Franchising Code Review Secretariat
Business Conditions Branch
Department of Industry, Innovation, Science, Research and Tertiary Education
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SUBMISSION ON THE DISCUSSION PAPER "REVIEW OF THE FRANCHISING CODE OF CONDUCT"

Submission by:

This is a personal submission by Derek Charles Douglas Sutherland (Lawyer). This is personal submission and the views contained in it are mine and are provided on that basis and do not reflect the views of the law firm (or necessarily by inference any of its clients) in which I am currently employed.

Contact details:

The Respondent requests that the personal contact details of the Respondent are to be kept Confidential refer to Attachment "A".

Date of Submission:

The 14th of February 2013

Whether Submission is to be kept confidential or not and able to be released to the public:

No the content of the Submissions are not confidential however the Respondent requests that the personal contact details of the Respondent not be released and be treated in confidence.

Initial comments:

1. Attached to this submission in Annexure "B" is a copy of the detailed Discussion Paper that was provided to the Commonwealth in July 2012 by the Respondent outlining some issues at that time that the Respondent thought were relevant to any review of the Code. In particular the issues in the Discussion Paper related to the following generally (and in no specific order):

   (1) The proposed scope of this review of the Franchising Code of Conduct;

   (2) Issues arising from introducing an obligation of good faith;

   (3) Issues arising from the introduction of a penalty regime for breaches of the Code;

   (4) The interplay with proposed State based Industry Codes of Conduct;

   (5) Current interpretational problems with the Code that could be exacerbated by the introduction of good faith or a penalty regime and which should be corrected;

   (6) The ability to have the ACCC make some type of binding determinations.

2.	The Respondent remains of the view that:
(a)	I do not support that there is an overwhelming and immediate need to: (1) codify an obligation on the parties to act in good faith in relation to all of their dealings (pre-contractual negotiations, contractual obligations and post contractual obligations or negotiations); or (2) seek to define in the Code a comprehensive definition of "good faith". It is also not unanimously or overwhelmingly accepted that the Courts will in every state and territory determine that there is an implied obligation to act in good faith implied under the common law into commercial agreements generally or into every franchise agreement specifically (whether regulated by the Code or not). The expert Panel engaged by the Commonwealth previously confirmed the difficulty in reaching any conclusive and all encompassing definition. It is my perception that most lawyers who act predominantly for franchisors and master franchisees would argue that any determination of existence of that obligation and its meaning should be left to the common law to determine and the definition of "good faith" continue to evolve at the same time as the nature and extent of that implied obligation. It is my perception that most franchisee lawyers would argue that it would be beneficial to have an express obligation of good faith apply to all dealings between the parties to a franchise agreement even if there is no comprehensive definition of what good faith is. *Is it to be a Code obligation or a contractual obligation or both?* I also caution that if an obligation is to be codified that care needs to be taken when drafting the wording to include into the Code that the Government has published a very clear and unambiguous policy intention as to how the obligation is intended to apply. Ultimately the wording of any such obligation that is crafted into the Code needs to be clear. It is possible that it could be expressed simply as an implied or an express and mandatory obligation deemed to be included into every franchise agreement (that is in fact regulated by the Code and irrespective of what the terms of the agreement say) (e.g. a "Contractual Obligation"). In that way it may be expressed to apply to some or all of the contractual provisions of the agreement or alternatively apply to all of the conduct or dealings of the parties to that agreement when exercising any right or power or performing any obligation. Alternatively it could be expressed as an express Code provision which if breached gives rise to express consequences (e.g. a "Code Obligation") that applies without the necessity to imply it or deem it to form part of the terms of the franchise agreement. That provision may relate to all or only some of the provisions of the Code (e.g. clauses 20, 21, 22, 23 and Part 4). Or alternatively so that it operates and relates to both of the above (e.g. in all of its dealings which covers the field). If the good faith obligation was imposed on the performance of obligations under the Code as well as to contractual dealings between the parties then it would need to be clearly expressed to be subject to that obligation to perform that obligation or exercise the power or right in good faith. In the later case for example it would be a Code Obligation (as opposed to a Contractual

Obligation) if the Code provided that a franchisor must act in good faith when considering a renewal decision under clause 20A(1)(b) or 20A(2)(b) whether to offer to negotiate a new agreement when there is no option to renew remaining.

Failure to do so may amount to a breach of the Code as opposed to simply a breach of contract.

Good faith in this context would require the parties to engage in negotiations in good faith to renew or enter into a new agreement at the end of term.

Another example may be that the parties have an obligation imposed on them to act in good faith when they must seek to resolve a dispute under the process in Part 4 of the Code.

The actual scope and wording of the obligation imposed therefore may have a direct impact on the extent of relief available to either the ACCC or an affected party. The nature and extent of the kind of relief which ultimately is available to either the ACCC or an affected party will depend on whether it is a Contractual Obligation versus a Code Obligation.

Currently the common law would suggest that an implied obligation to act in good faith is in fact a Contractual Obligation applying to dealings between the parties during the term and not necessarily to a statutory obligation (e.g. a Code Obligation) imposed on the franchisor to do something under the Code.

A Code Obligation if breached may give rise to an infringement notice or prosecution by the ACCC if a penalty is introduced however the intention as to whether that is the only relief available for that breach should also be made clear to avoid any ambiguity. If a penalty regime is not the only intended relief then it should be made clear that a prosecution for that breach does not prevent the enforcement of a contractual right by the parties (or for that matter a defence by one of them) arising out of that breach. In other words it may need to be expressed as both a Code Obligation and a Contractual Obligation.

Introduction of the obligation without consideration of the consequences (including those I foreshadowed in my Discussion Paper) may lead to unsustainable expectations of the nature and extent of relief being available.

Ultimately the Commonwealth may consider it most appropriate to make it a "Code Obligation" rather than a "Contractual Obligation" with the consequence of a breach being expressed in the Code as a specific consequence or remedy (including potentially enforcement rights of the ACCC) as well as allowing a party to a franchise agreement to also pursue its own relief as the circumstances require.

I believe that any attempt to impose that obligation requires a careful review of the language of the Code to ensure that there are clear types of conduct that the obligation applies to and to whom the obligation is extended (to all parties to the franchise agreement). It is problematic to seek to extend that obligation to related entities and persons associated with the franchisor or franchisee who are not parties to the franchisee agreement.

For example related entities to the franchisor may supply goods or services to the franchisees such as products or hold the head lease.

It may also be unnecessary to extend the obligation to apply to pre-contractual negotiations between the parties before the agreement is entered into. There are already extensive existing misleading and deceptive conduct provisions and unconscionable conduct provisions that would clearly cover pre contract negotiations.

Consideration of whether it should apply to post end of term obligations or negotiations is also

	directly relevant (such as obligations not to compete, not to use IP maintain confidentiality, application of post termination provisions such as options to buy, rights of first refusal, step in rights, termination of subleases or licenses etc). Any transitional provisions will need to be clear whether the obligation applies to all franchise agreements (irrespective of when they are entered into) or only some (like those entered into on or after the date of the amendment).
(b)	Any penalty regime needs to be measured and the ACCC enforcement of the Code focussed on deliberate anti avoidance rather than penalising franchisors for inadvertent or minor technical mistakes (where no real loss or damage is suffered) or where the language leaves interpretation of an obligation open. Presumably a penalty regime may also be contemplated to apply to conduct of individuals where it is proven that they are knowingly concerned in a breach. The extent and nature of penalties (and if implemented some form of infringement notice regime) for corporations and also for individuals should be made transparent. It would be preferable to focus penalties on other more expansive and typical business to business type conduct such as misleading and deceptive conduct and unconscionable conduct rather than simply targeting penalties at technical breaches of the Code, particularly where in the case of technical breaches, no loss or damage is occasioned. This requires a measured hand and will necessitate additional financial and human resources for the ACCC. This means clear amendments and subsequent education of the sector in the area of the forms of penalties and any defences, mitigating circumstances or official policies of enforcement (e.g. warning notices, infringement notices or strict liability offences) so that people understand clearly what can occur. In particular great care should be taken with the enforcement policy so that when considering an infringement notice regime it is clear that multiple notices are not able to be issued for essentially the same breach e.g. a failure to do something generally (e.g. update a disclosure document) should not necessarily warrant the issue of a separate infringement notice in respect to every franchise agreement in the network thereby taking what would otherwise amount to a small infringement penalty into a substantial pecuniary penalty. In addition any transitional provision needs to be clear whether it applies only to conduct or breaches that occur after the amendment date.
(c)	The Commonwealths' "*Franchising Code of Conduct Compliance Manual*" and other publications will need updating and it would be highly beneficial to the franchise sector for a detailed set of meaningful frequently asked questions and answers to be published for the benefit of franchisors and master franchisees so they can understand their obligations and interpret the sections of the code clearly and consistently. The ACCC currently targets those questions and answers directly to franchisees not franchisors and master franchisees.
(d)	The review of Oilcode takes place next year. It is not clear whether it is contemplated for the same or similar changes to be made for franchise agreements covered by that Code or whether fines or penalties are proposed for breaches of any mandatory industry code prescribed under the CCA. If it is greater consultation with those sectors may be required as this review is simply into this specific code of conduct. It is appalling that the provisions in the 2 codes (whilst based on the Franchising code) have not kept pace as reviews happen so changes in one code are not also made to the other where the provisions are the same.

(e)	There are a number of poorly drafted provisions of the Code that are still open to interpretation. It would be beneficial to "*close the gap*" and provide clarity in relation to those provisions to ensure the Code is working and to minimise the risk of unnecessary prosecutions for breaches if a penalty regime is introduced. Unfortunately previous reviews have not focussed on the overall provisions of the Code generally but been focussed on particular areas. Accordingly whilst some mistakes and improvements have occurred over time there are some unresolved wording and application issues that could be clarified or fixed now. An example is the transfer/ novation problem with the Code outlined below which is acknowledged widely in the legal fraternity as being broken and requiring fixing. It is already Government policy that when drafting industry codes it is important to ensure there is clarity in drafting. It is widely considered amongst the legal community that whilst the framework of the Code is sound, the language used is not precise and if the Government subsequently overlays a penalty regime to an industry code where the language is not always clear then it will create problems for the sector.
(f)	There is nothing fundamentally wrong with the general framework of the Code provided it remains a mandatory industry code policed and enforced solely by the Commonwealth. There remains widespread support for the Commonwealth to continue to regulate the sector without the States and Territories seeking to adopt the Code (or enact legislation) to grant themselves rights to investigate and prosecute for non compliance of what is a Commonwealth Code. The Commonwealth should move decisively to close that overlap once and for all to remove duplication, costs and uncertainty.

Discussion Questions and Responses:

Part Two: Disclosure under the Franchising Code of Conduct

1. **Has the additional disclosure requirement regarding the potential for franchisor failure effectively addressed concerns about franchisees entering into franchise agreements without considering the risk of franchisor failure?**

Response:

There appears to be no Government policy preference to make changes to insolvency laws to protect the rights of franchisees in the event of franchisor insolvency.

Whilst a warning statement has assisted to highlight that there is always a risk of head franchisor, franchisor or master franchisee failure, ultimately franchisees need further education and advice about the consequences that will occur in the event of insolvency of a head franchisor, franchisor or master franchisor.

This should be made much clearer in the ACCC Franchisees Guide publication issued by the ACCC. Possibly it should be made mandatory for a franchisor to give the guide to franchisees as part of the disclosure document and amend the statement required to be obtained under clause 11(1) of the Code before entering into the franchise agreement.

Many systems do provide that as part of the disclosure document already.

Franchisor insolvency is only one aspect of risk to a franchisee and any warning statement (and also education programs) should also specifically deal with not just the insolvency of the franchisor but also entities that may be relevant to the network such as the IP owner, any leasing company and any companies that supply goods or services to the network that may be related to the franchisor or to its owners.

This education and advice should include what would happen to their rights under the franchise agreement to continue to operate, the ability of the liquidator or administrator to require them to continue to pay royalties or end their agreements, what happens to any lease or occupation right or supply arrangement if the franchisee does not hold that right, what happens to their business if the system is to be sold or run under administration or receivership.

Arguably with the increase in franchisor or master franchisor failure due to insolvency, lawyers and other business and accounting advisors should be more focussed in this area when advising franchisees. However there is no mandatory obligation under the Code to compel the franchisee to seek that advice. Cost and access to good professional advice and courts for timely relief remains an issue for franchisees. It is unlikely lawyers will sign certificates if insurance companies and Law Societies become concerned that essentially the certificates do no more than act as a guarantee to franchisors that if a franchisee gets out of their agreement they will pursue the franchisees advisors.

Publications by the ACCC or prepared in conjunction with industry associations would be helpful.

At the last review it was a recommendation that a risk statement be prepared and there was consultation to occur between the ACCC and industry associations to try and develop a template for use in the sector. Nothing appears to have been done to further that goal. It would be preferential for the ACCC to develop those risk statements in consultation with the Sector.

The actual consequences to a franchisee are difficult (if not impossible) to comprehensively include in a warning or risk statement and if an obligation is imposed on the franchisor to prepare and give a risk statement to the franchisee, then if the franchisor prepares one and gives it the franchisees it should not be a breach of the Code if a franchisor cannot at the outset outlined every single possible consequence.

In other words any breach should be based around the failure to provide the Risk Statement rather than failing to address in the Risk Statement every possible consequence whether foreseeable or not.

2. Does the sector have any concerns regarding the operation of this requirement?

Response:

Yes, whilst the risk statement on the warning cover page of the Annexure 1 is useful this does not address and correct the current imbalance that occurs in the event of franchisor insolvency.

Franchisors do have a statutory right to immediately terminate a franchisee for special circumstances (without having to give a breach notice or reasonable notice under clauses 21 and 22) under clause 23(b) of the Code for bankruptcy, insolvency or the external administration of the franchisee.

Exercise of that right and the right to terminate any lease or licence granted to the franchisee regulated by State based Retail Shop Leases legislation may also be subject to any moratorium of enforcement of rights under the *Corporations Law*.

A landlord cannot commence to enforce its rights to recover possession until after the administrator has made an election about the lease premises within a specified period of 7 days from appointment.

There are rights conferred on external controllers in certain circumstances to disclaim onerous or uncommercial contracts. A franchise agreement could fall in this category where the liquidator is unable to continue to offer goods or services to the network.

If the preferred outcome of balance is to keep the system in tact for a potential resale of the network has merit, then a franchisee with a right to terminate (which is identical to that in clause 23(b) after appointment of an external administrator would frustrate this.

If the right to terminate was limited to the event where the company is placed into liquidation before the franchisee can elect to terminate then the franchisee could walk away from the restraint of trade and continue to operate (without the benefit of any IP) and take steps to secure the premises with the landlord.

If this proposition is correct then conferring a similar right to terminate on a franchisee if the company is placed into liquidation (as opposed to administration) or receivership or other external control may assist the franchisee to move on but it does not adequately address what will happen if the franchisee holds a head lease and must continue to occupy and conduct a business otherwise it will default under that third party contract.

Unfortunately any disclaimer of the franchise agreement or any lease by the external administrator may frustrate the attempt by the franchisee to minimise its loss or damage by continuing to trade.

There is currently no statutory obligation of a liquidator to offer the lease held by an insolvent franchisor to a franchisee nor for the ultimate landlord to offer a new lease or assignment of the lease to the franchisee and no assurance that the ultimate landlord would agree to accept the franchisee as tenant.

In some cases where the franchisor or a related entity holds the premises lease there is often arrears owing to the landlord which may have already been paid by the franchisee to the franchisor for rent which were not passed on. In this case the franchisee can suffer twice having to pay the rent and outgoings again to retain the premises. This occurred in the corporate collapse of Kleins.

There remains a difficult conundrum on how to reconcile imbalance between the protection of creditors over the protection of franchisees interests as consumers. The rights of insolvency professionals to disclaim or deal with assets of an insolvent franchisor do not necessarily help franchisees although it is acknowledged that where possible the sale of a system as a whole is one of the preferred commercial outcomes usually investigated as a priority which may benefit most of the franchisees in the network who wish to remain.

There have been instances where core assets such as trademarks and other forms of intellectual property are sold by the external controllers and end up in the hands of entities associated with the former directors and owners to exploit without the burden of an ongoing contractual obligation to franchisees.

There is no enforceable right to allow a franchisee to register an interest granted by the owner of the trade mark (or the franchisor if the exclusive right to use it in an area is licensed to it) to use a trademark under the *Trade Marks Act*. Generally franchise agreements charge upfront fees to joint the network but have ongoing fees or royalties to be able to continue to use the IP during

the term. The upfront fee is lost when the network collapses and franchisees must continue to pay royalties to use the IP even though the fundamental tenant of support and a long term relationship is broken.

As a consequence franchisees lose the right to use the IP if the franchise agreement is disclaimed. Possibly a review of the rights under this legislation could assist franchisees who have paid for the right to use the trademark to register their interest and right to continue to use it if the franchise agreement is disclaimed should they chose to do so before they rebrand.

Franchisees investments in a business opportunity are immediately affected without any fault of their own if their franchisor becomes insolvent. Their capital investment is diminished as they are unable to have certainty to continue to operate the business for an agreed contractual term under the brand and continue to receive the supply of goods or services into the future. There prospect of selling their business as a going concern without the benefit of the brand is lessened without incurring the costs of rebranding the business.

Often the failure of the franchisor will lead to a consequential failure of other franchisees and bankruptcy of guarantors through no fault of their own unless the system can be sold as a going concern or the franchisees able to re-brand and join another network or continue to operate independently. Unfortunately it often means that core rights are no longer available and it makes continued trading difficult.

Financiers appear to understand that franchisors can and do fail and they continue to seek security from franchisees and guarantors external to business assets and rights. Often franchisees are also expressly prohibited from charging or encumbering the rights under a franchise agreement which commercially appears to be a limited right in any event as it is subject to termination.

Most financiers will seek to negotiate a step in right to prevent termination of the franchise agreement if the franchisee defaults or becomes insolvent so that the franchisor does not act to terminate without notice and consultation with the bank to see if the business can be sold as a going concern and maximise the chance of a return to the financier and other creditors.

Step in rights (or obligations) of head franchisors or IP owners who licence their IP to the franchisor are often not adequately disclosed in Item 7 of Annexure 1.

Possibly greater disclosure of this would be beneficial so that franchisees understand that in the event of the insolvency of the franchisee or the franchisor (or the termination or expiration of a master franchise) what impact this will have on their agreement.

Whilst I have seen some Disclosure documents include brief disclosure on this issue as to whether the head franchisor may step in, there is no specific disclosure item in Item 7.1(f)(i) to (iv) of Annexure 1 (or Annexure 2) that specifically asks for disclosure of the potential impact on the franchisee's franchise agreement and whether the IP owner or head franchisor (which may not be the IP owner) will step in and takeover the system or observe the terms of the existing franchise agreements or offer or enter into new ones. There should be an express obligation to disclose whether the IP is currently subject to a form of security interest and how that affects the franchisee if the security interest is enforced in an insolvency.

It is preferable to give more disclosure to Franchisees about consequences of insolvency or termination of rights of a master franchisee under this Item.

Expenditure and other payments:

3. **Have amendments to the Franchising Code improved the transparency of financial information for franchisees? If not, why not? If so, what benefit is this having for franchisees?**

Response:

There are several places where the Code was amended that relate to financial information given to franchisees.

Specific headings included:

Payments to third parties
Unforseen capital expenditure
Attribution of legal costs
Disclosure of rebates and other financial benefits
Financial reports for marketing and cooperative funds
Financial details of the franchisor
Leasing arrangements

Payments to third parties (Item 13.6A of Annexure 1):

This has been an improvement to disclosure of other types of payments that may need to be made to third parties which can assist a franchisee to prepare a business plan. This is easier to complete for well established systems.

However in practice it is still common for franchisors not to be able to disclose every fee or payment unless they are a well established system and can collect that data from franchisees (including ranges for the franchisees legal and accounting costs for advice on the franchise documentation) as they may not be known to the franchisor. Some systems do not ask for this data from franchisees and often the supply is voluntary and subject to the willingness of a franchisee to be accurate in what they supply.

It is also unclear under the Code as to the effect of a failure to disclose a payment to a third party and whether that gives rise to some consequence.

Similarly it is not clear under the Code what is the consequence of a failure by the franchisor to disclose a payment to the franchisor under Item 13.6 which is accidently omitted and not disclosed under that item. This may or may not mean that the disclosure is defective or misleading. There have been arguments put forward that the failure to disclose may mean that the fee of payment is or is not recoverable by the franchisor.

However there is no express language used in the Code as to the consequence. For example there is NO clear language that says:

"If a franchisor does not disclose the nature or extent of a fee or payment under this Item or in its franchise agreement that must be made to it (or an associate of it) then the franchisor cannot enforce payment of that fee or payment under their franchise agreement."

Whether that sort of language is required depends on many things including whether non disclosure is so widespread that it is a serious mischief that must be remedied. I do not believe that it is.

Unforseen capital expenditure (Item 13A):

Disclosure under this item may usually contain a general statement that franchisees need to

allow for certain unexpected capital expenditure during the term that can occur for things such as premises upgrades and refurbishments on transfers or renewal of the lease, relocation costs or make good costs under the lease, replacement of obsolete equipment and computers, cost of replacing stock or property in the event of fire, flood or other damage or other destruction (irrespective of whether insurance policies cover these areas), replacement of signage, vehicles, telephone systems, furniture, plant and equipment etc.

This disclosure item could be improved by requiring the franchisor to disclose the relevant clause in the franchise agreement or associated agreement that has that corresponding obligation. This may highlight where the obligation arises even if the range or amount of the expenditure cannot be estimated by the franchisor.

The wording of the item is imprecise and often lawyers have suggested that if you follow the strict meaning it is difficult if not impossible to disclose something that is "unforeseeable". Some guidance (such as a guidance note) on its meaning and application would be beneficial. In my view the clause could be improved so that it highlights the likelihood of these events occurring and cross references to the relevant obligation. Alternatively the Department could develop a series of matters in the same way that Item 17.1(a) to (s) operates of things that the Department believes are typical **foreseeable capital expenditures** which may not necessarily be **quantifiable** at the time disclosure is given. These expenditures presumably are not limited to capital payments to the franchisor or associates of the franchisor but expenditures of any kind or nature to third parties.

Attribution of legal costs (item 13B):

This item heading talks about costs of dispute resolution NOT Reimbursement of legal costs generally. Arguably it deals only with costs of dispute resolution that goes to mediation (as opposed to breach notices that do not go on to mediation under Part 4 of the Code). This is because Part 4 talks about resolving disputes and giving dispute notices rather than notices of breach issued under clause 21 that may not escalate to a notice of dispute under Part 4.

The section also does not provide for disclosure of every obligation under the franchise agreement or other documentation to reimburse for other legal costs such as for reimbursement for legal costs for a new grant of for documenting renewals, transfers, amendments requests for consent to a transfer that does not proceed or to a relocation or for other agreements such as leases occupancy agreements or other documents like charges and security agreements etc. It could have dealt with these as well to give meaningful disclosure. In many cases it is included in Item 13.6 but quite often it is general and limited to things such as costs of documenting grants, renewals and transfers or novations.

Disclosure of rebates or other financial benefits Items 9.1 (j) and (k):

There appears to anecdotal evidence of compliance with this item however franchisees still request details of the rebates or financial benefits which franchisors usually withhold for commercially sensitive reasons.

Financial reports of marketing funds (Item12):

There is an interpretation problem whether the marketing fund financial year should be 30 June or the actual financial year of the franchisor.

Refer to my comment about this below and having this fixed urgently.

There remains a commercial problem with these provisions where the franchisees are required to reimburse the franchisor or an entity associated with the franchisor with their fair share of a

cost incurred or payable by the franchisor (or the associate) on their behalf collectively in circumstances where there is no separate fund or bank account brought into existence and it is simply a reimbursement of the cost (rather than something that the franchisor can recover its administration costs for).

Examples of this may include a "yellow pages" listing obligation for franchisees to pay their share to reimburse the franchisor its costs for paying for the group listing.

Another example may be the costs of the annual conference collected and run at cost or subsidised by the franchisor at a loss.

The administration costs of preparing an Annual Financial Statement (an AFS) and then to subsequently audit and conduct a vote for non audit are uncommercial where there are no funds available to do so.

It is submitted that an obligation for a franchisee to make a payment of a kind which is simply a genuine reimbursement of an expense should be treated as not amounting to a marketing or cooperative fund for that requirement of the Code.

There is no express consequence in the Code of what happens if the franchisor either fails to do the AFS or conduct the vote or have the AFS audited.

There could be greater clarity on this and expressly require the AFS for the last financial year to be available for inspection or provided with the Disclosure Document together with opening and closing balances of the fund as at end of the financial year and whether there are material arrears owing to the fund by franchisees, the franchisor or others who are required to contribute to the fund.

Franchisors should also be required to give an opening and closing balance of the fund (as at end of financial year) when requested so franchisees can determine whether there are significant arrears or loans in place with the franchisor that must be repaid. Any commercial terms of a loan should also be disclosed.

One solution may be to impose in the Code a provision that prevents the franchisor from recovering from the fund the costs of preparation of the AFS or the audit if it does not comply with the time frames. Similarly it would be possible to amend the Code to prevent a franchisor from being able to claim its reasonable administration costs out of the fund under clause 17(4) of the Code. These may be additional forms of direct relief besides penalties.

Some clarity in the form of a guidance note would be helpful about what "give" means.

For example is it sufficient to give the franchisee an annual financial statement of the marketing fund by simply sending an email with a link to a secure intranet webpage or is it necessary to physically give a pdf copy personally or by mail, email or facsimile.

There is no guidance in the Code about how a notice or document must be given under this section or the Code generally. In addition it would be useful to make some guidance notes clear on the voting process.

For example it should be made clear that a franchisor cannot treat a failure by a franchisee to cast a vote or respond to a request to vote as a positive vote in favour for non audit simply because the letter says that is how the voting process will occur. There is anecdotal evidence that at least one franchisor has tried to do so.

It should be made clear in the Code or a guidance note whether:

(a) The reference in clause 17(2)(a) of the Code to "*75 % of the franchisors' franchisees in Australia, who contribute to the fund*" is intended to include only franchisees who are not the Franchisor or associates of the Franchisor. It is often argued by Franchisors that they should have one vote for each corporate store they own where they contribute to that fund on the same basis as well as clarifying whether a franchisee would include a corporate franchised businesses operated by an entity associated with the Franchisor who pays to that fund.

(b) Similarly if a franchisee owns multiple franchises (in one or more entities) should it get one vote per franchise or is it one vote per person or if different amounts are contributed can the vote be weighted by reference to the amount contributed.

(c) Whether a franchisor can refuse to conduct the audit where there are insufficient moneys in the marketing fund to cover the costs of the audit which would otherwise require the franchisor to lend money to the fund or bear the expense itself until it can be recouped.

Financial details of the franchisor (Clause 20 of the Code):

The changes to clause 20 did not go far enough to deal with new franchisors who cannot provide 2 completed financial years of financial reports or who were not able to sign a solvency declaration as at the end of the previous financial year because they were not incorporated at that time.

Also the declaration does not contemplate the appointment of an administrator or controller to the franchisor or what sort of solvency (or insolvency) declaration an administrator or liquidator would be required to give if it has to provide a disclosure document to a franchisee or prospective franchisee or master franchisee.

In Clause 20 of the Code the obligation to give either 2 financial years worth of financial reports or an audit report to support the directors' solvency declaration continues to be an issue for new franchisors who have not been in existence for at least 2 completed financial years.

There should be an amendment or guidance note to make it clear that if you cannot give the 2 years financial reports then you must complete an audit report. It could also be made clearer:

(a) If there is only one years' worth of financial reports is that sufficient or must they do the audit report (there have been occasions where I have seen only one years financial reports and no audit report);

(b) That if at the end of the last financial year the franchisor was not in existence (e.g. not incorporated until the current financial year) then what is to occur to both the solvency declaration and the audit report. The Code does not take into account commercial practice and recommended structuring advice that a separate new entity operates as the franchisor and often IP and corporate stores or supply arrangements are through associated entities.

For example if the franchisor was not in existence at the end of the financial year there should be an option to allow the declaration to be given as at the date of the declaration (which might be as at a date in the current financial year). This allows the franchisor to comply. It should also allow the party to give further information if the franchisor was not solvent at that time to allow an external administrator/ liquidator to use appropriate wording that does not require an admission of solvency either at the time the external administrator/ liquidator has to provide a disclosure document to a purchaser of the system or a franchisee.

What is meant by a "financial year" – the period ending 30 June or the actual franchisor's financial year?

The Government in a previous review removed the old Clause 9 of the Code. Unfortunately that clause included some very important words that enabled franchisors to give disclosure by reference to the *'financial year of the franchisor'*.

Not every franchisor's financial year ends 30 June. There are many franchisors and master franchisees who have financial years that are different to 30 June. There has been some concern that the ACCC now take the view that financial year must be the period ending 30 June each year. This needs to be clarified and fixed as if it is correct it will lead to immediate adverse consequences to franchisors who have always disclosed by reference to their financial year.

It would also mean unnecessary duplication of financial reports (and consolidated reports) and audit reports to align to a 30 June period, this could not have been intended.

As financial year is not defined this should be immediately fixed to ensure that it relates to the financial year of the entity disclosing (e.g. the Franchisor or if joint disclosure is given in respect to each entity their respective financial year). Often a US head franchisor will have a 31 December financial year end whereas the Australian master franchisee has a 30 June year end. Reconciling these in various parts of the disclosure document – Tables in item 6, Marketing statements and audit reports, solvency declarations and financial reports are all affected by this.

Leasing arrangements:

I am not aware of problems with disclosure in this area particularly under the Retail Shop Leases Act applies to the type of occupancy agreement.

Earnings Information and projections and forecasts (item 19):

There remains a problem with the Code provisions that deal with the provision of earnings information and the risk of information supplied that may constitute a projection or forecast. This problem existed before the amendments in 2010 and remains an issue for the sector.

As a consequence of the risk of litigation most franchisors are reluctant to give turnover or earnings of other franchisees that have been reported because they have not verified that data or they are concerned about making a representation that this prospective franchisee could do as well as or better than the franchisee who provided the information.

As a consequence often a franchisee cannot get meaningful information for greenfield franchise opportunities whereas actual trading data for the sale of an existing franchise is available and more reliable.

Often historical data is provided to franchisors by franchisees and then reproduced in some format. It may be impractical to give all historical franchisee data of every franchisee to a prospective franchisee to allow them to conduct their own due diligence. There remains a diverse practice of how to present that information to minimise risk of litigation arising from a representation being made of earnings or profit.

Whilst disclosure of the typical costs assists it then requires the franchisee to make a decision in its planning about how much income or profit it is likely to make. Franchisees commercially look for guidance from franchisors and other franchisees. Franchisors are still reluctant to give earnings information about income, revenue or profit other than for the actual store being sold.

Actual store figures involved in a sale of an existing franchise can be verifiable however

greenfield franchises make comparison to benchmarks or averages or quartiles a difficult concept. As a consequence some systems advise prospective greenfield franchisees to make enquiries of other franchisees to identify turnover and costs.

There exists a lack of understanding and a legitimate concern by franchisors on how to present meaningful financial earnings information to franchisees including operational costs of running the franchise (which would fall within the meaning of "earnings information") without it constituting a projection or forecast. As a consequence many franchisors refrain from giving financial *earnings information* which may be useful as they are concerned it may be a projection or forecast of earnings or profit.

There is no definition of what is a *projection* or *forecast* contained in the Code. Education in this area and a simple explanation or guidance note with examples would help. As a consequence there remains a lack of access to franchisees of information to enable them to prepare meaningful plans because of the perception of risk of litigation.

Franchisees must still rely on their own due diligence and often the willingness of other existing franchisees to provide data or meaningful information to enable them to complete their own business plan.

Many franchisors do not want to require prospective franchisees to submit business plans to them as they may show a level of prospective earnings the franchisee may think it will earn. A franchisor cannot approve the business plan without the risk that the approval amounts to a representation as to a future matter (i.e. the level of earnings or profit that can be achieved) and then having the onus of proof under the ACL to demonstrate they had "reasonable grounds" to make that representation.

It would be useful if a franchisor could supply without the risk of being sued a Chart of Costs which may present typical or average costs for running a franchise in that region or nationally so franchisees can use it to identify in a user friendly way the variable and fixed costs or range that franchisees have reported. Similarly disclosure of revenue figures for the highest, lowest or average reported revenue of an existing franchised store and or corporate store should be able to be disclosed without fear of it constituting a projection or forecast. A franchisor should be deemed to have "reasonable grounds" to make a representation where it provides that information in a specified format.

Also if the franchisor can provide a range of revenue in a format for example High /Low /Average or by reference to certain quartiles then it should have some form of safe harbour protection which I understand occurs in the US. At the moment the reverse onus of proving you had reasonable grounds to make a representation justifiably concerns franchisors and the outcome is that this means what could be meaningful financial information is not made available and makes meaningful preparation of business plans problematic.

4. Does the sector have any concerns regarding the operation of these amendments?

Response:

Yes it is still an issue as the amendments did not solve the problems in the areas identified in the response to Question 3.

Contract variation transfer and novation:

5. **Have the amendments regarding unilateral variation, transfer and novation been effective in addressing concerns about franchisors' ability to make changes to franchise agreements? Why or why not?**

Response:

No they have not. They still cause confusion and do not help to disclose useful information.

There is still ambiguity about whether you disclose operations manual changes *(where the operations manual does not form part of the franchise agreement), whether you have to disclose a list of the changes every time you may update the "*then current form of franchise agreement*" you may offer for new franchisees or for use in a transfer, novation or renewal.

The wording in the code dealing with "Transfer" and "Novation" is flawed and remains a real commercial problem as the wording of the Code and especially the amendments to the Code do NOT reflect normal commercial practice in the sector.

Unilateral variations Item 17A

There remains a degree of confusion and therefore an inconsistency in this item of disclosure about what is a unilateral variation to a franchise agreement that must be disclosed under this item.

There are several reasons for this confusion arising from the practical application of the change:

(1) I believe that most lawyers would interpret this to mean a change unilaterally forced on a franchisee by the franchisor under an existing franchise agreement to vary an existing provision of a franchise agreement without having to get the franchisees consent at that time. Alternatively there may be a right to require a change to the agreement (and require the franchise to sign an amendment deed) under the contractual terms that the franchisor has a unilateral discretion to implement it.

In other words a change that is forced on the franchisee that has commenced to apply since 1 July 2010 that may affect an existing franchise agreement entered into on or after 1 July 2011 (the wording of Item 17A.1).

An example may be where the franchisor has a power to change a territory or Prime Marketing Area in a franchise agreement entered into on 1 December 2011 unilaterally as population demographics change in 2012 and follows the provisions of the agreement to change the territory or Prime Marketing Area by notice for an existing franchisee say on 1 July 2012.

(2) Another commercial difficulty relates to when and whether a unilateral variation has actually occurred – for example when a franchisor wants to update and make a change to the *then current version* of the franchise agreement offered to prospective franchisees for new grants or to a prospective purchaser from the franchisee on a transfer, novation or offered to a franchisee when they exercise the right to renew an existing franchise agreement (a *relevant event*).

The franchisor may have the right in that event to change the *new form of agreement* to be signed upon a *relevant event* but would argue that it does not actually vary the terms of the existing agreement with the franchisee and therefore NOT amount to a unilateral variation requiring disclosure under this Item.

(3) In the later case these updates to the *then current version of the franchisee agreement* do not or may not immediately commence to apply to pre-existing franchise agreements irrespective of whether they were entered into before 1 July 2011. (*Item 17A.1 relates to disclosure of unilateral changes to EXISTING franchise agreements entered into in financial years that commence on or AFTER 1 July 2011*).

I am only aware of one US system operating in Australia where a franchisee who may be granted a second franchise signs a new agreement for the new franchise that deems both the new agreement and the old agreement for the other franchise to be on the same terms as the new agreement. This would be an example of a unilateral variation of a whole agreement to the then current version because they acquired a second franchise and the franchisor wanted all of the agreements to be on the same and most current form.

(4) An update to a template "*then current franchise agreement*" offered to new franchisees may not unilaterally apply immediately or affect an existing franchisee unless and until the *relevant event* occurs. As a consequence their existing franchise agreement may not be unilaterally varied (or affected) until the transfer, novation or renewal occurs and the variation would be to replace the entire old agreement with the *then current version* at that time. In that event it is a new agreement for the franchisee (or transferee or novatee) to sign which may vary the old terms but it is still a new agreement.

(5) Typically it is generally accepted that an amendment by the Franchisor or head franchisor to an Operations Manual (if it is expressed to form part of the franchise agreement or is incorporated by reference) would require disclosure under Item 17A. It would be beneficial to the sector that the Government understand this commercial practice as most franchise agreements do NOT now deem it to be part of the franchise agreement but as a separate set of policies and procedures that must be followed.

(6) That change in practice started as a consequence of earlier changes that were made to the Code that expressly allowed a franchisee the right to keep the disclosure document if it did not proceed with the franchise AFTER disclosure was given irrespective of whether the franchisee entered into the franchise agreement and terminated during the cooling off period or continued.

(7) If the Operations manual formed part of the franchise agreement then it would have to be disclosed by annexure to the Disclosure Document and the franchisee could keep it even after the term of the franchise despite any contractual obligation to return it. Franchisors do not want their intellectual property and core policies and procedures to be used, they want them kept confidential and returned if the prospective franchisee does not proceed or the agreement ends.

A more commercial way to deal with this is to require a franchisor to give access to the operations manual to a prospective franchisee before it signs the franchise agreement that will allow them to read it but not allow them to keep it.

You would need to separately define what an operations manual and change the provision in Item 23 to ensure it is clear they cannot keep it. If this occurred franchisors would be more likely to disclose changes to operations manuals under this Item. Also a simple change that requires the franchisee to return any intellectual property of the franchisor (such as the manual) within 7 days if the prospective franchisee does not proceed.

(8) As a consequence for protection of their intellectual property many lawyers draft the terms of their franchise agreements so that the operations manual is NOT to be part of

the terms of the franchise agreement and therefore any changes made are not therefore a unilateral variation to the franchise agreement and are not therefore disclosed.

(9) Also any increases in fees or rights to increase fees that affect existing franchise agreements where they are unilaterally determined by the franchisor or head franchisor should also be required to be expressly disclosed.

(10) Arguably a transfer or novation by the franchisor of its rights to a new franchisor would also amount to a unilateral variation as well as the franchisee would need to sign new documentation.

(11) Most franchisor lawyers have since the amendments were introduced included general comments in their clients disclosure documents (under Item 17A.3) about the ability of the franchisor to vary the franchise agreement that will be used in a transfer, novation or renewal of a franchisee's agreement as the then current version of the franchise agreement may be updated periodically for changes to the law or for commercial reasons.

(12) Arguably changes to the then current version of the franchise agreement from time to time may not be unilateral variations to an existing franchise agreement if they do not apply until a transfer or novation or renewal event occurs.

(13) If it was the intention that after 1 July 2010 every franchisor must list every update it makes to its current version in the franchise agreement even if it does not commence to immediately apply to existing franchisees then this should be made clearer in Item 17A the same should be considered for Operations Manuals.

(14) A unilateral amendment to a franchise agreement by a franchisor may not necessarily amount to an "*extension of the scope of a franchise agreement*" as that expression was intended to apply when it was added to the Code in the last 2010 amendments.

As a consequence the application of clauses such as clauses 6A(a), 11(1)(a), 11(3), 13(2) – cooling off, do not apply to unilateral variations that arise from the exercise of a right, power or discretion. An example may be where a franchisee has a defined Prime Marketing Area that is linked to a determination or discretion of the Franchisor to define it or amend it during the term. There may be no need to enter into an agreement to document it, the change occurs by notice, not by entering into an agreement to record it.

It is not uncommon in the motor dealership sector for KPI's (such as minimum sales or stock levels) and PMA's to be changed unilaterally and it may have a significant commercial affect on a dealer. That change may not "*extend the scope*" of the agreement but simply vary the contractual application of a right or obligation substantially so that in essence it is a significant variation to the commercial application of an obligation under an existing agreement.

As a consequence a franchisor may not have to comply with clauses 11(1)(a), or 13(2) because it is not required to "*enter into an agreement* to ...*extend the scope*". The words "*enter into an agreement*" suggest a formal agreement being negotiated and signed rather than simply a franchisor giving notice of a unilateral change.

This sort of change may be argued to be "*unconscionable*" in all of the circumstances, however a franchisee has little recourse because it has no say at all in its application and if it wishes to pursue that action it will invariably end their relationship. This sort of

conduct highlights the imbalance that can occur in the relationship where a wide discretion to change important aspects can have a significant and immediate adverse effect.

It is not clear if this change was intended to require franchisors to get a Clause 11(1) statement before they vary the terms of the franchise agreement at all or through the exercise of a unilateral right, power or discretion.

As the expressions "*extend the scope*" and "*extension of the scope*" have never been defined it is difficult to identify what changes were intended to be captured and whether a variation to an agreement that changes the scope but does not add to it (but rather reduces it) amounts to an "*extension*".

Clarity in this area is now needed both as to what is meant by "*extend the scope*" and "*extension of the scope*" and also how it fits with unilateral variations and in fact any variations to the terms of the agreement generally.

If the policy intent is to get Clause 11(1) statements before a variation occurs (including a unilateral variation) then that needs to be made clear.

Provide a list of changes for a renewal of an existing franchise agreement

Given the purpose of disclosure in Clause 6A of the Code for renewal it is important for a franchisee to know when it goes to renew whether it will be on the same terms as its old agreement or on the then current version.

Often it is confusing to track what has changed to the agreement since they first signed it and can be more expensive because a lawyer has to review the 2 agreements to identify what has changed.

Also given the current commercial practice of the franchisee being required to exercise its rights to an option to renew (and there being no obligation to give the disclosure document with a notice to renew under Clause 20A to a franchisee) disclosure of these changes does not happen until the execution copies go out to a franchisee.

At that stage it is too late and from the time they exercise the option to the time they finally sign they may not know what the renewal terms will be. It may be useful for a notice required to be given by a Franchisor under Clause 20A to accompany the Disclosure Document to effect the renewal.

Potential improvements in disclosure for franchisees would include a change in the wording of the item so that in addition to any unilateral variation to an existing franchise agreement a franchisor must provide disclosure to a franchisee at the time they are renewing their franchise agreement *(but on the then current terms of the franchise agreement unilaterally required by the franchisor*) or to a prospective franchisee receiving a transfer or novation a list under this Item or separately identification of the relevant clauses that have changed from the original franchise agreement they entered into or the previous franchisee had applying to it.

Some franchisors I have heard offer a highlighted redlining and strikeout copy to show what has changed since the franchisee entered into its existing franchise agreement. This can significantly simplify and expedite the renewal process.

Which change to the then current version applies over time?

It is important to remember that during the term of a franchise the *then current version of the*

franchise agreement may be changed or updated for many reasons including for changes in the law or as a consequence of new legal representation requiring totally new documents and as a consequence it may be that the version that actually unilaterally varies the original franchise agreement is not able to be determined until the actual trigger event (transfer, novation or renewal) occurs.

The changes at that time (and how they differ to the original franchise agreement) may be far more relevant for the purposes of meeting the purpose of disclosure under clause 6A of the Code. It also would prevent unnecessary disclosure of changes made that subsequently no longer apply and are accordingly now irrelevant.

Unilateral changes during the term that are unfair or change the nature of the rights granted

Many proponents for change argue that a franchisor should not be able to unilaterally change the terms of the franchise agreement during the term and that this should be entrenched in the Code. That concept does not sit well with franchising where the model must adapt during the term to survive. Also most franchise agreements contain provisions that allow the franchisor to have the franchisee sign the then current franchise agreement upon a relevant event occurring.

A possible solution could be to provide a Code right to a franchisee that allows them to challenge a unilateral variation made during the term if that change is unfair or unconscionable. That unilateral change could relate to all of the franchisees generally or that franchisee specifically.

This review ability would need to work with the existing unconscionable conduct provisions that would allow a franchisee a right to approach the courts when a franchisor seeks to unilaterally change its franchise agreement during the term if the franchisee believes in all the circumstance the change is an "*unfair term*" being forced on them that significantly adversely changes the nature and extension of the rights granted to them.

I say this reluctantly because I believe that currently for a franchisee to get relief on the basis of a change in the franchise agreement amounting to unconscionable is a "*high bar*" to reach.

I am not a supporter of the suggestion that the unfair contracts regime should apply to franchise agreements, however there is merit in the argument that once the parties have negotiated the agreement a unilateral variation of a material right or obligation should be subjected to a form of scrutiny as to whether it is unfair or unconscionable. How that would work in practice is unclear but may provide an easier way to maintain balance in the relationship.

As a consequence a franchisor seeking to change its agreement unilaterally during the term possibly should be obliged to demonstrate that the proposed change is a "fair term".

Transfer and novation

The changes made to the Code over time in clause 20 have proven to be problematic.

They include:

(a) A definition of Novation that reflects ONLY a pure legal novation of *the franchise* on the same terms as the *terminated franchise*. It does not refer to the terms of the "franchise agreement" or "terminated franchise agreement" specifically. You then have to go to the definition of a "franchise" to identify what actually terminates.

Novation as defined in the Code is a narrow type of transaction that would not include

the entering into of a new agreement where any of the terms changed such as allowing the purchaser to reset the term of the franchise from what is the balance of the term remaining to a new 5 year term. Often franchise agreements allow for that process to occur. You would therefore have to treat it as a "transfer" and not a "novation". Many if not most agreements would contain clauses like this.

The wording does not contemplate that a sale of a franchise can occur by way of the old agreement ending and a new agreement being entered into by the purchaser on the "then current terms and conditions" being entered into. This typically happens on a renewal or a transfer of the franchise. Many franchise agreements continue to use a different form or concept on a sale (but may refer to it as novation) in their clauses so that the outgoing franchisee and guarantors are released from some but not all of their obligations (such as restraint, confidentiality etc) and the prospective transferee signs a new agreement on the then current terms.

(b) There remains an inconsistent use of terminology in clause 20. Clause 20(1) refers to consent to a transfer or novation of the "*franchise*" where the definition of transferee in clause 20(5) refers to a "*transfer or novation of the franchised business*" - arguably it is the *franchise* or the *franchise agreement* that is novated and not the "*franchised business*" and the assets comprised in the *franchised business* are transferred or sold when the rights under the franchise agreement are novated or transferred. The word "franchise" has a defined meaning and does not include the words the "franchised business".

(c) The definition of Novation refers to "*in relation to a franchise*" rather than in relation to the "*franchise agreement*". The terminology in the Code does not reflect the way in which franchisors typically require franchise business sales to occur. It is common for outgoing franchisees to be required to sign some form of deed which may as a consequence contain a mutual release of future obligations (other than continuing obligations such as restraints etc) at the same time the incoming franchisees sign a new franchise agreement on the then current terms offered by the franchisor.

The normal and well accepted legal concept of novation looks at the consequences of novation (namely the end of the existing contract). Most lawyers equate that concept with the example of a novated car lease where one party drops away from all liability or obligation and the new party will enter into the agreement (but on the same terms as the old agreement) with the other party. This form of novation does not contemplate the ongoing contractual obligations such as restraint and confidentiality that always normally continue to exist after the termination, expiration or transfer of novation of a franchise on the franchisee and guarantors and may be less likely to apply for a sale by a franchisee but apply if there was a novation by the franchisor or its rights to a purchaser of the system. So in reality a pure novation does not really occur without some other form of deed being put in place both with the outgoing franchisee and a deed of novation or new franchise agreement with the incoming buyer.

(d) I have seen arguments in the sector (which I do not agree with) that the wording of Clause 20 of the Code somehow grants the franchisee a statutory right to chose whether to request a sale by EITHER transfer or novation despite what the terms of their agreement say about the process of them selling their franchised business (including the rights under their franchise agreement). Most franchisors do not want their franchisees to simply novate the agreement but will allow them to sell their franchise if the buyer signs a new agreement on the then current terms and the outgoing franchisee signs a deed as well.

Arguably the intention of Clause 20(2) is clear, namely to ensure that the franchisor's

consent to a franchisee wanting to sell their franchised business could not be unreasonably withheld.

It appears in some circumstances franchisees are seeking to argue that this gives them the right to insist on a pure legal novation as defined in the code when the franchise agreement and escape ongoing liability to the franchisor or changes to the then current version of the franchise agreement being required to be signed by a purchaser (which may be different terms) even though when they entered into the agreement they agreed to a method that expressly provided the way in which the transaction was to proceed.

The wording in the Code needs to be clearer particularly if penalties and a good faith obligation is included.

I would suggest that the definition of Novation be amended to amend the words "*on the same terms*" to capture also agreements to be signed that are on the then current terms so it reads "*...on the same terms or different terms...*". This could fix the problem with different meanings of what a novation really is otherwise the commercial reality of how franchisors deal with a sale would have to include in the definition of transfer this arrangement.

It may be beneficial to then include adding words to the definition of "Transfer" that refers to the process (if any) set out in the franchise agreement, so that it is clear that if the agreement sets out the process then the franchisor cannot withhold its consent to the sale of the franchise unreasonably.

(e) To ensure that Clause 20(2) is unambiguous it should also be amended to read:

"*A franchisor must not unreasonably withhold its consent to the transfer or novation of the franchise where the franchisee intends to transfer or novate the franchise in accordance with the terms specified in the franchise agreement.*"

(f) It is essential that Clause 20(3)(b) should also now be amended to add the words "*or the franchisee*" after the words "*proposed transferee*" that it is reasonable for a franchisor to withhold consent if the franchisee or the proposed transferee does not meet a reasonable requirement of the franchise agreement for the transfer or novation. Currently franchisors would argue that however it is not an express circumstance and should be.

As a consequence the whole transfer and novation concept for sales by franchisees to other franchisees as well as a sale of the whole franchise system by a franchisor needs to be carefully reconsidered and updated to ensure that existing anomalies and definitions and problems do not continue.

(g) The application in practice of clause 20(4) also causes problems when trying to identify when the 42 day period commences to run. Often franchisees write to their franchisor seeking consent to a sale but they provide NO information about a potential purchaser or the intended terms of the contract of sale to enable the franchisor to make an informed decision whether to consent or not as it is unable to evaluate the proposed purchaser or guarantors.

The Code should provide that the period commences when all information reasonably required by the franchisor under the franchise agreement has been provided. Unfortunately it doesn't suggest when it starts other than the implication that once the franchise has made a request in writing that the time period starts.

As a consequence of franchisees having NO EXPRESS Code obligation to provide that information to start the process, it can lead to uncertainty of when the 42 day deeming period commences. I suggest the wording be clarified so it is clear when the time period commences and place an obligation on the franchisee to provide all information required under the franchise agreement to enable the franchisor to be able to properly evaluate the request.

Otherwise it should be expressed to be permissible that the franchisor can give a conditional consent subject to the parties complying with their obligations to supply documentation and information and comply with other provisions of the agreement even if to do so may take longer than 42 days from the initial written request.

I have also noticed in many recent transactions that franchisees and prospective transferees are seeking to settle sales of their businesses without co-operating with the franchisor to allow disclosure to properly occur.

As a consequence of there being no express prohibition being imposed on a franchisee from selling its interest in a franchise until after the prospective transferee getting disclosure they can simply settle and leave it to the franchisor to worry about their compliance obligation.

(h) One other very concerning problem with the amendments related to Clause 13(2) of the Code.

Clause 13(2) clearly provides that the 7 day cooling off period does NOT apply to a "*transfer*".

Unfortunately for some reason it does not also expressly say it does not apply to a "*novation*".

It is not clear if this was intentional or not or simply a drafting mistake. The definition of "*transfer*" does not include "*novation*" and throughout the Code reference appears to transfer or novation as if they are separate distinct meanings and consequences.

As a consequence there appears to be a question whether the code allows a franchisee a 7 day cooling off period if the franchise agreement is to be novated (as opposed to assigned or transferred).

The definition of "*transfer*" clearly contemplates the sale, grant or transfer of a "*franchise*". If you then look at that definition for assistance a "*franchise*" includes "*the rights and obligations under a franchise agreement*".

Most lawyers would treat "*transfer*" as referring to the older method of assignment of the existing terms of a franchise agreement like an assignment of a lease which would be on the same terms as the existing lease and the assignor would remain liable under the original lease. In this method there is no termination and any release of the outgoing franchisee or guarantors may be dependent on signing a deed of release.

As a consequence of that drafting mistake if a franchisor seeks to novates its rights there is the likelihood of a serious and unintended consequence where an opportunistic franchisee may argue that it either refuses to sign a novation agreement or that it has 7 days from entering signing the novation agreement within which it can get out of its contractual obligations.

This makes the sale of a franchise network extremely difficult because the franchisor is selling and wanting to novate all of the franchise agreements to the purchaser.

Usually a novation agreement is prepared and signed rather than a whole new franchise agreement and the incoming buyer gives the disclosure document with their existing franchise agreement and the novation deed and obtains the statements in writing required under clause 11.

This problem is made worse because clause 13(1)(a) is couched in language that suggests that the existing franchisee entering into a new franchise agreement with the buyer of the system has a right to terminate within that cooling off period as a consequence of entering into the novation agreement. Commercially that consequence could never have been intended.

Also if franchisees have some right to refuse to sign up with a transferee or novatee why then do they also not have a corresponding obligation similar to that imposed on a franchisor not to unreasonably withhold its consent or cooperation. Arguably absent a share sale arrangement the sale of a franchise system by novation of existing agreements can be very complicated and difficult.

6. **Does the sector have any concerns regarding the operation of these amendments?**

Response:

Yes refer to the detailed Response to Question 5.

Novation and transfer need to be fixed to bring in line with commercial practices in the sector and to avoid language issues if the code is to include penalties and good faith

Disclosure regarding franchisor conduct:

7. **Have the changes to the Franchising Code led to improved franchisee knowledge about franchisors and their conduct before they enter into franchise agreements? Why or why not?**

Response:

I am unable to provide anecdotal evidence. Possibly franchisee lawyers have been advising their clients on these issues.

In relation to the specific examples given in this part:

Access to franchisees – yes, contact details can assist but there is always a question whether the details of former franchisees are current as there is no obligation to track and update them when they leave the system.

Confidentiality clauses - yes probably greater consideration of the circumstances where an obligation or document that contains those provisions is to be signed.

Materially relevant facts – yes

Undertakings - yes

Good faith – no, clause 23A does not really assist at all.

This information is difficult to obtain and measure.

8. **Is the information being provided useful to franchisees?**

Response:

Yes some information is of use. Although more relevant publications from the ACCC and education programs for franchisors on these obligations or a set of frequently asked questions and answers on these areas would also be beneficial

9. **What effect has the requirement to provide this additional information had on franchisors?**

Response:

They do not appear to be onerous obligations to disclose

10. **Does the sector have any concerns regarding the operation of the new provisions?**

Response:

No

Disclosure exemption for foreign franchisors:

11. **What impact has the removal of the foreign franchisor exemption had on the sector?**

Response:

The problems with compliance by overseas head franchisors remains an issue but not because of the removal of the exemption.

There remains a consistent problem with the disclosure required to be given by head franchisors who have appointed Australian Master franchisees.

These problems are not new and include:

(a) The fact that typically financial years of foreign franchisors are not typically ending 30 June and as a consequence the periods do not marry up for giving joint disclosure.

(b) It is problematic to have ongoing disclosure obligations under clause 18 of the Code for foreign franchisors when it should be incumbent upon the Australian Master franchisee to be able to give that disclosure for both.

(c) The template Annexure 1 does not provide flexibility for overseas head franchisors to give separate disclosure about the nature of the master franchise and explain in simple terms what a franchisee needs to know. The items are not always relevant to disclose

core important information about the relationship between the head franchisor and the Australian master franchisees to give meaningful information that is not simply a duplication.

Recommendation:

It would be useful for another Annexure to be developed and able to be used that specifically addresses relevant information a head franchisor should disclose to a franchisee that deals with the essential obligations that have been delegated under the master franchise agreement and what impact it will have on the franchisee if the master is terminated or not renewed. This will avoid duplication of the same information.

12. Has the removal of the exemption caused any issues?

Response:

I have no specific anecdotal evidence of it causing any issues.

Efficacy of the disclosure amendments as a whole:

13. On the whole, do the 2008 and 2010 disclosure amendments ensure franchisees are provided with adequate information?

Response:

Whilst it provides more relevant information than they previously had, there are areas of disclosure that could always be improved for more meaningful information to be given. Many of these suggestions have formed part of previous submissions to government.

In particular specifying a new template Annexure 3 for Head franchisor disclosure would be beneficial to disclose more relevant information to sub-franchisees about the nature of the master franchise granted here in Australia. The Code would need to be amended to reflect that either joint disclosure could be given or the Head Franchisor could complete Annexure 3.

In reality the information to disclose should be reduced to avoid duplication and tailored to specific relevant information that can improve the franchisees understanding of the master franchise relationship and how the franchisee is affected. It should include things such as:

(a) Whether the head franchisor is to be a party or have step in rights or obligations if the master agreement expires and is not renewed, or is terminated or the master becomes insolvent;

(b) If the agreement is a territory development agreement a summary of the obligations to grow the network in Australia;

(c) Intellectual property ownership and use;

(d) Details of the term, renewal and rights of either party to terminate;

(e) Whether it is necessary to give Financials of the head franchisor and if necessary a

	solvency declaration – Audited accounts should not be necessary;
(f)	What security interests have been granted over the intellectual property (e.g. the nature of secured creditors rights can affect the right of a franchisee to use or continue to use the IP in the event of an insolvency);
(g)	Whether there is a right to acquire, merge with or establish a competing or complimentary network that may be linked or cobranded. There are many examples of companies that operate multiple systems that are in some ways connected. The effect of this should be at least disclosed and how the different businesses may intersect (e.g. through common loyalty programs, shared marketing funds, common suppliers and whether the supply terms are the same or preferential from one system to the other).

14. Is the extra onus on franchisors justified by the benefit this disclosure is providing to franchisees?

Response:

Yes.

Part Three: Good faith in franchising

Overview:

15. How effective were the targeted amendments in 2010 to the Franchising Code in addressing specific issues, instead of inserting an overarching obligation to act in good faith?

Response:

The additional disclosure obligation for end of term arrangements has been helpful to disclose what considerations are relevant. Greater consideration has been required to consider the consequences if the franchise is not to be renewed or the franchisee decides not to continue in the system.

Unfortunately the obligation to give renewal notices under Clause 20A has not really commenced to apply yet and the consequences of this amendment will become more relevant in 2013 and beyond when agreements entered into on or after July 2010 renew.

Clause 5(1B) of the Code makes it clear that the renewal notice regime applies only to franchise agreements entered into after 1 July 2010.

As a consequence the obligation to make the decision to renew or not under this amendment has not really been tested.

There are arguably practical problems with the wording of clause 20A – refer to my discussion paper contained in Annexure "B" provided to government in July 2012.

16. How effective is section 23A of the Franchising Code, which provides that nothing in the common law limits the obligation to act in good faith?

Response:

This section clearly contemplates that the Common law may imply an obligation of good faith into a franchise agreement that is regulated by the Code.

Refer to my discussion paper and comments about the ability of the parties to modify or exclude in a franchise agreement an implied obligation of good faith.

Clause 23A does not impose any obligation to act in good faith nor does the Code expressly seek to override a contractual provision that otherwise seeks to exclude or modify that implied obligation. Arguably it is left to the common law and the parties to approach the courts to argue that there is an implied obligation to act in good faith into their franchise agreement.

Express language to override existing contractual terms would be required if it is intended that good faith be included in dealings between parties to franchise agreements that are regulated by the Code.

That may require the code to be amended in clause 23A expressly to require the parties to a franchise agreement regulated by the Code to act in good faith in their dealings. The extent of its application needs to be made clear so the parties know whether it applies to agreements entered into before the amendment is made (e.g. all franchise agreements not just those entered into after the date the amendments commence).

A transitional provision should make it clear that it may apply to conduct after the amendment occurs under an existing franchise agreement but it should be left to the parties to argue whether the common law implied obligation applied up until that time to that agreement.

There may be franchise agreements covered by Oil code or not regulated by the franchising code (because they do not meet the 4 tests) that may have different obligations applying.

Clause 23A does not make it clear what happens if the obligation to act in good faith is imposed not by common law but because of some state based industry code (such as being proposed in SA) or what happens if "good faith" is defined in that state and the definition is different to the common law.

This potential overlap and inconsistency needs to be considered carefully in the development of any obligation of good faith into franchise agreements.

17. What specific issues would be remedied by inserting an obligation to act in good faith into the Franchising Code which would not otherwise be addressed under the unwritten law or by the ACL?

Response:

Many lawyers believe there is already an implied obligation to act in good faith which will be imposed by some courts in some states although this may not be uniform in every state or territory of Australia and the meaning of good faith continues to evolve with the common law.

Imposing an express obligation may override current judicial interpretation of whether there is an implied obligations in those states where the judiciary currently would not apply one.

If an obligation is inserted will it give rise to a right or remedy in the Code that gives some conclusive relief for a breach of that obligation or is it simply breach of a contractual term that

the parties must then take up in court to enforce.

If it does not make it clear then the consequences of inclusion of a good faith obligation would not be clearly understood by parties to a franchise agreement.

It needs to make it clear whether the obligation covers all dealings (contractual) as well in the performance of Code obligations (such as clause 20 and clause 20A, clause 21, 22 and 23 and Part 4 (clauses 24 to 31) which impose Code obligations to do or not do something as opposed to contractual obligations in the franchise agreement).

It would be beneficial to have good faith apply to dispute resolution not under Part 4 but any form of dispute resolution (under a franchise agreement) or that may arise as a consequence of the intervention of a State Small Business Commissioner seeking to get the parties together to mediate the dispute under their legislation (not the Code).

Issues such as who has the burden of proof (is it reversed to the party alleged to have not acted in good faith), what remedies are available and through what method are not satisfied simply by adopting a common law implied obligation or some codified obligation.

Any inclusion of an obligation to act in good faith would also have to take into account:

(a) How that change affects the interpretation and application of an existing franchise agreement and any express existing wording that may impose a different standard to apply in the exercise of a right, power or discretion – it may also have to deal with any express exclusion or modification of an implied obligation to act in good faith.

(b) How should it relate to and apply if there is a different defined obligation of good faith imposed under a state based industry code (for example if SA prescribe a industry code for franchising and impose their own codified and had a different defined obligation of good faith into SA franchise agreements).

(c) How does it interrelate with the concept of an express ACL obligation not to engage in unconscionable conduct. It should NOT follow that just because there may be a proven breach of an obligation of good faith that it should automatically equal or amount to "*unconscionable conduct*".

Refer to the comments in my discussion paper in Annexure "B".

18. If an explicit obligation of good faith is introduced, should 'good faith' be defined? If so, how should it be defined?

Response:

No, it should be left to the common law to evolve to the specific circumstances at the time.

This may however require a court of competent jurisdiction to consider it on a case by case basis.

Whilst it is always beneficial to have clear meanings this concept, just like unconscionable conduct is not capable of a one size fits all meaning.

19. If an explicit obligation to act in good faith is introduced, what should its scope be? That is, should it extend to: the negotiation of a franchise agreement, and/or the execution of a

franchise agreement, and/or the ending of a franchise agreement, and/or dispute resolution in franchising?

Response:

If an obligation was codified then in my view:

Who should it apply to - It should apply to all parties to a franchise agreement that is regulated by the Code. It is problematic to try and extend it to related entities and associates who are not parties to the agreement but may supply goods and services to the franchisee.

If a franchise agreement is not captured by the Code then arguably a common law implied duty of good faith under the common law may still apply.

What should it apply to – There is a temptation to "cast the net widely" and make it apply to all of their dealings whilst they are in the franchise relationship as this gives certainty and makes it clear it applies to all of the parties.

Alternatively on a narrower application it should at least apply to the exercise of a right or power and *the performance of an obligation* under the franchise agreement. In my view it should also definitely apply to the exercise of a right or power *and the performance of an obligation* under the Code.

It would be easy (but problematic) to suggest that the obligation be expressed to apply to pre-contractual negotiations. I think this is unnecessary as there are already extensive obligations not to mislead or deceive and the unconscionable conduct provisions which already cover this mischief. There is merit in applying it to post contractual obligations and negotiations after the agreement ends or is terminated.

It is more logical and less problematic that it should apply to certain specific problem areas such as clause 20 and clause 20A, clause 21, 22 and 23 and Part 4 (clauses 24 to 31).

There may be benefit in having it apply to all dealings between the parties during the term of the franchise agreement and also to post termination dealings that continue to apply after the term need to be considered as well.

For example franchisees and guarantors not observing restraint provisions is always a problem and often their conduct during the term in seeking to set up a post termination arrangement before the end of term to deliberately and dishonestly avoid the restraint could be said to be not acting in good faith.

Any implied obligation to act in good faith however should not be held out as some form of catch all remedy or argument to get quick and easy relief for any contractual or code breach.

Arguments have been made whether the obligation of good faith should extend to related entities of the franchisor or to a narrower "*associate of the franchisor*" in supply of goods or services to franchisees. This is problematic as they are not parties to the franchise agreement and arguably therefor not bound by the Code even though they may be an associate.

This would have to cover leasing companies supply companies and IP companies in which the franchisor (or its directors and owners) have an interest.

Franchisees have few powers, rights or discretions so unless amendments are to be made to add obligations then franchisees should be obliged to perform their obligations and act in their dealings with the franchisor in good faith.

Consideration needs to be given to whether an obligation to act in good faith should be expressly mandated to cover the conduct of parties in a dispute any mediation arising under Part 4 of the Code or arising from a dispute between the parties to a franchise agreement. Currently they must act in a reconciliatory manner and there are useful provisions in Part 4 of the Code however there is also evidence that dispute resolution may take place outside of the application of Part 4 and in that event arguable good faith may not apply in those processes.

Also it is important to note that not every mediation agreement would contain an express obligation on the parties to act in good faith.

20. If a specific obligation to act in good faith was introduced into the Franchising Code, what would be an appropriate consequence for breaching such an obligation?

Response:

The problem is that it all depends on the circumstances. One size does not fit all when it comes to relief and arguably that is why it is best left to the Courts to determine.

If the conduct relates to renewal or non renewal or the exercise of a right, power or discretion then arguably it may be appropriate (or at least tempting) to include a deeming provision similar to clause 20(4) that applies to a failure to give that consent or to give legitimate or lawful reasons.

However if third party rights such as landlords are affected then this sort of relief may directly affect third parties who are not subject to the Code and become problematic.

There may be specific parts of the Code to which you could craft a specified outcome for breach such as:

(a) **Clause 22** as to the determination and giving of "*reasonable notice*" of termination as well as to having legitimate and proper (as opposed to unreasonable or unfair) reasons for terminating "*on reasonable notice*" – The Code is silent on these points and it is often put forward that a party is not acting in good faith if it does not give reasonable notice or the reasons are not balanced against the loss or damage to be suffered by the franchisor. Often what is reasonable comes down to what loss is suffered and how long it would take to recoup that loss or damage by continuing to operate for a longer period of "notice" before the agreement can end.

As a consequence it is common for a party to argue the notice is unlawful and seek relief to have the notice set aside and declared to be ineffective and unable to be acted on. The automotive sector have argued for many years that agreements that allow for termination by notice (without cause) lead to a significant imbalance in the relationship and there should be a minimum term or a significant period of minimum notice to ensure the other party can mitigate or reduce its loss. A unilateral right to terminate without cause or even because of an inability to meet KPI's that are unilaterally determined and imposed during a term is most often found in motor vehicle dealership agreements and agreements in the automotive industry rather than in your typical quick service restaurant agreement even though both may be tied to tenure under a long term lease.

(b) **Clause 20A** for failing to give a renewal notice or appropriate notice or failing to act in good faith when it gave a non renewal notice – a deemed renewal is the logical answer for the latter however that may not be practical where third parties are involved like landlords who may not grant a new lease. An alternate may be if adequate notice is

given that they have to allow a holding over to ensure the complete notice period is given.

(c) **Clause 17** Marketing and other cooperative funds – failing to do the AFS or the audit or conducting a vote could result in a franchisor being specifically prohibited from recovering its "*reasonable costs of administering and auditing the fund*" under that clause either totally for that year or at least until it complies with the obligation. This gives a powerful financial incentive to comply or to pay for it themselves. Any deliberate and unlawful maladministration of the marketing fund should also prevent recovery of costs as well.

(d) **Part 4** – Failing to act in good faith in a mediation or a dispute resolution should result in a costs order being made against that party (for example if they do not turn up or act in a reconciliatory manner).

I have given some other examples in my Discussion Paper.

21. If a specific obligation to act in good faith was introduced into the Franchising Code, how would such an obligation interact with the provisions of the ACL?

Response:

There may be circumstances where the breach of an obligation of good faith may be extremely serious but still not amount to unconscionable conduct. It **should not automatically be deemed** to be unconscionable conduct as that may give rise to unintended consequences.

A breach of a codified obligation to act in good faith would presumably be a breach of the Code unless it is simply expressed to be an express term mandated to apply to every franchise agreement regulated by the Code (e.g. a contractual obligation). In that event it would be a breach of the contract allowing the parties to seek appropriate contractual relief.

A breach of the Code could give rise to penalties or other relief otherwise it may be prudent to look to specific clauses like clause 20A and see what specific consequence under the Code could apply to give relief. Some clauses in the Code do lend themselves to having a specific consequence for breach.

Any penalties or specific relief should allow for defences or mitigating circumstances to be taken into account particularly if there is a penalty regime imposed. Refer to other comments contained in my Discussion Paper in Annexure "B".

22. If the Franchising Code was amended to contain an explicit obligation to act in good faith, would there need to be other consequential amendments to the Franchising Code?

Response:

Yes some language would need to be relooked at. Refer to the example I have given to the interpretation of Clause 20A in the Discussion Paper I provided in Annexure "B".

I suspect the relevant clauses would be clause 20, clause 20A, clauses 21, 22, 23 and Part 4 to ensure that the parties must act in good faith and possibly they are taken to be acting in a reconciliatory manner if they act in good faith as well.

If any penalties are introduced for general breaches it should be mandatory for the ACCC to consider whether there are mitigating circumstances or defences available such as if they acted in good faith.

Part Four: End of term arrangements for franchise agreements

Overview:

23. Have the amendments regarding end of term arrangements and renewal notices been effective in addressing concerns about inappropriate conduct at the end of the term of franchise agreements? Why or why not?

Response:

Not really for reasons given above and because as a consequence of the commercial reality that clause 20A notices have not really commenced to apply because those agreements which were entered into on or after 1 July 2010 usually have terms of 3 or 5 years which have not required the notices to be given yet.

The amendment was not expressed to apply to every existing agreement.

Part Five: Dispute resolution in franchising

24. Has conduct and behaviour during mediation changed since the introduction of the 2010 amendments to the Franchising Code, including requiring parties to approach mediation in a reconciliatory manner? If so, in what ways?

Response:

In some ways it has changed behaviour of franchisors however some franchisees still refuse to attend or participate in mediation commenced by franchisors with little consequence to them. The OFMA may not have any enforcement powers to compel them to attend.

The Code does not require the parties to act in good faith to resolve any dispute (whether under a Part 4 process or franchise agreement process or through some dispute resolution process under a state small business commissioner process. It is not clear whether you act in a reconciliatory manner if you act in good faith in relation to resolving that dispute.

The Code currently does not require the parties to engage in dispute resolution in good faith only in a reconciliatory manner. Introduction of this requirement may require a change to this obligation.

There is some anecdotal evidence from at least one lawyer I have spoken to of an example where a dispute that was referred to a state Small Business Commissioner by a franchisee is being dealt with by way of a mediation and conducted under their legislation.

The Small Business Commissioner involved apparently was advised by the Franchisor's solicitors that the franchisor wanted the dispute resolution to be conducted in accordance with Part 4 of the Code or the method set out in their franchise agreement and this was refused.

If this is correct then the ACCC and the small business commissioners need to have a protocol

on how franchise disputes are to be resolved or it means the whole Part 4 process of the Code is useless if a dispute is referred to a state small business commissioner.

25. Does the sector have concerns regarding the operation of the amendments?

Response:

No, however if a good faith obligation applied to dispute resolution under Part 4 of the Code as well then this may change things and how parties behaved. Currently there is no obligation to act in good faith, just in a reconciliatory manner.

Perhaps that part of the Code could include as an example of acting in a reconciliatory manner where the parties are acting in good faith in seeking to resolve the dispute or vice versa that you are taken to be acting in good faith if you approach resolution of the dispute in a reconciliatory manner.

Part Six: Enforcement of the Franchising Code

26. Is the current enforcement framework adequate to deal with the conduct in the franchising industry?

Response:

Yes the current framework does work generally well for most industries covered by the Code. The existing unconscionable conduct and misleading and deceptive conduct provisions appear to work and there are clear examples where they have worked for the benefit of both the franchisor and the franchisee.

The problem of mismatched expectations causes parties to believe that the code is ineffective. Unfortunately there is no simple cheap and effective means of resolving a dispute in court quickly. Mediation appears to have improved the prospects of resolving a dispute but does not always work.

Seeking to establish a separate Tribunal for franchising has been posed even using the existing regimes such as VCAT or QCAT. Unfortunately consistency in decisions and allocation of resources to hear them expeditiously would be an issue.

There is no overwhelming or demonstrated need to extend the ACL "unfair contracts" regime to franchise agreements on a business to business basis.

It is apparent that industry specific issues confronting the automotive sector remain of concern and they continue in their desire to either have a separate automotive code apply to them or to have specific provisions to protect participants inserted into the Franchising Code of Conduct. It would be useful for government to examine this in more detail, remembering that they are the ONLY form of agreement that is deemed to be a franchise agreement without applying the tests in clause 4(1) of the code. They therefore cannot restructure themselves to fall outside and in essence are captured by this Code because of the nature of the good or service they sell being a "motor vehicle".

There is no doubt that many dealers and their representative organisations would argue that the current framework to protect them is inadequate given the size and nature of their investment

and the significant imbalance in the relationship caused by an ability to unilateral change significant rights and obligations at any time during the term, a lack of security of tenure by virtue of short term agreements or a unilateral right to terminate without cause on notice.

This arguably may explain why that sector raises issues of exit payments for goodwill and recovery of loss on termination of a motor vehicle dealer agreement arising from that notice period. The losses caused on termination simply by notice can be extensive.

A framework where there is an obligation to act in good faith may assist but on its own may not necessarily be the sole or appropriate remedy.

This should require further consideration and review of the nature and extent of disputes that arise in that sector and whether a separate code is now required whether by inclusion of a new Part to the Code to apply to them or for additional relief. The main areas of concern in that sector appear to relate to good faith, unilateral variations and terminations and they appear to be in some cases quite legitimate concerns.

Greater allocation of human and financial resources to the ACCC could assist to implement improvements to compliance.

Focus by the ACCC on deliberate anti-avoidance of the Code in its entirety is preferable. There are breaches of the code that could clearly have specific relief.

Refer to examples in the attached discussion paper.

27. How can compliance with the Franchising Code be improved?

Response:

Greater allocation of resources for targeted Education.

More relevant publications from the ACCC to assist franchisors to understand their obligations where there are grey areas of interpretation of the code rather than simplistic publications for franchisees

An ability to seek a binding private ruling determination from the ACCC so the parties can act on that interpretation would be extremely beneficial (e.g. is this agreement a franchise agreement or not – does the fractional franchise exemption apply).

Better language in the Code that gives clarity to areas that are currently grey or just poor drafting.

28. What additional enforcement options, if any, should be considered in response to breaches of the Franchising Code?

Response:

A penalty regime has often been suggested with the ACCC being responsible to ensure a measured enforcement for deliberate anti-avoidance but if it were to be seriously considered then the language of the Code would need to be improved and remove some interpretational grey areas.

Defences and mitigating circumstances would need to be considered as well as who bears the

onus of proof.

There is a lack of clarity as to how the enforcement powers are to be inserted – into the Code or into the ACL or CCA and whether they will apply only to this Code or any mandatory Commonwealth Industry Code.

Refer to my Discussion Paper in Annexure "B".

29. What options are available to businesses to address breaches of the Franchising Code, or any other adverse conduct in the franchising industry?

Response:

A complaint to the ACCC or seeking to commence the dispute process under Part 4 or commence proceedings.

Many franchisees in SA and other jurisdictions with a Small Business Commissioner may approach that body for assistance first (before approaching the ACCC) to force an outcome on a franchisor.