a case, only to discover that a court finds that the conduct is not unconscionable; and

(c) if a party believes another party's conduct falls within an example of unconscionable conduct, but the other does not, this is likely to be the source of a legal dispute.[26]

Similar issues are likely to arise as a result of the inclusion of an express obligation of good faith.

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[20] Department of Industry, Innovation, Science, Research and Tertiary Education (Cth), *Commonwealth Government Response to the report of the Parliamentary Joint Committee on Corporations and Financial Services, Opportunity not opportunism: improving conduct in Australian franchising* (2008).
[21] Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Opportunity not opportunism: improving conduct in Australian franchising*, December 2008 (*Opportunity not opportunism*).
[22] *Opportunity not opportunism,* 13.
[23] The Treasury and the Department of Innovation, Industry, Science and Research (Cth), *Strengthening statutory unconscionable conduct and the Franchising Code of Conduct* (February 2010) ix. (*Strengthening statutory unconscionable conduct*).
[24] *Strengthening statutory unconscionable conduct,* ix.
[25] see *Strengthening statutory unconscionable conduct,* 22.
[26] *Strengthening statutory unconscionable conduct,* 23.

Equally, the wording noted in the Discussion Paper (which was proposed by earlier reviews of the Code) for the statutory duty of good faith would also cause confusion. The wording previously recommended was as follows:

> *Franchisors, franchisees and prospective franchisees shall act in good faith in relation to all aspects of a franchise agreement.*[27]

It is submitted that this wording goes beyond the obligation that is implied into agreements. Typically, the implied duty of good faith is concerned with the exercise of contractual powers and performance of contractual obligations.[28] Critically, the concept of acting in good faith *'in relation to all aspects of a franchise agreement'* would capture, among other things, pre-contractual dealings Imposing a duty of good faith even before the parties have agreed to a franchise agreement is inappropriate, especially where either party is free to walk away from negotiations at any time (and, in the case of franchisees, can exercise a 7 day cooling off right).

For the reasons outlined above, we submit that the introduction of an obligation to act in good faith would increase confusion for franchisors and franchisees. This would undermine the purpose of industry codes as stated in the *Policy Guidelines on Prescribing Industry Codes* [29] (**Policy Guidelines on Prescribing Industry Codes**). Industry codes are intended to enhance the wellbeing of the Australian people by *'reducing complexity that industry participants or consumers are required to deal with'*.[30] It is our view that the introduction of an express obligation of good faith would actually increase complexity for members of the franchising industry.

3.3 The type of conduct that would amount to a breach of good faith is already caught by other areas of the law.

Conduct that would amount to a breach of a statutory obligation to act in good faith is likely to already be covered by one of the following:

(a) unconscionable conduct;

(b) misleading and deceptive conduct;

(c) the common law duty of good faith; or

(d) a breach of the franchise agreement.

The affected party is therefore able to access a wide range of penalties and remedies, under the CCA and the common law. We submit that it is therefore unnecessary to include an express obligation of good faith in addition to the areas outlined above.

Alternatively, it may be that the introduction of an express obligation of good faith in the Code would be aimed at addressing conduct that is not already included under one of the areas outlined at (a) – (d) above. This would unnecessarily subject the franchising industry to a higher standard of conduct than other businesses. This would place the franchising industry at a comparative disadvantage and would result in 'excessive regulation' of the franchising industry, in breach of the Commonwealth government's stated policy on industry codes.[31]

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[27] *Opportunity not opportunism*, Recommendation 8.
[28] See, for example, *Trans Petroleum (Australia) Pty Ltd v White Gum Petroleum Pty Ltd* [2012] WASCA 165, 150.
[29] The Treasury (Cth) , *Policy Guidelines on Prescribing Industry Codes under part IVB of the Competition and Consumer Act 2010*, May 2011 (*Policy Guidelines on Prescribing Industry Codes*).
[30] *Policy Guidelines on Prescribing Industry Codes*, 6.
[31] *Policy Guidelines on Prescribing Industry Codes* iv.

4. Penalties should not be introduced for breaches of the Code.

26. *Is the current enforcement framework adequate to deal with the conduct in the franchising industry?* 29. *What options are available to businesses to address breaches of the Franchising Code, or any other adverse conduct in the franchising industry?*

4.1 There are already sufficient remedies available to address breaches of the Code.

In our view, the current enforcement framework adequately deals with conduct in the franchising industry. To the extent it is raised, we oppose any extension of the 'fine based' penalties (ie civil pecuniary penalties or infringement notices) for breaches of the Code.

Section 51A of the CCA provides that a corporation must not, in trade or commerce, contravene an applicable industry code.[32] A breach of the Code therefore gives rise to a wide range of penalties and remedies under the CCA. The Australian Competition and Consumer Commission (**ACCC**) is able to enforce these remedies. However, a franchisor or franchisee is also able to access certain of these remedies for breaches of the Code.

The penalties or remedies available under the CCA include:

(a) the ACCC may issue to the public a written notice containing a warning about the conduct (section 51ADA);

(b) injunctions (section 80);

(c) actions for damages (section 82);

(d) court enforceable undertakings (section 87B);

(e) a variety of orders to redress loss or damage suffered by non-parties (section 87); and

(f) non-punitive orders, such as a community service or probation order (section 86C).

The ACCC also has broad investigation powers under Division 5 of the CCA. Many breaches of the Code would form a breach of the franchise agreement, entitling parties to bring a breach of contract claim.

The ACCC does not have the ability to obtain civil penalties for the breach of section 51A of the CCA, but we consider that this is appropriate. The High Court of Australia in *Master Education Services Pty Ltd v Ketchell*[33] noted that the purpose of the Code is to *'regulate the conduct of persons in the franchising industry in order to improve business practices, to provide some protection to franchisees proposing to enter into franchise agreements and to decrease litigation*'[34]. The High Court observed that the law permits a franchisee to seek such relief as is appropriate to the circumstances of the case.[35] There are a variety of remedies available for breaches of the Code that enable a Court to grant relief that is appropriate and proportionate to the loss and damage suffered as a result of that breach.[36]

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[32] *Competition and Consumer Act 2010* (Cth)
[33] (2008) 249 ALR 44 *(Ketchell)*.
[34] *Ketchell*, 25.
[35] *Ketchell*, 39.
[36] *Ketchell*, 39.

The High Court's comments in *Ketchell* reflect the fact that the relationship between franchisor and franchisee is essentially a private relationship between two businesses. The damage that results from the contravening conduct of a franchisor is often limited to damage to the particular franchisee. Conferring additional powers on the ACCC to issue penalties for Code breaches is, in the circumstances, unnecessary and arguably inappropriate.

In our submission, civil penalties should be reserved for circumstances where there is a need for preventing public harm. Conduct properly punishable by the imposition of civil penalties includes the types of conduct already proscribed by the CCA, including:

(a) unconscionable conduct;

(b) false representations; and

(c) anticompetitive agreements (which, in a franchising context, most relevantly arise under section 47 of the CCA, in situations where a franchisor might seek to impose restrictive arrangements with suppliers to the franchise network).

If the powers of the ACCC are to be expanded in relation to the Code, then the focus should be on broadening its audit and educational powers, rather than seeking to punish non-compliance with a Code that was designed to provide protection to private contracting parties, rather than proscribing norms of conduct.

4.2 There is no reason to subject franchisors to an additional range of penalties.

We dispute the proposition that civil penalty provisions are *'necessary in order to ensure that there are consequences for non-compliance with the Franchising Code'*.[37]

First, as noted, there is little evidence to suggest that Code breach gives rise to public harm of the type that might warrant the imposition of civil penalties. To the extent that a party to a franchise agreement has engaged in a Code breach that might give rise to such harm (such as a material breach of a disclosure obligation, or a unilateral action designed to inflict harm on the other party), it is likely to also amount to a breach of other provisions of the CCA (such as the misleading and deceptive conduct or unconscionable conduct provisions), and is properly enforced as a breach of those proscribed norms of conduct.

Second, appropriate consequences already exist for non compliance with the Code. The ACCC has wide ranging investigatory and audit powers to ensure franchisors are complying with the Code. Moreover, if Code non-compliance is detected, the ACCC is able to seek various forms of remedies to ensure that the non-compliance is remedied. The ACCC also has various public warning powers – the force of this responsive remedy should not be underestimated as the public condemnation (which is required to be disclosed to all future franchisees) can have a devastating impact on the future conduct of a franchise operation and acts as a powerful deterrent to potential non-complying franchisors.

Third, we note the proposition in the Discussion Paper regarding the potential of large penalties to have an adverse effect on the viability of a franchisor's business.[38] Regard must be had to the interconnected nature of the franchising industry and the difficulty in penalising one party, for example the franchisor, without a flow on effect to the franchisee. There is a real possibility that adding penalties to the already highly regulated franchise sector in Australia will stunt the

[37] *Discussion Paper,* 29.
[38] *Discussion Paper,* 30.

growth of franchises in Australia. This is particularly the case in relation to overseas investors who already view Australia as being subject to a substantial level of regulation.

4.3 The inclusion of penalties in an industry code is inappropriate and contrary to stated government policy.

The Commonwealth Government's stated policy on penalties in industry codes is that:

> *Industry codes are complementary to general prohibitions on unfair practices that may occur in trade or commerce, and should encourage compliance and focus on remedies rather than simply seeking to punish contraventions.*[39]

It is our view that the introduction of specific penalties for breaches of the Code would undermine this stated policy without good reason.

5. The foreign franchise exemption should be reinstated.

11. *What impact has the removal of the foreign franchisor exemption had on the sector?*
12. *Has the removal of the exemption caused any issues?*

5.1 The foreign franchise exemption was an appropriate concession that should be reinstated.

The exemption for foreign franchises should be reinstated. This was an appropriate concession for disclosure requirements under the Code. In our view, the exemption did not operate to the disadvantage of franchisees or substantially impact the standard of disclosure provided.

The amendment to the Code removing this exemption operates as a disincentive to foreign franchisors considering entering the Australian market. The disclosure requirements result in unnecessary red tape for foreign franchisors as well as additional administrative and legal costs.

We refer to the International Franchise Association's submissions to the 2008 review of the Code.[40] The International Franchise Association submitted that the extension of these regulatory requirements to foreign franchisors has resulted in additional costs *'which must be taken into account by franchisors looking to enter the Australian market'*.[41] This obligation is *'highly burdensome for franchise systems that are not engaged in current sales activity in Australia'*.[42]

We refer to the Policy Guidelines on Prescribing Industry Codes which provide that one key function of an industry code is to *'increase the aggregate output from a particular industry'*.[43] It is our view that the removal of the exemption undermines this function by providing an unnecessary barrier to foreign franchisors considering entering the Australian market. We therefore submit that the exemption should be reinstated.

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[39] *Policy Guidelines on Prescribing Industry Codes* 9.
[40] Matthew Shay and David French (International Franchise Association), *Commonwealth Parliament Inquiry into the Franchising Code of Conduct* (2008) (*International Franchise Association Submissions*).
[41] *International Franchise Association Submissions*, 4.
[42] *International Franchise Association Submissions*, 4.
[43] *Policy Guidelines on Prescribing Industry Codes*, 6.

5.2 If the exemption is not reinstated, there should be reconsideration of the application of the Code to foreign franchisors.

If foreign franchisors remain responsible for giving disclosure under the Code, consideration should be given to a separate regime of disclosure for foreign franchisors. The Code should reflect the significance of the appointment of a master franchisee.

We submit that it is the master franchisee who is better placed to provide the majority of information required in the disclosure document, not only as the contracting party but also with its knowledge of the Australian market. The foreign franchisor, as a foreign company, is often not in a position to provide many aspects of disclosure. For example, it is inappropriate and unreasonable to require a foreign franchisor to provide information regarding unforeseen capital expenditure, as required under clause 13A, Annexure A of the Code. Often the foreign franchisor is not actually in a position to make such disclosure.

However, there are other matters in which the foreign franchisor is better placed to provide information. As things currently stand, the Code requires foreign master franchisors and local master franchisees to provide the same information to a local franchisee. For example, it is reasonable to require a foreign franchisor to provide disclosure regarding intellectual property including the ownership or licensing arrangements regarding intellectual property that the franchisee will have rights to. We submit that the disclosure requirements for foreign franchisors should be streamlined and restricted solely to information that is relevant to the relationship between the master franchisee and the franchisee.

6. The Code in its current form adequately addresses concerns about end of term arrangements, in particular whether compensation should be paid for goodwill and non-renewal of franchise agreements.

6.1 The issues of concern regarding end of term arrangements

The Discussion Paper notes two issues of concern regarding end of term arrangements:

(a) franchisors terminating or refusing to renew franchise agreements when they do not have 'good cause' for doing so; and

(b) lack of clarity or fairness regarding the benefits the franchisee is entitled to when they leave the franchise, in recognition of their contribution to the 'goodwill' of the franchise system as a whole.[44]

We discuss each of these issues in turn.

6.2 Renewal of franchise agreements

We understand that some franchisees have called for an amendment to the Code requiring a franchisor to have 'good cause' if it decides not to renew a franchise agreement. Such an amendment would have the undesirable result of forcing franchisors to renew agreements at the end of term against their will and is contrary to a critical component of the bargain struck between the parties.

Moreover, the effect of such an amendment is that franchisors will be forced to continue to deal with franchisees, against their will and contrary to the principle of freedom of contract. Presumably, such an obligation would be capable of enforcement by Court order (being akin to

[44] *Discussion Paper,* 24.

an order for specific performance of a contract). It is well established that Courts will not make an order granting specific performance of an agreement that requires the maintenance of an ongoing co-operative relationship against a party's will. Justice Dixon has stated that specific performance is *'not a form of relief which can be granted if the contract involves the performance by one party of services to the other or requires their continual cooperation'*.[45]

In our view, by their very nature, franchise agreements require high levels of trust and cooperation. It is therefore inappropriate to compel a franchisor to renew a franchise agreement contrary to its decision not to enter into a second term. Such an amendment would be an inappropriate extension of the Code in breach of an established common law position.

There are likely to be a variety of other ramifications of compelling a franchisor to renew the franchise agreement against its wishes. For instance, it will create a range of difficulties and disputes which would require regular recourse to legal advisers and the Courts. This would increase inefficiency and confusion, contrary to the stated purpose of industry codes.[46] This is also likely to result in increased administrative and legal costs.

The Code has been amended to require the franchisor to disclose the length of the term of the franchise agreement, whether the franchisee will have the option to renew and if so, the process the franchisor will use to determine whether to renew or extend the agreement.[47] These amendments ensure that franchisees are aware of the length of term when they enter into the agreement. Further, the law dealing with misleading or deceptive conduct where the franchisor has misled the franchisee about the length of the term adequately addresses this concern.

In our view, this issue has been adequately addressed and does not require further regulation. In this respect, we note that complaints relating to termination of franchise agreements have decreased since 2010.[48]

6.3 Payment or compensation for goodwill

In a franchise system, the relevant goodwill will usually be the property of the franchisor and will be comprised of the intellectual property, systems, and any marketing plans or procedures that the franchisee is permitted to use. As the principal aspects of goodwill belong to the franchisor, there is no reason why a franchisee should be compensated for the 'loss' of something which it was not entitled to retain.

It is possible for a franchisee to generate its own separate goodwill under a franchise agreement. The franchisee retains this goodwill at the end of the franchise agreement and is able to apply it to a different business or franchise upon the expiry of the term. As the franchisee retains this goodwill, there is no need for a franchisee to be compensated in this regard.

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[45] *J C Williamson Ltd v Lukey* (1931) 45 CLR 282, 298.
[46] *Policy Guidelines on Prescribing Industry Codes*, 6.
[47] The Code, annexure 1, section 17C; annexure 2, section 9C.
[48] see Australian Competition & Consumer Commission, *Small Business in Focus: Small Business, Franchising and Industry Codes Half Year Report* (July-December 2012) 2; Australian Competition & Consumer Commission, *ACCC Report: Small Business, Franchising and Industry Codes* (January – June 2012) 2; Australian Competition & Consumer Commission, *Comparison of franchising and small business complaints and enquiries* (1 January – 30 June 2011) 3.

7. The Code continues to have interpretational issues

We submit that there are ongoing interpretational issues with the Code that must be addressed. These interpretational issues significantly hinder the operation of the Code and should be considered as a priority as part of the review.

The importance of addressing these issues is increased if, contrary to the view expressed above, penalties are introduced for Code breaches. It is unfair to penalise franchisors for failing to comply with the Code where, in many respects, the application of the Code and what it requires of franchisors is uncertain.

We refer to the Policy Guidelines on Industry Codes. Industry codes are to achieve their aims by *'reducing complexity that industry participants or consumers are required to deal with'*.[49] The variety of interpretational issues contained in the Code contribute to confusion between franchisees and franchisors, ultimately increasing the chance of disputes and litigation.

In our view, there are a number of areas of the Code which would benefit from further clarification, which we set out below. However, the issues identified below are what we consider to be the major areas that require clarification.

7.1 Clarify the meaning of 'agrees to termination of the franchise agreement' (section 23(g))

Section 23(g) of the Code provides *'a franchisor does not have to comply with sections 21 or 22 if the franchisee (among others) agrees to termination of the franchise agreement'*.

It is understood that this clause is intended to mean that two parties can reach an agreement at the time of termination on a form of mutual termination. However, does the section allow for parties to agree, at the time the franchise agreement is entered into, on circumstances that will warrant immediate termination? We understand that this is a point of contention for many lawyers and the meaning of the clause is open to different interpretations. This ambiguity should be clarified.

7.2 Clarify the 14 days requirement for when a disclosure document must be given (section 10)

Clause 10 of the Code provides that a franchisor must give a disclosure document at least 14 days before the prospective franchisee enters into a franchise agreement. It is intended that this time requirement starts again, and another disclosure document is required, if there are small changes or amendments made to the franchise agreement?

In our view, this should be clarified to ensure that no further disclosure document will be required in those circumstances. The requirement of a further disclosure document in this regard could operate as a disincentive to franchisors to engage in negotiations with the potential franchisee about amendments to the franchise agreement.

7.3 Remove the reference to transfer (clause 20)

Clause 20 concerns 'transfer or novation of a franchise'. Is it intended for the term 'transfer' to mean the same process as novation? Or is transfer also intended to cover an assignment of a franchise agreement? We submit the clause should be amended to clarify whether 'transfer'

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[49] *Policy Guidelines on Prescribing Industry Codes*, 6.

means 'assignment' and/or 'novation'. Alternatively, it many be that the reference to 'transfer' should be removed entirely.

8. The level of disclosure under the Code is adequate

We observe that the Discussion Paper raises a number of questions about the adequacy of the current disclosure requirements under the Code.

As a general proposition, we are of the opinion that the current level of disclosure is more than adequate. As things stand, the current level of disclosure represents a significant up-front and ongoing cost to franchisors and acts as a significant barrier to entry into the franchise sector for many franchisors. The ongoing cost also creates an incentive for franchisors to re-arrange their business operations so as to fall outside the operation of the Code.

We oppose any recommendation which would serve to increase the disclosure burden on franchisors.

9. Conclusion

For the reasons outlined above, it is our submission that the Code is effective in its current form and should not be amended to include provision for good faith or penalties or alter end of term arrangements. The Code, and the broad legislative regime under the ACL, are sufficient to ensure an appropriate standard of conduct by members of the franchising industry.

We submit that any further amendment to the Code should be considered within the context of the common law and the stated policy of industry codes.

We also note that we consider that there are a number of interpretational issues with the Code which ought to be the subject of review and clarification. We have set out the major interpretational issues in this submission but would welcome the opportunity to discuss further the issues identified in this submission, together with others not set out above.

We welcome the opportunity to discuss any of our submissions in greater detail.

MINTER ELLISON
NATIONAL FRANCHISING GROUP
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