



**Small Business
Commissioner**
SOUTH AUSTRALIA

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Dear Mr Wein

Thank you for your recent invitation to meet with the South Australian Small Business Commissioners. We appreciated the opportunity to present our views to you regarding the 2013 Review of the Franchising Code of Conduct.

Please find attached our submission. Each of our recommendations is designed to promote greater transparency with franchising relationships; deliver efficient dispute resolution processes and promote full compliance with the Federal Franchising Code through direct financial penalties.

If you require any clarification of matters raised in the submission we would be most pleased to elaborate at your convenience.

Yours faithfully

Mike Sinkunas
SMALL BUSINESS COMMISSIONER

Frank Zumbo
DEPUTY COMMISSIONER

INFORM | MEDIATE | ADVOCATE



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Government
of South Australia

SUBMISSION TO THE

FEDERAL GOVERNMENT'S

2013 REVIEW OF THE FRANCHISING CODE OF CONDUCT

February 2013

Context of the submission by the South Australian Small Business Commissioner and Deputy Commissioner

The South Australian Small Business Commissioner and Deputy Commissioner welcome the opportunity to provide input to 2013 Review of the Federal Franchising Code of Conduct.



Small business is critical to the South Australian economy and the franchising sector in South Australia has enjoyed strong growth of the past 15 to 20 years. South Australia has a prevalence of small to medium enterprises, (with 96% of businesses being small businesses as defined by the ABS criteria), with relatively fewer local headquarters of multinational enterprises that serve as connectors to global innovation and markets, and higher costs per capita of infrastructure due to its smaller population and industry base.

The South Australian economy is currently undergoing a period of transformation, directed by significant and strategic government investment. Mining and mining exploration is developing strongly as well as the defence sector, with both having a significant influence in the State's economic resurgence. Agribusiness (especially in wine, grains, aquaculture, livestock and food processing) remaining a major contributor to Gross State Product, and manufacturing, including advanced manufacturing is still significant, though this sector is clearly challenged by a range of factors. Educational services, particularly at tertiary level, are a major export, and other fields such as environmental services including water-related and renewable energy products and services, are growth opportunities. To underpin this transformation there is over \$94 billion of projects in the pipeline to assist the further development of the State.

Our submission contains feedback, ideas and suggestions, in order to assist the Reviewer and the Federal Government determine their position with regard to future direction of the Federal Franchising Code of Conduct. The views expressed in this submission are those of the South Australian Small Business Commissioner and Deputy Commissioner in their capacity as independent statutory holders. The views expressed in this submission are relevant to the 2013 Review of the Federal Franchising Code and are not to be taken as a comprehensive list of the views and possible concerns of the South Australian Commissioners on franchising issues generally, or those issues outside the terms of reference of the 2013 review..

The South Australian Small Business Commissioner and Deputy Commissioner hold independent statutory offices under the Small Business Commissioner Act 2011. This Act was passed by the South Australian Parliament on 20 October 2011. The Office of the Small Business Commissioner officially opened on 29 March 2012. As part of the reforms the Commission has responsibility for administration of the *Small Business Commissioner Act 2011*, the *Retail and Commercial Leases Act 1995* and responsibilities under the *Fair Trading Act 1987* and more recently (from 1 January 2013) responsibilities within the *Health and Safety Act 2012*.

What the South Australian Small Business Commissioners are seeking from an improved Commonwealth Franchising Code of Conduct.

The South Australian Commissioners would support the following general principles and features of an improved Commonwealth Franchising Code of Conduct.

1. A *nationally connected* dispute resolution system for the franchising sector that caters for *strong regional differentiation and 'on the ground' support*. This should encourage a collaborative approach by both Commonwealth and State governments in building the most effective small business dispute resolution models for franchisees and franchisors which accurately reflect local circumstances.
2. That direct financial penalties for breaches of the Federal Franchising Code of Conduct are introduced

The information that follows in this submission expands on the key issues above and also provides comments and feedback on the terms of reference presented in the Review's Discussion paper

Summary information relating to franchising related disputes in the South Australian context

Since the South Australian Office of the Small Business Commissioner opened on 29 March 2012, there have been 401 enquires related to franchising with 57 cases to date (as of 31 January 2013). This amounts to 10% of all enquiries and 15% of cases handled by the Commissioners to date.

The following are some of the key issues raised in relation to franchising disputes from the evidence base to date:

- Increasing complexity of franchising contracts/agreements and the increasing challenge faced by franchisees and their advisers to comprehend and understand the voluminous documentation given to franchisees by the franchisor;
- Lack of transparency in parts of franchisor disclosure requirements;
- Marketing funds – lack of transparency and an apparent lack, in some instances, of audited disbursement of the marketing fund
- Requirements by franchisors for franchisees to purchase goods and/or services from franchisor – third line forcing and a lack of transparency regarding rebates that may be paid by suppliers to franchisors or an associate of the franchisor;
- Termination issues;
- End of term arrangements;
- Claims of misrepresentation
- Claims of unconscionable or unfair conduct, including claims of unfair contract terms in franchise agreements and related agreements that franchisees are required to sign; and

- Retail lease related issues especially where a franchisor holds the lease.

Within this context, the South Australian Commissioners make the following key recommendations to the 2013 Review of the Federal Franchising Code.

KEY REFORM RECOMMENDATIONS FROM THE SOUTH AUSTRALIAN COMMISSIONERS

The South Australian Commissioners would submit that there are 3 key areas needing to be addressed within the Federal Franchising Code for the benefit of the Australian franchising sector:

- Availability of direct financial penalties for breaches of the Federal Franchising Code, as well as the availability of infringement notices for breaches of the Federal Franchising Code;
- Full transparency by franchisors of critical items of information to enable franchisees to complete their due diligence; and
- Either a general statutory duty of good faith that defines good faith in plain English terms or at the very least a statutory duty of good faith defined in plain English terms in relation to mediation under the Federal Franchising Code.

Availability of direct financial penalties and infringement notices for breaches of the Federal Franchising Code

The issue of having direct monetary penalties available for breaches of the Federal Franchising Code should be straightforward for the simple reason that it would be consistent with the availability of direct financial penalties for breaches of other provisions of the *Competition and Consumer Act 2010* (Cth). Given that a failure to comply with a requirement of the Federal Franchising Code of Conduct is a breach of the Code and each breach undermines the effectiveness of the Federal Code there is an urgent need to have an effective deterrent against breaches of the Federal Franchising Code. In short, unless, there is an appropriate deterrent to prevent breaches of the Federal Franchising Code, it is clear that aspects of that Code may simply be ignored by unscrupulous or opportunistic franchisors as there may not be an effective remedy for franchisees to pursue.

Parliamentary support for the imposition of civil financial penalties for breaches of the Federal Franchising Code

The imposition of civil financial penalties for breaches of the Federal Franchising Code has received unanimous support from the Federal Parliamentary Franchising Inquiry and the South Australian Parliamentary Franchising Inquiry. Indeed, at the federal level the Parliamentary Joint Committee on Corporations and Financial Services which inquired into the operation of Australia's Franchising Code of Conduct¹ made a very clear recommendation regarding the need for pecuniary penalties for breaches of the Franchising Code of Conduct so as to assist in the Code's enforcement:

Enforcement of the Code

Recommendation 9 (paragraph 9.35)

The committee recommends that the *Trade Practices Act 1974* be amended to include pecuniary penalties for breaches of the Franchising Code of Conduct.

The introduction of these penalties would assist the ACCC in its enforcement role by providing a greater deterrent for conduct that contravenes the Code.²

Similarly, the South Australian Economic & Finance Committee³ in its Report into Franchises made the following recommendation:

The Committee recommends that the Franchising Code of Conduct be amended to introduce specific penalties for breaches of the disclosure requirements under the Code.⁴

Clearly, the imposition of direct financial penalties for breaches of the Federal Franchising Code has the clear backing of recommendations made by two independent Parliamentary franchising inquiries and, accordingly, the imposition of direct monetary penalties is not only consistent with the imposition of direct financial penalties for other provisions of the *Competition and Consumer Act* but is also based on solid policy foundations. In short, the imposition of such direct financial penalties is an appropriate policy position, especially to promote full compliance with the Federal Franchising Code.

The South Australian approach to direct financial penalties and infringement notices for breaches of mandatory codes of conduct

¹ http://www.aph.gov.au/Senate/committee/corporations_ctte/franchising/index.htm

² See pages xvi-xvii of the report:
http://www.aph.gov.au/Senate/committee/corporations_ctte/franchising/report/report.pdf

³ <http://www.parliament.sa.gov.au/Committees/Pages/Committees.aspx?CTId=5&CId=173>

⁴ See p. 42 of the Report.

See

A central feature of the South Australian legislative model dealing with mandatory codes of conduct is the availability of direct civil penalties for breaches of mandatory codes prescribed under the South Australian Fair Trading Act. Indeed, under section 86B(1) of the South Australian Fair Trading Act the South Australian Small Business Commissioner is able to commence action in the South Australian Magistrates Court seeking such a civil penalty:

(1) If the Magistrates Court is satisfied that a person has committed a civil penalty contravention, the Court may make an order (a **civil penalty order**) that the person pay to the Commissioner an amount as a civil penalty not exceeding—

(a) in the case of a body corporate—\$50 000; and

(b) in the case of a natural person—\$10 000.

With the potential for civil penalties of up to \$50,000 for a company and up to \$10,000 for an individual it is readily apparent that in South Australia there is a meaningful deterrent against breaches of mandatory codes. While not as large as civil penalties for breaches of competition and consumer law provisions,⁵ there can be no doubt that the maximum direct financial penalties under the South Australian Fair Trading Act for breaches of mandatory codes will send a clear message to those industry participants covered by such codes under the South Australian Fair Trading Act

Direct financial penalties for breaches of mandatory industry codes – A civil expiation notice

The ability of the relevant South Australian Commissioner to issue a civil expiation notice (more generally known as an infringement notice) under the South Australian Fair Trading Act is another innovative way in which to not only deter breaches of mandatory codes, but to also provide a cost effective way of dealing with alleged breaches of such codes. The intention behind a civil expiation notice is set out in section 86C of the South Australian Fair Trading Act:

If an expiation fee is fixed by the regulations for a civil penalty contravention, a civil expiation notice may be given to a person alleged to have committed the contravention and the alleged contravention may be expiated in accordance with this Subdivision.

Importantly, the legal effect of an `expiation' is outlined in section 86F of the South Australian Fair Trading Act:

⁵ See, for example, section 76 of the *Competition and Consumer Act 2010* (Cth).

- (1) Subject to this Subdivision, if a civil penalty contravention, or contraventions, to which a civil expiation notice relates are expiated in accordance with this Subdivision, proceedings may not be commenced for a civil penalty order against the person to whom the notice was given for that contravention or those contraventions or any other expiable civil penalty contravention arising out of the same incident.
- (2) The expiation of a civil penalty contravention—
 - (a) does not constitute an admission of guilt or of any civil liability; and
 - (b) will not be regarded as evidence tending to establish guilt or any civil liability; and
 - (c) cannot be referred to in a report furnished to a court for the purposes of determining sentence for an offence.

Clearly, the issuing of a civil expiation notice by the relevant South Australian Commissioner is an alternative to commencing court proceedings for a civil penalty. Not surprisingly, a civil expiation fee under a civil expiation notice can only be for a significantly lesser amount than one that can be imposed by the Magistrates Court. With expiation fees of up to \$6,000 for a company or \$1,200 for an individual,⁶ it is apparent that paying an expiation fee allows a person who has allegedly breached a mandatory code or provisions of such a code to quickly resolve the matter without any admission of liability.

Full transparency by franchisors of critical items of information to enable franchisees to complete their due diligence

While obviously a franchisee can access a considerable amount of information from the existing franchisor disclosure document and the franchise agreement and other documents the franchisee is required to sign, as well as from publicly available information about the franchisor, it is unfortunate that even after considering all this information it is still possible for a franchisee to be missing or be unable to access some critical pieces of information about the franchisor that no amount of due diligence can remedy. These critical missing pieces of information represent dangerous gaps in the existing disclosure requirements under the Federal Franchising Code.

Of these gaps, two are particularly noteworthy and relate to (i) an inability of franchisees to get information regarding the actual amounts of rebates or other financial benefits received by franchisors or their associates from suppliers where franchisees buy goods or services from the supplier; and (ii)

⁶ See section 28F(1)(c) of the South Australian Fair Trading Act.

an inability of a franchisee to get access to the franchisor's most recent financial reports.

Requiring franchisors to disclose full details of all rebates and other financial benefits received by the franchisor or associate of the franchisor

Under Item 9 of the franchisor disclosure document to be produced in accordance with Annexure 1 of the Federal Franchising Code a franchisor must currently disclose (i) whether franchisor or an associate of the franchisor receives a rebate or other financial benefit from the supply of goods or services to the franchisee, and (ii) whether the rebate or other financial benefit is to be shared with franchisees:

9 Supply of goods or services to a franchisee

9.1 For the franchisor's requirements for supply of goods or services to a franchisee — details of:

- ...
- (j) whether the franchisor, or an associate of the franchisor, will receive a rebate or other financial benefit from the supply of goods or services to franchisees, including the name of the business providing the rebate or financial benefit; and
- (k) whether any rebate or financial benefit referred to under paragraph (j) is shared, directly or indirectly, with franchisees.

Here the requirement is to just disclose the mere fact that rebates or other financial benefits are received by the franchisor or an associate of the franchisor, and whether they are to be shared with franchisees. Unfortunately this is not enough as full disclosure of the amounts or methods for calculating such rebates is essential as they may adversely impact on the financial viability of the franchisee's business. As such rebates and other financial benefits need to be funded in some way the suppliers of goods or services to franchisees may increase the price of goods or services supplied to franchisees in order to fund the rebates or the other financial benefits to be paid directly or indirectly to the franchisor or an associate of the franchisor. These higher prices may place the franchisee at a competitive disadvantage in the market place and may undermine the financial success of the franchisee's business. Higher supply prices due to the need to pay rebates or other financial benefits to a franchisor or an associate of the franchisor may prevent a franchisee from being competitive with competitors to the franchisee's business and may ultimately undermine a franchisee's chances of business success.

Clearly, franchisees or prospective franchisees need to be able to fully assess how the payment of rebates or other financial benefits to the franchisors or an associate of the franchisor may impact on a franchisee's competitive position in the marketplace. Given that in practice franchisees are likely to be

ultimately paying for any rebates or other financial benefits paid to the franchisor or an associate of the franchisor, franchisees have a genuine right to know the amount and size of such rebates and other financial benefits. Secrecy as to the actual amounts of the rebates or other financial benefits represents a serious gap in the current disclosure requirements as franchisees are being denied access to a valuable piece of information that could potentially adversely impact on a franchisee's financial viability and competitive positioning in the marketplace.

Such secrecy may also undermine the relationship between the franchisor and franchisee as it may be perceived by a franchisee as the franchisor withholding a vital piece of information for the financial benefit of the franchisor or an associate of the franchisor. It is trite to say that good and successful franchising relationships are built on honesty, openness and transparency between the franchisor and franchisee.

In interests of greater transparency the current disclosure requirements could be easily amended so as to require franchisors to also disclose the full amount and methods of calculation of any rebates or other financial benefits to paid to the franchisors or an associate of the franchisor, or which is to be shared with franchisees are disclosed to franchisees.

Requiring franchisors to provide franchisees with the franchisor's most recent financial reports

There can be no doubt that the franchisor's financial viability affects not only the franchisor itself but also all its franchisees. Obviously, a franchisee has a very direct and genuine interest in the franchisor's financial viability for the duration of the franchising relationship. Indeed, the franchisor (amongst other things) holds the intellectual property rights for the franchise system and could hold the head lease for the franchisee's business premises. Given this high level of control over the franchisee's business, it is clear that a franchisor's financial instability would put at serious risk all these particular aspects of the franchisee's business and could leave the franchisee financially devastated if franchisor failed.

This issue arises as a result of the present drafting of item 20 of the franchisor disclosure document under Annexure 1 of the Federal Franchising Code which provides that the franchisor's financial reports do not have to be given to franchisees where an audit statement is given to the franchisee in accordance with item 20.3:

20 Financial details

- 20.1 A statement as at the end of the last financial year, signed by at least 1 director of the franchisor, whether in its directors' opinion there are reasonable grounds to believe that the franchisor will be able to pay its debts as and when they fall due.

20.2 Financial reports for each of the last 2 completed financial years in accordance with sections 295 to 297 of the *Corporations Act 2001*, or a foreign equivalent of that Act applicable to the franchisor, prepared by the franchisor.

20.2A If:

- (a) the franchisor is part of a consolidated entity that is required to provide audited financial reports under the *Corporations Act 2001*, or a foreign equivalent of that Act applicable to the consolidated entity; and
- (b) a franchisee requests those financial reports; financial reports for each of the last 2 completed financial years, prepared by the consolidated entity.

20.3 Items 20.2 and 20.2A do not apply if:

- (a) the statement under item 20.1 is supported by an independent audit provided by:
 - (i) a registered company auditor; or
 - (ii) if the franchisor is a foreign franchisor — a foreign equivalent for that franchisor; within 12 months after the end of the financial year to which the statement relates; and
- (b) a copy of the independent audit is provided with the statement under item 20.1.

Given that existing and prospective franchisees may be investing significant sums of money in the franchised business, it is essential that they are able to make an informed decision about the franchisor's financial viability. Requiring franchisors to provide a full set of audited financial reports to potential and existing franchisees would allow prospective franchisees to assess the franchisor's financial viability before investing in the franchisor's system and it would give existing franchisees some advance warning if the franchisor is struggling financially. The sad reality at present is that franchisees may be the last to find out about a franchisor's financial problems and that places franchisees at a considerable disadvantage. Indeed, by not having access to the franchisor's most recent financial reports franchisees are being kept in the dark about a very critical piece of information that franchisees may not have any other way of getting as the franchisor may be unwilling to voluntarily provide to franchisees its most recent financial reports.

The provision of a full set of audited financial reports can be achieved by simply deleting Item 20.3 in Annexure 1 of the Franchising Code. The exception currently found in item 20.3 too easily excuses franchisors from providing their actual financial reports to franchisees or prospective franchisees. Given that a competent franchisor would in any event be preparing financial reports for the business and have those reports audited as part of good business practice, the cost of requiring franchisors to provide their most recent financial reports to potential and existing franchisee would be negligible, especially if the reports were provided electronically to franchisees or potential franchisees. The benefits to franchisees and prospective franchisees would be substantial as it would allow them to assess

the franchisor's financial viability on an ongoing basis. After all, franchisees are investing in the franchisor's business and should be able to do their due diligence on the franchisor's financial viability.

Either a general statutory duty of good faith that defines good faith in plain English terms, or at the very least a statutory duty of good faith defined in plain English terms in relation to mediation under the Federal Franchising Code.

Good faith is good franchising. Good franchising embodies a transparent and mutually beneficial relationship where the franchisor and franchisee act towards each other in a fair, honest, reasonable and cooperative manner. Franchising is an interdependent relationship where the success of the relationship depends on both the franchisor and franchisee working together towards a common goal in a manner that acknowledges that the success of each party is very much dependent on the success of the other party.

The nature and success of interdependency between the franchisor and the franchisee can be best described by reference to the parties acting in good faith. Within this context, both parties acting in good faith helps build and maintain an ongoing and mutually beneficial franchising relationship.

A duty to act in good faith is a well establish guiding principle in contractual relationships in Australia and around the world. In fact, a statutory duty of good faith is specifically applied to commercial relationships in many jurisdictions around the world and has expressly been incorporated in the Ontario Franchising Law known as the *Arthur Wishart Act (Franchise Disclosure)*, 2000.⁷

Within an Australian franchising context a general statutory duty of good faith that defines good faith in plain English terms could be included under the Federal Franchising Code. Alternatively, and at the very least, a statutory duty of good faith defined in plain English terms in relation to mediation under the Federal Franchising Code.

Acting in good faith can be defined in plain English to mean acting fairly, honestly, reasonably and cooperatively. These terms capture the essence of an implied duty of good faith and, in turn, reflect what the courts have held to be to the underlying duties of parties to a commercial contract. Indeed, it is especially noteworthy that acting fairly, honestly, reasonably and cooperatively are recurring themes either individually or collectively in these and other cases in which an implied duty of good faith has arisen. In turn, such cases point to the acting fairly, honestly, reasonably and cooperatively as being integral to the standards of conduct imposed by the Courts on parties to commercial contracts.

⁷ See <http://www.canlii.org/en/on/laws/stat/so-2000-c-3/latest/so-2000-c-3.html>

Within this context, an implied duty of good faith linked to concepts of fair dealing and reasonableness is now considered to apply to franchise agreements. For example, Byrne J made the following comments in *Far Horizons Pty Ltd v McDonald's Australia Ltd* [2000] VSC 310 (18 August 2000):

“I do not see myself as at liberty to depart from the considerable body of authority in this country which has followed the decision of the New South Wales Court of Appeal in *Renard Construction (ME) Pty Ltd v Minister for Public Works*. I proceed, therefore, on the basis that there is to be implied in a franchise agreement a term of good faith and fair dealing which obliges each party to exercise the powers conferred upon it by the agreement in good faith and reasonably...”

The comments in relation to acting reasonably were echoed in Burger King Corporation v Hungry Jack's Pty Limited [2001] NSWCA 187 (21 June 2001);

“...it is worth noting that the Australian cases make no distinction of substance between the implied term of reasonableness and that of good faith.”

Acting reasonably was seen as central to acting fairly and in good faith by Finkelstein J in *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903 (2 July 1999);

“...provided the party exercising the power acts reasonably in all the circumstances, the duty to act fairly and in good faith will ordinarily be satisfied.”

On the issue of acting honestly Einstein J in Aiton v Transfield [1999] NSWSC 996 (1 October 1999) made the following comments:

“...parties are subject to a universal duty to act honestly: *Meehan v Jones* [1982] HCA 52; (1982) 149 CLR 571 per Gibbs CJ at 580-581; per Mason J at 589-590; per Wilson J at 597-598.”

Finally, in relation to a common law duty to cooperate Sheller JA in Alcatel Australia Limited v Scarcella [1998] NSWSC 483 (16 July 1998) made the following comments:

“...the common law imposes a duty on the parties to a contract to cooperate in achieving the objects of the contract. See *Mackay v Dick* (1881) 6 App Cas 251 at 263; *Secured Income Real Estate (Australia) Limited v St Martins Investments Pty Limited* [1979] HCA 51; (1979) 144 CLR 596 at 607; *Perri v Coolangatta Investments Pty Limited* [1982] HCA 29; (1982) 149 CLR 537; *Meehan v Jones* [1982] HCA 52; (1982) 149 CLR 571.”

Clearly, acting fairly, honestly, reasonably and cooperatively are concepts that are well known to the common law and can be usefully drawn upon to define the statutory duty of good faith

A statutory duty of good faith is directly consistent with international practice

Having a statutory duty of good faith which is defined by reference to acting fairly, honestly, reasonably and cooperatively is directly consistent with international practice. For example, the Canadian Province of Ontario has enacted a statutory duty of good faith which is found in section 3 of the *Arthur Wishart Act (Franchise Disclosure), 2000*:⁸

Fair dealing

3. (1) Every franchise agreement imposes on each party a duty of fair dealing in its performance and enforcement.

Right of action

- (2) A party to a franchise agreement has a right of action for damages against another party to the franchise agreement who breaches the duty of fair dealing in the performance or enforcement of the franchise agreement.

Interpretation

- (3) For the purpose of this section, the duty of fair dealing includes the duty to act in good faith and in accordance with reasonable commercial standards.

The reference to fair dealing and acting in accordance with reasonable commercial standards highlights the importance of acting fairly and reasonably within franchising relationships.

Clearly, a statutory duty of good faith defined in plain English goes to the heart of franchising relationships for the simple reason that acting fairly, honestly, reasonably and cooperatively are hallmarks of a successful ongoing relationships such as a franchising relationship. In fact, a franchising relationship is a two way relationship where neither party can act solely in their own self interest. A franchisor and franchisee are mutually dependent on each other for their individual success. A franchisor and franchisee need to act in unison towards a common goal and for either party to try and behave solely in their individual self interest would simply lead to the breakdown of the relationship.

⁸ See <http://www.canlii.org/en/on/laws/stat/so-2000-c-3/latest/so-2000-c-3.html>

In reality a franchisor and franchisee need to behave in a cooperative manner having regard to each other's interests in the relationship. Of course, a franchisor and franchisee have their own legal identify, but the fact they are in a mutually dependent relationship means that they need to cooperate in order to achieve their common goal. In short, the mutually dependent and ongoing nature of the franchising relationship means that a franchisor and franchisee need to have regard to each other's interests when participating in the franchising relationship. Within this context, a statutory duty of good faith describes the manner in which a franchisor and franchisee are to behave towards one another.

Thus, a statutory duty of good faith would provide an overarching guiding principle which would help strengthens the relationship between a franchisor and franchisee by ensuring that they behave in a mutually beneficial manner throughout their franchising relationship. Indeed, a statutory duty of good faith highlights that a franchising relationship is not an exploitative one between completely self-interested adversarial and competitive rivals, but rather a franchising relationship is a mutually dependent and beneficial relationship between two parties working towards a common goal.

The important role and considerable benefit of having a statutory duty of good faith within a franchising context is clearly highlighted by the fact that three separate independent inquiries have recommended the enactment of a statutory duty of good faith. Indeed, a statutory duty of good faith was recommended by South Australian Parliamentary Franchising Inquiry⁹ and the Federal Parliamentary Franchising Inquiry.¹⁰ Previously, a statutory duty of good faith was also recommended by the 2006 *Review of the Disclosure Provisions of the Franchising Code of Conduct* (the Matthews Review).¹¹ The following comments by the Matthews Review regarding the value of a statutory duty of good faith are particularly noteworthy:

“The interdependency between franchisors and franchisees is fundamental to the franchise sector. Notwithstanding the various legal remedies already available to both franchisors and franchisees under various laws... the Committee considers that recognition in the Code of a concept of good faith and fair dealing would provide positive reinforcement to the development of improved relationships and dealings between franchisors, franchisees and prospective franchisees.”¹²

Based on this policy rationale the Matthews Review made the following recommendation:

⁹ See

<http://www.parliament.sa.gov.au/Committees/Pages/Committees.aspx?CTId=5&CId=173>

¹⁰ See

http://www.apf.gov.au/Senate/committee/corporations_ctte/franchising/report/report.pdf

¹¹

<http://www.innovation.gov.au/SmallBusiness/CodesOfConduct/Documents/FranchisingCodeReviewReport2006.pdf>

¹² See page 47 of the Report.

Recommendation 25

A statement obligating franchisors, franchisees and prospective franchisees to act towards each other fairly and in good faith be developed for inclusion in Part 1 of the Code.¹³

When the recommendations by South Australian Parliamentary Franchising Inquiry; the Federal Parliamentary Franchising Inquiry and the Matthews Review for a statutory duty of good faith are taken together it is clear that there is a very strong policy foundation for the statutory duty of good faith.

A final word from the South Australian Commissioners

Each recommendation in this submission represents a balanced and targeted response to issues that have arisen in inquiries and cases considered by the South Australian Commissioners. It is essential that the Federal Franchising Code has no gaps and that it is backed by direct financial penalties to ensure full compliance by all franchisors with the Code. The Australian franchising sector would benefit considerably from the gaps in the Federal Franchising Code being closed and from direct financial penalties being available for breaches of the Federal Franchising Code.

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¹³ Ibid.