



Franchising Update: Parliamentary Joint Committee Report on Franchising

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In June 2008, the Parliamentary Joint Committee on Corporations and Financial Services commenced an inquiry into whether any amendments should be made to the Franchising Code of Conduct (the “Code”) in order to raise the standard of conduct of participants in Australia’s growing franchising sector.

Having reviewed over 150 submissions from various participants in the franchising industry, the Committee offered eleven recommendations in its report, titled “Opportunity not opportunism” which was released on 1 December 2008. The key recommendations were summarised below.

The major theme of the Committee’s report was how to best deal with so-called “rogue” franchisors that have been reported to have opportunistically dealt with franchisees, particular in relation to unfairly terminating or failing to renew franchise agreements or in negotiating resolution of disputes. Somewhat controversially, it was felt that the best method of preventing or limiting this behaviour would be through the introduction a new obligation into the Code requiring franchisors, franchisees and prospective franchisees to act in good faith.

It was noted that some of the changes to the Code made in March 2008 may already be working to limit the activities of such rogue franchisors – the Committee therefore recommended that the government review the effect of those changes in the next two years with a view to making further amendments as required.

Disclosure documents

The Committee recommended that the disclosure requirements of the Code be amended so that franchisees are offered a clearer understanding of what will happen when the franchise relationship comes to an end, including:

- the liabilities and consequences franchisees will face in the event that the franchisor’s business fails; and
- the potential transferability of equity or goodwill in the value of the business as a going concern.

The Committee declined to make recommendations for other information to be added to disclosure documents, noting that disclosure documents are becoming increasingly long and that better disclosure does not necessarily mean more disclosure.

Registration of franchise systems

The Committee recommended that the government develop a simple online registration system for Australian franchisors, with each franchisor required each to lodge an annual statement that they are meeting the requirements of the Code and the Trade Practices Act (TPA) and to report on the extent of their franchise network.

The Committee did not go as far as to recommend that franchisors be required to register and lodge their disclosure documents and/or franchise agreements – it was felt that this would be too much of a burden on franchisees and would create an expectation



that the documents had been vetted or approved in some form when in fact it is the role of legal advisors to review the documents.

The Committee also recommended that the Australian Bureau of Statistics be required to collect and publish statistics relevant to the franchising industry, particularly relating to franchise disputes and unit turnover, since other statistics collected about the franchising sector tended to be from voluntary surveys that may not be representative of the sector as a whole.

Limiting opportunistic behaviour

The Committee explored a range of submissions regarding fairness in relation to the termination and non-renewal of franchise agreements.

The Committee was particularly concerned stopping franchisors engaging in opportunistic conduct, particularly “churning” (whereby a franchisor habitually offers a franchise, terminates and then re-sells the franchise, making a profit each time the business changes hands regardless of the business’s profitability). The Committee decided against recommending provisions to specifically address these issues, such as giving franchisees an automatic right to renew, requiring franchisor’s to show good cause if failing to renew, or requiring franchisors to compensate a franchisee in the event of non-renewal by buying the franchising back at market value.

Instead, and despite submissions to the contrary from several high-profile franchisors, the Committee recommended that a specific provision be added to the Code that *“franchisors, franchisees and prospective franchisees shall act in good faith in relation to all aspects of a franchise agreement”*.

It should be noted that the Committee felt that it was best to leave the definition of “good faith” to the Courts and therefore the recommended addition to the Code does not include any definition or examples of what constitutes good faith (nor what constitutes a lack of good faith).

The Committee decided against recommending any more exhaustive provisions that might prevent or reduce opportunistic behaviour, such as giving franchisees an automatic right to renew, requiring franchisor’s to show good cause if failing to renew, or requiring franchisors to compensate a franchisee in the event of non-renewal by buying the franchising back at market value.

ACCC investigation and enforcement

The Committee agreed with submissions that the Australian Competition and Consumer Commission (ACCC) was often a “toothless tiger” in the franchising sector.

Therefore, a number of recommendations designed to address this problem were made. Firstly, it was recommended that the *Trade Practices Act 1974* (TPA) include pecuniary penalties for breach of the Code. Further, although outside the scope of the inquiry, the Committee recommended that consideration be given to including pecuniary penalties for breaches of the misleading and deceptive conduct and unconscionable conduct prohibitions of the TPA.

Finally, the Committee felt that the ACCC should have the power to investigate parties thought to be engaging in conduct contrary to the Code.

Improved dispute resolution



Despite accepting that the processes of mediation and litigation may be unfair to franchisees, the Committee felt that the obligation to the parties to act in good faith combined with the increased role of the ACCC in investigating and enforcing the TPA and the Code would be sufficient to facilitate fairer outcomes in the dispute resolution process.

The Committee's only other recommendation in relation to disputes was that the name of the "Office of the Medication Adviser" be changed to the "Office of the Franchising Mediation Adviser" to better reflect of the role that the office has in the franchising sector.

The Committee did not accept submissions that an alternative dispute resolution body be set up, such a franchising tribunal or a franchising ombudsman.

Other recommendations that were not made

The Committee felt it unnecessary to make recommendations that may have:

- clarified the definition of "franchise agreement";
- mandated that franchisees or franchisors undergo education programs (although it was noted that the ACCC perhaps should take a more proactive approach, particularly to educating prospective franchisees);
- ensured the accreditation or performance of legal and business advisors; or
- allowed franchisors to immediately terminate for three strikes (that is, after a franchisee has breached of the agreement on three occasions, even if the franchisee has remedied those breaches).

Summary

It is clear from the report that the Committee's primary concern was maintaining the right balance between the rights and obligations of franchisors and those of franchisees.

This concern was borne out in the recommendations of the Committee, which should go some way to protecting franchisees from opportunistic behaviour by rogue franchisors without being too burdensome for the majority of franchisors, who aim to foster sound working relationships with their franchisees.