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| **Name** | Kenneth Rosebery |
| **State** | New South Wales |
| **Stakeholder Type:** | Franchisor |
| **Industry Type:** | Food |
| **1. What are the critical pieces of information that should be contained in a summary document?** | |
| The value of most enterprises is determined by reference to financial statements. In the case of an incumbent franchisee selling to a buyer, accurate financial statements, principally a profit and loss statement, are the best way to make a reasonable assessment of value. Whereas the disclosure document does not generally allow a reader to put various risks or costs into context. A balance sheet is of limited value as it is more specific to the circumstances of the vendor which may not be relevant to the profit performance of the franchised business. Only the directors of an entity can be responsible for the provision of accurate financial statements and not the franchisor who is generally not in a position to validate the information without extraordinary cost of audits even if they could be imposed. Most prospective franchisees are not skilled at interpreting profit and loss statements and accordingly it is essential that they obtain professional accounting advice from a CA, CPA or IPA member.  In the case of a prospective buyer looking at a Greenfield site, the most critical information is benchmarking data collected from existing established franchise units, such as key expense ratios and average historical revenues. Again, most prospective franchisees are not skilled at translating such data into a budget / cash flow and accordingly it is essential that they received professional accounting advice from a CA, CPA or IPA member.  Whilst The Cheesecake Shop collects financial reports and produces benchmarking data which it makes available to prospective franchisees via its Disclosure Document, there may be practical challenges with many franchisors being able or sufficiently resourced to replicate this. Accordingly, the simplest and most powerful check and balance in this regard is to ensure that prospective franchisees receive professional advice from people who are skilled at providing business advice. | |
| **2. If a national franchise register is established, what information should it contain? What would be the benefits and costs of a national franchise register?** | |
| Evidence from some states in the USA is that such registers are very expensive to maintain, particularly if done so by a government agency. It is not clear what if any benefit accrues to prospective franchisees and accordingly the cost of such a mandatory requirement is likely to be high.  The Franchise Council of Australia is proposing to operate its own registry for members and such a solution is likely to be more efficient and avoids the imposition by government of expensive 'red tape', even if the benefits remain unproven. | |
| **3. There are a number of existing educational resources on franchising. What additional education options for prospective franchisees should be made available? If there was an online educational resource which brought together the available franchising education options, what would its costs and benefits be?** | |
| The existing educational resources are good. The issue is that most prospective franchisees either are not aware of them or simply don't believe that they need it. The advice of accounting and legal professionals prior to committing to a franchise is therefore likely to be more effective, easier to mandate and practical to implement, than an emphasis on pre-entry education alone. | |
| **Problem 1.1: Disclosure can be hard to comprehend, critical information may be hidden in detail and some information is not provided in the disclosure document.** | |
| Option 1.1.3: Simplified disclosure requirements. Require that a simplified disclosure document, which provides all materially relevant information needed to assess the franchise business, is provided to prospective franchisees | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| There is already extraordinary levels of detail in most disclosure documents and this apparently still leads to calls by some for even more disclosure. In our experience, a minority of prospective franchisees read or understand the disclosure document. The prescriptive form of the current disclosure document makes the document long and cumbersome.  If the onus were put on the franchisor to use its own discretion to disclose what is materially relevant, then in our opinion this would lead to more incisive and legally responsible disclosure. Albeit, creating uncertainty and risk for the franchisor.  However - despite the anecdotal reports of misinformation during the enquiry, it is not clear what evidence there is that poor disclosure is at the heart or cause of many of the issues raised. What justification can there be for increasing the cost of 'red tape' for unproven benefit? | |
| **Problem 1.2: The reliability of information provided to prospective franchisees may be difficult to assess** | |
| Option 1.2.1: Status quo (no changes) | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| Reliability of what is essentially financial or legal information can only really be assessed by those qualified and skilled to do so. Accordingly, a mandatory requirement to have legal AND accounting advice is both necessary, cost effective and practicable to implement. If such professionals give a recommendation not to proceed to a prospective franchisee, then this provides a natural incentive for franchisors to provide information sufficiently accurate, verifiable and incisive such that these professionals can be convinced of the value and risk of a proposed purchase.  It is not practical to require a franchisor to verify a franchisee's financial statements, as such a legal test would require an audit of each franchisee. The cost of this would inevitably be borne by franchisees and this would be a burdensome cost not imposed on their independent competitors. | |
| **Problem 1.3: Information gaps – a potential franchisee might be unaware of which types of information are materially relevant to inform their decision to enter an agreement.** | |
| Option 1.3.3: Mandate all prospective franchisees receive legal and financial advice before entering into a franchising agreement | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| I have already made this point above. 1.3.3 is practical because lawyers and accountants (CPA, CA, IPA qualified) are readily accessible to prospective franchisees and the cost of such advice is likely to be reasonable (moderated by competition). Such advice can be obtained reasonably quickly and therefore is unlikely to impose unintended delays and costs. Such a solution can be adapted to the many forms and business models that franchising incorporates. | |
| **4. What are the practical implications (costs and benefits) for prospective franchisees and franchisors of increasing cooling off or disclosure periods?** | |
| It is not clear that in any of the problems raised by the enquiry that the length of the cooling off period was the cause of any problem. This therefore appears to be a solution to a problem that does not generally exist. However the effect of 'rad tape' and possible costs could be high.  The unintended consequences of any extension of the cooling off period will relate to situations where lease commitments intersect with the need for a franchisee to be committed and/or where the vendor is an existing franchisee, where it is likely to be impractical to unwind a transaction post completion of a sales and purchase. | |
| **5. How easy is it for franchisors to provide reasonable estimates of leasing costs before they are finalised?** | |
| It is easy to provide a reasonable estimate in our situation, however the problem may arise if any immaterial variation on the estimate creates a need to re-disclose or extends the cooling off period. Having said that, we cannot recall such a situation arising across 226 leases over the last 10 years. In nearly all cases that we can recollect, the lease costs were known.   If the franchisee were receiving mandatory legal and accounting advice, then would such a professional recommend proceeding if there was a risk of material variation to a lease cost? We think they would not. | |
| **6. How often are leasing arrangements finalised after the cooling off period expires? What are the implications of having the cooling off period commence after a lease is finalised?** | |
| In the case of greenfield sites, we always try to make a binding lease commitment contingent on a franchisee being committed. If a cooling off period commenced after the lease is finalised, then this creates a significant risk exposure to a franchisor. In such a circumstance, some franchisors may simply require the prospective franchisee to take the head lease rather than the franchisor, imposing the risk on the franchisee anyway but without the additional security and oversight of the franchisor. Landlords are likely to impose a higher bank guarantee cost on a franchisee tenant without the franchisor holding the head lease.  Other practical issues may arise here. What exactly is meant by 'finalised' - execution by the lessor, the presence of a physical copy of an executed lease, stamping of the document? - all of which are often delayed in the administrative and legal processes - even if the lease is legally binding by virtue of the existence of a written offer and acceptance. | |
| **Problem 2.1: Cooling off rights may expire before franchisees and franchisors have adequate time to appropriately reflect on their business arrangements after entering the agreement** | |
| Option 2.1.1: Status quo, with clarification of the operation of existing cooling off requirements in the code | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| if it's not broken don't fix it. Most franchisors are still reeling from the costs and changes brought about by the vulnerable workers amendment act. We're getting regulatory fatigue, so why bring in measures when the problem is not apparent? | |
| **Problem 2.2: Cooling off rights may expire before lease arrangements are finalised** | |
| Option 2.2.1: Status quo (no changes) | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| see above | |
| **Problem 2.3: Cooling off rights in transfers, extensions and renewals can be unclear, including with respect to franchisee to franchisee sales** | |
| Option 2.3.1: Status quo (no changes) | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| The buyer needs to get legal advice in a franchisee to franchisee sale and purchase. Problems rarely arise if at all, when the prospective franchisee is well advised. | |
| **7. What would ‘meaningful information’ look like in terms of marketing fund disclosure?** | |
| Audited annual financial statements in compliance with current arrangements. Already the Ultra Tune decision has imposed a higher standard of detail in audited financial statements for marketing funds. Let that pan out before making any more changes. | |
| **8. How does the benefit of increased frequency of reporting of marketing funds compare to the costs of increased administration?** | |
| If you are suggesting audited financial statements every quarter than add at least a $100,000 to the cost of administering a large fund. The cost of which comes from the marketing fund to the detriment of franchisees in general. If the reporting is unaudited, then what use is that to a franchisee where the franchisor is trying to hide something? | |
| **Problem 3.1 Marketing funds are not always transparent** | |
| Option 3.1.1: Status quo (no changes)  Option 3.1.3: Increase awareness and provide guidance around existing legal obligations | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| In the aftermath of the Ultra Tune decision most franchisors would prefer more clarity around the reporting standards. There are practical challenges in doing so, given the diversity of franchise systems and their use of marketing funds. | |
| **9. What information should franchisors disclose in relation to supplier rebates? Are there any barriers to providing this?** | |
| Franchisors need to demonstrate that all supply arrangements are competitive with goods or services of comparable quality and standards. In the end it is the cost of goods sold being at a level that allows a profitable business that is the key issue. This then comes back to financial information, benchmarking data and accounting advice prior to purchase as the best way for a franchisee to monitor the reasonableness of purchases.  There are significant practical issues that arise if detailed disclosure is mandatory, including; the confidentiality of pricing and rebate arrangements, such that disclosure may prevent them being offered in the first place by a supplier fearful that other customers will argue for such rebates; rebates may not be known in advance and may be dependent on achieving purchase targets; rebates can be avoided by restructuring supply to a wholesaling arrangement. | |
| **10. If franchisors are required to ensure franchisees get a return on their significant capital expenditure, how might this be done in practice?** | |
| It can't be without destroying the risk and reward inherent in commercial arrangements. Whilst a franchisor can target on average a reasonable return on capital, this cannot be guaranteed in specific cases as it creates a moral hazard where a franchisee can reduce their effort or diligence knowing that the franchisor will pick up the tab.  Good financial benchmarking data and/or financial statements from a vendor franchisee, reviewed by an accounting professional can most likely avoid a prospective franchisee entering a system where there is a poor return on capital. Speaking to current and former franchisees is probably the best way of discovering if there are issues in this regard with a particular system. | |
| **11. If franchisees are given a right to review capital expenditure business cases (which must be presented to franchisees by the franchisor under clause 30(2)(e) of the Franchising Code for expenditure that the franchisor considers is necessary for capital investment), how would this right be exercised?** | |
| What does review mean? Veto? No franchisee or franchisor generally wants to make additional capital expenditure but this may nevertheless be necessary for competitive business reasons. Most good franchisors will take capital expenditure proposals where they affect all or most franchisees to their franchisees for consultation anyway. However any right of veto will likely make change more difficult and frustrate the ability of franchise systems to remain relevant and competitive in a dynamic business environment. | |
| **Problem 4.1 Supplier rebates can lead to conflicts of interest** | |
| Option 4.1.1: Status quo (no change) | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| We cannot see any practical way that 4.1.2 or 4.1.3 can be implemented without significant damage and cost.  Detailed disclosure risks the suppliers avoiding such arrangements to the detriment of the system.   Most retail franchise systems set maximum pricing by virtue of published prices on the internet that cannot be exceeded without infringing misleading and deceptive conduct requirements. To bar rebates in such circumstances may be unfair and disadvantage to franchisees and franchisors. Some franchise systems exist solely on rebates as opposed to levying franchise fees.  In any event those franchisors that employ a wholesaling structure, avoid the need for rebates and so such an imposition of barring rebates, may simply create a shift to such wholesaling arrangements. | |
| **Problem 4.2 Conflicts of interest in the context of capital expenditure** | |
| Option 4.2.1: Status quo (no change) | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
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| **Problem 4.3 Unilateral variations can lead to conflicts of interest and exploitation** | |
| Option 4.3.1: Status quo (no change) | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| A franchisor must have the right to vary is business model in response to a dynamic environment. For example, how can franchisors respond to a regulatory change such as the vulnerable workers amendment, without some changes to standards and requirements of franchisees? It will be difficult to find a franchisee that supports the extra controls that a franchisor needs to impose in order to comply with the changed law, nevertheless they needed to occur.   In the end of the day, franchisees want to make money and accordingly if good financial data is readily available and franchisees are generally satisfied, then a prospective franchisee is protected more than by imposing a requirement that will damage a franchise system in the longer term. | |
| **12. A number of stakeholders have told the Taskforce that the cost of arbitration can be comparable to going through the court system, and that conciliation may be a preferable alternative alongside mediation. In what circumstances could conciliation be an effective alternative dispute resolution process?** | |
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| **13. Would you consider including arbitration to resolve disputes in your franchising agreement, if a clear voluntary option were provided?** | |
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| **Problem 5.1: Some disputes are not being resolved in a fair, timely and cost effective manner.** | |
| Option 5.1.1: Status quo (no change) | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| It's not broken - don't fix it. Mediation is very effective and most disputes that get this far are resolved. There is no evidence that franchising experiences a higher level of disputation than any other sector of the economy. | |
| **14. Under what circumstances should franchisees be allowed a no-fault exit from the franchise system?** | |
| None | |
| **15. If goodwill was required to be fully clarified in the franchise agreement, how might this be done in practice? What would be the costs and benefits of this approach?** | |
| It can't be. | |
| **Problem 6.1 Reasonable exit arrangements may not be, or may not be perceived to be, available or accessible for some franchisees** | |
| Option 6.1.1: Status quo (no change) | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| Mediation is already available in all but the most egregious of breaches of a franchise agreement. No change is necessary. 6.1.2. arguably already exists within the code. 6.1.3 might be useful and acceptable but risks unintended consequences and more regulatory fatigue. | |
| **Problem 6.2 Excessive restraint of trade clauses may inhibit lawful pursuit of subsequent business interests** | |
| Option 6.2.1: Status quo (no change) | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| Restraint of trade is already limited in law and precedent. Avoid regulatory fatigue and leave this alone - the current law is sufficient. | |
| **Problem 6.3 There are different expectations around the treatment of goodwill in franchise arrangements** | |
| Option 6.3.1: Status quo (no change) | |
| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
| The franchisee needs to obtain legal and accounting advice so they understand the extent to which goodwill may exist or can be transferred. In most cases goodwill can only exist to the extent that cash flows are maintainable and transferrable. There is so much diversity in franchise systems it is difficult to see how any such provision can be constructed without unintended consequences. | |
| **16. What are the implications of amending the Oil Code of Conduct to increase the number of common provisions between the Oil and Franchising Codes? What would be the costs and benefits of this approach?** | |
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| **17. What are the implications of repealing the Oil Code of Conduct and adding specific fuel retailing provisions to the Franchising Code?** | |
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| **Problem 7.1: Some franchisors experience additional regulatory burden from having to comply with both the Franchising Code and the Oil Code** | |
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| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
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| **Problem 7.2: Compliance with the Franchising Code, Oil Code and where relevant the Competition and Consumer Act and the Australian Consumer Law, remains imperfect** | |
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| **Please give an explanation of your choice(s). This includes the reasons an option may not be suitable. What are the costs, benefits and risks of your choice(s), and what other options could be considered?** | |
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| **Are there any other comments you would like to make?** | |
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