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**FRANCHISING AND THE TRADE
PRACTICES ACT 1974 (CTH)**

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Franchising and the *Trade Practices Act 1974 (Cth)*

by Vahan Bedrossian¹

Franchising is a significant type of business structure in the Australian economy. The franchising sector itself constitutes a multi-billion dollar industry. Given the financial significance of the industry and the fact that the stereo-typical franchise involves a relatively sophisticated franchisor and a relatively less sophisticated franchisee, it was inevitable that disputes between franchisors and franchisees would threaten the prosperity of the industry and the efficiency and effectiveness of franchising as a business model. In that context, regulation became inevitable. An experiment with voluntary regulation of the industry in the 1990s was unsuccessful.

The availability of the Trade Practices Act 1974 (Cth) provided an ideal foundation for a regulatory framework for franchising. Now, just over 10 years since the Franchising Code of Conduct came into force, available statistics show a healthy growth in the industry and a decline in disputation between franchisees and franchisors.

Notwithstanding this progress, significant disputes continue to arise in franchising. Those disputes tend to be expensive experiences for both franchisors and franchisees. Further and importantly, those disputes distract from the profitable conduct of the business (both for franchisors and franchisees).

Compliance with the Franchising Code of Conduct by franchisors and knowledge of its terms and operation on the part of franchisees will reduce the likelihood of such expensive disputes.

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TABLE OF CONTENTS

Table of Contents	2
Part I: INTRODUCTION.....	3
A. Some Statistics	3
B. Short History of Regulation of Franchising	4
C. Current Legislative and Regulatory Framework	5
Part II: FRANCHISING CODE OF CONDUCT	7
A. “Part 1” of the Code – “Preliminary”	7
B. “Part 2” of the Code – “Disclosure”	11
C. “Part 3” of the Code – “Conditions of franchise agreement”	17
D. “Part 4” of the Code – “Resolving disputes”	21
Part III: ENFORCEMENT OF CODE	23
A. Mechanism for Enforcement of Code	23
B. Requirement for a Successful Claim under Section 51AD.....	26
Part IV: CONCLUSION.....	28
Attachment: Franchising Code of Conduct (including amendments up to and including 1 March 2008)	

PART I: INTRODUCTION

A. Some Statistics

1. Each two years, the Asia-Pacific Centre for Franchising Excellence at Griffith University conducts a survey of the franchising industry in Australia. The most recent survey, the Franchise Australia 2008 Survey, shows that franchising continues to be an area of rapid growth in the Australian economy.
2. The findings of this 2008 survey include that:
 - (a) franchised businesses represent approximately 3.7% of all small businesses in Australia;
 - (b) total sales turnover for the franchising sector was approximately \$130 billion;
 - (c) the total number of people employed in franchised businesses was approximately 413,500; and
 - (d) disputes in the franchise sector have reduced over recent years and it is now estimated that only about 2% of franchisees are in dispute with franchisors. However, approximately 17% of franchisors reported having been an a dispute with at least one franchisee such that external advisors were required to assist. This was a reduction from about 35% in the equivalent 2006 survey.
3. These recent statistics, both in relation to the financial significance of the franchise sector and also the apparently low rate of disputation, are likely to have been the product, at least to some extent if not to a significant extent, of the concerted efforts over a number of years on the part of regulators to provide fair and appropriate guidelines for the conduct of franchise businesses.
4. Notwithstanding this, disputes arise in the franchise sector. Those disputes, which the Franchise Australia 2008 Survey classified as being 'significant', involved a number of issues, including:
 - (a) compliance with the system (66%);
 - (b) profitability (37%);
 - (c) territorial issues (21%);

- (d) communication problems (18%); and
- (e) fees (16%).

B. Short History of Regulation of Franchising

5. Throughout the history of the *Trade Practices Act 1974* (Cth) ("the Act"), various parliamentary committees have undertaken various reviews of the Act and the issues arising from the need to provide some satisfactory regulation of franchising. These have included: the Swanson Committee (1976); the Blunt Committee (1979); the Beddall Committee (1990); the Reid Committee (1997); and the Mathews Review (2006).
6. Where a franchisor has been a corporation engaged in trade or commerce, complaints against the conduct of the franchisor have always been amenable to the reach of the remedies made available by the Act. The difficulty was often fitting the special nature and circumstances of a franchise relationship within the relatively narrow confines of a claim for misleading or deceptive conduct under section 52 of the Act. The inclusion in the Act in 1986 of an ability to claim relief for 'unconscionable conduct', pursuant to what is now section 51AB, clearly expanded the range of circumstances, in respect of which relief could be claimed. As did the further expansion of that jurisdiction in relation to unconscionable conduct by the insertion of section 51AA in 1992 (effective from January 1993) so as to include the ability to relieve against 'unconscionable conduct within the meaning of the unwritten law of the States and Territories'.
7. The difficulty, however, has always been the need to accommodate regulation directed specifically to the needs and desires of particular industries, of which the franchising industry is one. That difficulty was addressed in 1998 by the inclusion of a new part, Part IVB, in the Act. This part of the Act was addressed to "industry codes" (that is, 'codes of conduct').
8. Part IVB was included in the Act by the *Trade Practices Amendment (Fair Trading) Act 1998* (Cth), which commenced on 22 April 1998. Part IVB provided a scheme, by which either voluntary or mandatory codes of conduct for different industries could be declared by appropriate regulations to be 'prescribed' codes for the purposes of

the Act. Breaches of the relevant codes, if they applied, constituted a breach of the Act, which prohibited conduct in breach of such codes, and gave rise to an ability to seek relief under the remedial provisions of Part VI of the Act.

9. So as to avoid any doubt in relation to the operation of Part IVB of the Act, franchising was expressly declared to be an 'industry' for the purposes of the Part (sub-section 51ACA(3)(a)).
10. Shortly after Part IVB was included in the Act, the *Trade Practices (Industry Codes - Franchising) Regulations 1998* (Cth) came into force (on 1 July 1998). Those regulations set out the terms of the *Franchising Code of Conduct* ("the Code").

[A copy of the current Code is attached to this paper. This incorporates the most recent amendments to the Code, which were brought into effect by the *Trade Practices (Industry Codes - Franchising) Amendment Regulations 2007* (No. 1) and which commenced operation on 1 March 2008.]

C. Current Legislative and Regulatory Framework

11. Section 51AE is the legislative authorisation for the prescription by regulation of industry codes, whether mandatory or voluntary, for the purposes of Part IVB of the Act. With respect to voluntary codes, the Act permits the regulations to specify the method by which a corporation will agree to be bound by the code and the method by which it can cease to be bound by the code.
12. Various relevant definitions applicable for the purpose of Part IVB of the Act are set out in section 51ACA, being definitions of the terms: 'applicable industry code'; 'consumer'; 'industry code'; 'mandatory industry code'; and 'voluntary industry code'.
13. Section 51AD is the critical operative provision. It provides:

A corporation must not, in trade or commerce, contravene an applicable industry code.
14. By framing the relevant prohibition in such general terms, the drafters of section 51AD created a legislative framework whereby individual industries with individual circumstances and/or problems might have their own industry regulated by a

specifically designed industry code, which would gain the force and protection of the Act via sections 51AE and 51AD².

15. The specific terms of the Code are identified and discussed later in this paper.
16. Of relevance also are the terms of section 51AC of the Act. That provision prohibits 'unconscionable conduct in business transactions'. Relevantly for the application of that provision, the matters to which a court may have regard for the purpose of determining whether a corporation or a person has contravened section 51AC include "the requirements of any applicable industry code" (sub-section 51AC(3)(g) and (4(g)) and "the requirements of any other industry code" (sub-section 51AC(3)(h) and 4(h)).
17. Thus, disputes involving franchisors and franchisees may be the subject of claims for relief based not only upon breaches of section 51AD of the Act, but also other provisions, such as:
 - (a) section 51AA – 'Unconscionable conduct within the meaning of the unwritten law of the States and Territories';
 - (b) section 51AB – 'Unconscionable conduct';
 - (c) section 51AC – 'Unconscionable conduct in business transactions';
 - (d) section 52 – 'Misleading or deceptive conduct';
 - (e) section 53 – 'False or misleading representations'; and
 - (f) section 59 – 'Misleading representations about certain business activities'³.

² In addition to the Franchising Code of Conduct, two other codes have come into effect for the purposes of Part IVB of the Act. The 'Oilcode' came into effect on 1 March 2007 upon the making of the *Trade Practices (Industry Codes - Oilcode) Regulations 2006* (Cth) and the 'Horticulture Code' came into effect on 14 May 2007 upon the making of the *Trade Practices (Horticulture Code of Conduct) Regulations 2006* (Cth).

³ This provision may be of particular importance in certain circumstances, because it provides a specific prohibition against the making of false or misleading representations regarding "the profitability or risk or any other material aspect of the business activity" in circumstances where a corporation "invites" persons to engage in a business activity requiring the performance of work (or the investment of moneys together with the performance of work) (sub-section 59(2)).

PART II: FRANCHISING CODE OF CONDUCT

18. A copy of the current Code is attached to this paper. Nevertheless, set out below is an identification of the various parts of the Code and the provisions within each of those parts, to which the greatest attention and care ought to be directed.

A. "Part 1" of the Code – "Preliminary"

19. Part 1 of the Code is, as its name suggests, the preliminary portion of the Code. It must not, however, be overlooked, because critical (and occasionally underestimated) definitions are set out in clause 3 thereof. These include (but without setting out every definition appearing in the clause):

- (a) **disclosure document**, which has the meaning given by clause 6 of the Code.

[Clause 6 falls within Part 2 of the Code, dealing with disclosure. It is discussed later.]

- (b) **franchise**, which is defined as "including"⁴ the following:

- the rights and obligations under a franchise agreement;
- a master franchise;
- a subfranchise;
- an interest in a franchise.

[As with a number of other of the definitions in the Code, the definition of 'franchise' is broad and inclusive. The purpose of various of these definitions was to provide as broad a definition of the relevant aspect of franchising as possible, without of course straying from what is the essence of a franchise, so as to prevent the ability of participants in the industry, particularly franchisors, to evade their obligations under the Code by deliberately adopting any particular legal structures or arrangements.]

- (c) **franchise agreement**, which has the meaning given by clause 4 of the Code.

⁴ A number of definitions in the Code adopt the same approach, namely to provide an identification of those matters that are expressly included within the definition, but without excluding the possibility of others.

[This definition is discussed further below, because of its significance, including sometimes in circumstances where its application was unintended by the parties to the business relationship.]

(d) **interest in a franchise** “includes a legal or beneficial interest in:”

- a franchise agreement or a franchised business; or
- shares or voting rights in a corporation, not being a listed corporation that owns a franchised business; or
- units or voting rights in a unit or other trust that owns a franchised business; or
- the capital or income of a partnership that owns a franchised business.

[Again, the broad nature of this definition is apparent. Of particular note is the inclusion of ‘beneficial’ interests and also what might be described as indirect interests in relation to franchises, such as units or voting rights in a unit or other trust that owns a franchised business. When combined with the broad reach of the remedies provisions identified in Part VI of the Act, including by reason of the wide definition of “a person involved in a contravention” as set out in section 75B, it is clear that the Code reaches into every corner of the franchising sector.]

20. Clause 4 of the Code sets out the full definition of a ‘franchise agreement’. The definition comprises 4 separate components, each of which needs to be satisfied for a franchise agreement to be found to exist. In short, the four components are as follows:

- (a) A franchise agreement can be a written or oral agreement and even an implied agreement. [sub-clause 4(1)(a)]
- (b) A franchise agreement is an agreement, in which “the right to carry on the business of offering, supplying or distributing goods or services in Australia under a system or marketing plan substantially determined, controlled or suggested by the franchisor or an associate of the franchisor”. [sub-clause 4(1)(b)]

[The relevant nexus to Australia in order for the Code to apply is, as identified in this definition, effectively the conduct of business in Australia by the franchisee. Foreign franchisors, such as foreign corporations, are not exempt from the application of the Code. When the Code was first brought into effect, clause 5(3)(a) provided that the Code did not apply to franchisors who/which were resident, domiciled or incorporated outside Australia and had only a master franchise or one franchisee in Australia. The most recent amendments to the Code, which took effect from 1 March 2008, removed that exemption.]

- (c) A franchise agreement requires the operation of the business to be “substantially or materially associated with a trade mark, advertising or a commercial symbol”. [sub-clause 4(1)(c)]
- (d) Finally, a franchise agreement will require, as an essential feature, the payment, or an agreement to pay, an amount to the franchisor. [sub-clause 4(1)(d)]

21. Notwithstanding the broad nature of the definition of ‘franchise agreement’, certain categories of relationship are expressly identified as not in themselves constituting a franchise agreement, including employer/employee, partnership, landlord/tenant, and lender/borrower relationships.

[Please note: The above relationships can constitute franchisor/franchisee relationships in appropriate circumstances. The Code simply clarifies that the mere fact that the parties have a relationship that falls into the aforementioned descriptions does not mean that they automatically are treated as subject to the Code and the Act.]

22. An important consequence of the wide nature of the definition of ‘franchise agreement’, as set out in clause 4 of the Code, is that there may not always be certainty that an agreement is a franchise agreement for the purposes of the Code. The mere fact that the parties to an agreement call an agreement a “franchise agreement” would not necessarily mean that it was, although it would be extraordinary for commercial parties to mistake the nature of their relationship to that extent.

23. More importantly, however, agreements, which either one or both of the parties may never have thought to have been a franchise agreement, may well fall within the definition.
24. Occasionally, the Courts have had to deal with the preliminary contested issue as to whether or not an agreement is actually a franchise agreement. See, for example, *A CCC v Kyløe Pty Ltd* [2007] FCA 1522 at [22]-[69] per Tracey J and *Capital Networks Pty Ltd v.au Domain Administration Limited* [2004] FCA 808 at [92]-[126] per Bennett J. In both of those cases, it was held that the agreements were not franchise agreements for the purposes of the Code. One area where the line between agreements that are franchise agreements as opposed to those that are not can be uncertain is in relation to the issue of the extent to which the supply of goods or services is undertaken pursuant to “a system or marketing plan substantially determined, controlled or suggested by the franchisor” (sub-clause 4(1)(b)).
25. In *A CCC v Kyløe Pty Ltd* [2007] FCA 1522 at [58], Tracey J referred to the analysis undertaken by Bennett J in the *Capital Networks Pty Ltd* case and stated:

In *Capital Networks*, Bennett J distilled from the American cases, a number of factors which assisted in determining whether the required degree of control over the system or marketing plan was exercised by the alleged franchisor:

- the extent to which the distributor’s business involved the sale of the alleged franchisor’s products – the smaller the percentage the less likely it will be that the necessary degree of control will be found to exist;
- whether or not the alleged franchisor ostensibly assumed responsibility for product outlets causing them to be operated with the appearance of some centralised management and with uniform standards as regards the quality and price of goods sold, services rendered and other material instances of the operation;
- whether or not the alleged franchisor placed the distributor under an obligation to advertise, to conduct promotions and to stock accessories; and
- the extent to which the alleged franchisor controls the franchisee’s business having regard to matters such as prescription of the hours and days of operation, advertising, financial support, auditing of books, inspection of premises, control over lighting, employee uniform, prices, trading stamps, hiring, sales quotas and management training.

26. Clause 5 of the Code provides that its provisions apply to any franchise agreements entered into on or after 1 October 1998. It must be kept in mind, however, that a 'franchise agreement' is defined by clause 4(2)(a) of the Code to include a "transfer, renewal or extension of a franchise agreement". Therefore, unless a current franchisee still remains (more than 10 years after the commencement of the relevant provisions of the Code) within the original term of the franchise agreement, no franchise agreement will be exempt from the application of the Code.
27. Although it would be a relatively unusual circumstance for it to be applicable, the further exemption from the Code specified in clause 5(3)(b) should be noted. This covers franchisees, who have become franchisees but for the specific purpose of continuing to supply goods already supplied previously by them (for at least 2 years) and provided that their sales as a franchisee are not likely to provide more than 20% of their gross turnover for goods or services of that kind.

B. "Part 2" of the Code – "Disclosure"

28. Part 2 of the Code sets out the obligations imposed upon a franchisor in relation to disclosure to a franchisee or a prospective franchisee.

Division 2.1 of the Code – "Disclosure document"

29. The disclosure document provisions (Division 2.1 of the Code) are included in clauses 6 to 7. Although it is not intended to provide in this paper any analysis of the individual components of satisfactory versus unsatisfactory disclosure documents, the following observations can be made generally about the Division 2.1 provisions.
30. A franchise disclosure document is not a document that can be prepared once, when the franchisor first sets up the franchise or when the franchisor first takes on a particular franchisee, and then forgotten. It is a document that must be reviewed and revised for franchisees on a regular basis (see clause 6(1) of the Code).

31. As identified by clause 6A, the purpose of a disclosure document is:
 - (a) to give a prospective franchisee, or a franchisee proposing to enter into, renew or extend a franchise agreement, information from the franchisor to help the franchisee to make a reasonably informed decision about the franchise; and
 - (b) to give a franchisee current information from the franchisor that is material to the running of the franchised business.
32. The circumstances, in which a franchisor is obliged to provide a disclosure document, namely always, are identified in clause 6B. In particular, a franchisor, which has a sub-franchisor which itself conducts the franchise, is not excluded from the obligation to provide a disclosure document. That franchisor may either provide its own separate disclosure document to the sub-franchisee (clause 6B(2)(a)(i)) or, alternatively, may join with the sub-franchisor in providing the sub-franchisee with a joint disclosure document (clause 6B(2)(a)(ii)).
33. The format of the disclosure document is mandated by clause 7 of the Code. Annexures 1 and 2 to the Code provide the detailed identification of the format of, and the information required to be contained in, a disclosure document. [Those annexures are not included in the copy of the Code attached to this paper.]
34. Annexure 1 provides the full length version of the disclosure document. There is identified in the annexure a comprehensive list of the information required, including:
 - (a) Details of the franchisor;
 - (b) Business experience of persons who have management responsibilities with the franchisor;
 - (c) Details of current proceedings, including civil litigation, and details of recent convictions (in previous 10 years), civil judgments (in previous 5 years), and bankruptcies or external administrations (in previous 10 years);
 - (d) Identification of existing franchises;
 - (e) Details of payments required from the franchisee;
 - (f) Details of the obligations to be undertaken by the franchisor;
 - (g) Details of obligations to be imposed upon the franchisee; and

- (h) If earnings information is given, only reliable financial information.
35. Annexure 2 provides a short form of the disclosure document, which can be utilised by a franchisor. However, if a franchisee or prospective franchisee, who is provided with a short form disclosure document, wishes to be provided with the further information that would have been included in the long version disclosure document (had it been utilised by the franchisor), they simply have to ask for that additional information and the franchisor is obliged to provide it (clause 6C – “Additional information”).
36. Clause 6C of the Code identifies, therefore, an important entitlement on the part of the franchisee or prospective franchisee.
37. Thus, through the combined effect of clause 6B of the Code (“Requirement to give disclosure document”), clause 6C (“Additional information”), and clause 7 (“Layout”), the Code provides for an extremely detailed set of disclosure obligations on the part of a franchisor.
38. Gone are the days when a franchisor may have thought that their role, obligation and function was simply to ‘sell’ franchises and then allow the franchisees to work out for themselves whether or not the business proposition entailed by the franchise was to their desire and whether there was any relevant undisclosed risk that would be faced by taking up a franchise.
39. In essence, the regulatory structure of the Code has recognised that franchisees, who had a tendency to receive the blunt end of the informational asymmetry, are in need of significant protection through positive entitlements to information. The Code seems clearly also to have recognised that franchising is not an industry that involves one-off or financially-immaterial transactions. People proposing to become franchisees are often called upon to invest large amounts of capital, both in terms of upfront or ongoing franchise fees and in terms of their own capital expenditure for the purpose of making the business a success. It is not, therefore, a situation that is amenable to the *caveat emptor* principle. It is really in the nature of an ongoing (one might even say almost fiduciary) relationship between the franchisor and franchisee.

Division 2.2 of the Code – “Before franchise agreement”

40. Given the aforementioned importance of the decision by a prospective franchisee to enter into a franchise agreement or by a franchisee to renew or extend a franchise agreement, Division 2.2 of the Code focuses specifically upon obligations that are imposed upon a franchisor prior to entry into the franchise agreement by the prospective franchisee.
41. Clause 10 (“Franchisor obligations”) specifies that, at least 14 days prior to entry into the franchise agreement or the making of a non-refundable payment by the prospective franchisee, the franchisor must give the prospective franchisee:
- (a) a copy of the Franchising Code of Conduct;
 - (b) a disclosure document; and
 - (c) a copy of the franchise agreement, in the form in which it is to be executed.
42. Clause 11 (“Advice before entering into franchise agreement”) is a significant provision. It provides:
- (1) The franchisor must not:
 - (a) enter into, renew or extend a franchise agreement; or
 - (b) enter into an agreement to enter into, renew or extend a franchise agreement; or
 - (c) receive a non-refundable payment (whether of money or of other valuable consideration) under a franchise agreement or an agreement to enter into a franchise agreement;unless the franchisor has received from the franchisee or prospective franchisee a written statement that the franchisee or prospective franchisee has received, read and had a reasonable opportunity to understand the disclosure document and this code.
 - (2) Before a franchise agreement is entered into, the franchisor must have received from the prospective franchisee:
 - (a) signed statements, that the prospective franchisee has been given advice about the proposed franchise agreement or franchised business, by any of:
 - (i) an independent legal adviser;
 - (ii) an independent business adviser;
 - (iii) an independent accountant; or

- (b) for each kind of statement not received under paragraph (a), a signed statement by the prospective franchisee that the prospective franchisee:
 - (i) has been given that kind of advice about the proposed franchise agreement or franchised business; or
 - (ii) has been told that that kind of advice should be sought but has decided not to seek it.
 - (3) Subclause (2):
 - (a) does not apply to the renewal or extension of a franchise agreement with a franchisor; and
 - (b) does not prevent the franchisor from requiring any or all of the statements mentioned in paragraph (2)(a).
- 43. It was the mandatory obligation of the franchisor under each of clause 11(1) and 11(2) of the Code that formed the central issue of dispute during the long history of the litigation in *Master Education Services Pty Ltd v Ketchell* [2008] HCA 38; (2008) 82 ALJR 1322. That case is discussed later in this paper.
- 44. The purpose of clause 11 is tolerably clear, although any doubt is removed by reference to the relevant explanatory statement that accompanied the regulation. It aims to ensure that prospective franchisees are given as much warning as is reasonably practical as to:
 - (a) their entitlements under the Code;
 - (b) the information contained in the franchisor's disclosure document;
 - (c) the precise terms that will become part of the franchise agreement; and
 - (d) the importance of obtaining independent advice (legal, business, and accounting) in relation to the prospective franchise.
- 45. It is perhaps slightly curious that clause 11(2)(a) speaks of the franchisor obtaining a signed statement regarding advice having been obtained by the franchisee from "any of" the three types of advisors, yet clause 11(2)(b) imposes as an alternative requirement the provision of a statement relating to "each kind of statement" not received. The better view of the correct interpretation of those two sub-clauses would seem to be that they be read together so as to require all three types of advice (legal, business, and accounting) to be dealt with, either by a signed statement of receipt of advice or, alternatively, by an acknowledgement that the franchisee has been told that that advice should be sought but has decided not to seek it.

46. Two important features of the structure of clause 11 of the Code, being also matters raised in submissions to the High Court in the *Master Education Services Pty Ltd v Ketchell* case and which may have contributed to the views expressed by the Court at [39]⁵, are:
- (a) that the requirements placed upon the franchisor (in sub-clauses 11(1) and (2)) each involve the receipt by the franchisor of a document from a prospective franchisee; and
 - (b) that each of the signed statements required by sub-clauses 11(1) and (2), although constituting an acknowledgement by the prospective franchisee of the matters identified therein, are of an evidentiary nature only – that is, the fact that a prospective franchisee has signed the aforementioned statements, although no doubt reducing or removing the risk that they might allege unfairness, does not mean that the substance of the signed statements were accurate. For example, although stating that they had, the prospective franchisee may not, in fact, have read (carefully or at all) the disclosure document. Further, the reverse may be the case – just because no signed statement is obtained, it certainly does not follow that the prospective franchisee has not carefully read and taken the opportunity to understand the documents.⁶
47. Some practical questions arise from the above. For example, what happens if the prospective franchisee neglects (or even refuses) to supply the signed statements mandated by clause 11?

⁵ At [39], the Court stated: “Some cases of non-compliance with cl 11 might involve substantial non-disclosure; others may only involve a failure to obtain the written statement, confirming that the franchisee has read and understood the disclosure document and the Code. This is such a case.”

⁶ Also, it would not be unreasonable to ask the question: What precisely is meant by “and had a reasonable opportunity to understand”? No doubt, each case would have to be assessed on its own facts and circumstances, including in light of the sophistication of the prospective franchisee and the degree of access to professional advisors that was available to the prospective franchisee.

48. There are two answers, one of which is the technically proper approach and the other is the pragmatic and probably relatively safe approach, particularly in light of the High Court's judgment in the aforementioned case:

- (a) The first option is for the franchisor simply to refuse to enter into the franchise agreement until such time as the required signed statements are obtained. Not only is this technically the better approach, but it also is likely to elicit a very prompt response from a prospective franchisee, who actually desires to enter the franchise.

On the other hand, it is hardly an unknown circumstance for parties entering a commercial arrangement to leave procedurally important (sometimes even substantively important) steps to a later point in time, preferring rather to concentrate upon fast-tracking the flow of commercial benefit from the arrangement.

- (b) The second option is simply, in lieu of having actually received the required signed statements, to engage in a thorough process of having recorded and documented (particularly in written communications with the prospective franchisee) the steps taken to chase up the provision of the signed statements and the advices given to the prospective franchisee as to why it is important that such signed statements be provided. This must, of course, be accompanied by unchallengeable proof that the three critical documents (the Code, the disclosure document, and the proposed franchise agreement) were supplied to the prospective franchisee in accordance with clause 10 of the Code.

C. "Part 3" of the Code – "Conditions of franchise agreement"

- 49. Part 3 of the Code sets out mandatory conditions that apply to franchise agreements.
- 50. Clause 13 ("Cooling off period") mandates a cooling off period of 7 days, which commences from the earlier of the date of the entry into the franchise agreement or the making of any payment (including of valuable consideration) under the agreement. Such cooling off period does not apply in respect of renewals, extensions or transfers of existing franchise agreements (clause 13(2)).

51. Clause 16 (“Prohibition on release from liability etc”) is of great significance, particularly in the context of disputes regarding the making of pre-contractual representations by a franchisor. It provides:
- (1) A franchise agreement entered into on or after 1 October 1998 must not contain, or require a franchisee to sign:
 - (a) a general release of the franchisor from liability towards the franchisee; or
 - (b) a waiver of any verbal or written representation made by the franchisor.
52. As previously stated, the structure of the Code is such that ongoing disclosure on a regular basis (at least annually) is required by a franchisor. Clause 18 of the Code (“Disclosure of materially relevant facts”) goes a step further in imposing that obligation upon franchisors.
53. Clause 18 requires effectively immediate disclosure to all franchisees of “materially relevant facts” within 14 days after the franchisor becomes aware of them. Those matters that are required to be disclosed in this ongoing way are identified at sub-clause 18(2). Those matters include the details of any judgment against the franchisor and the details of any civil proceedings in Australia that have been commenced against a director of the franchisor by at least 10% or 10 of the franchisees in Australia.
54. The rationale for the above requirements is clear and compelling. Nevertheless, in some unfortunate circumstances, the burden upon a franchisor can be great. For example, a franchisor, which loses a civil proceeding at first instance but intends to appeal (or even has appealed), is still required to disclose the unfavourable judgment to all franchisees. In some cases, that required disclosure, irrespective of how unreasonable the decision of the court or tribunal may seem to be, can provide a significant impediment to the sale by the franchisor of other franchises.
55. If there was ever a clear motivation for a franchisor, who relies upon the ongoing sale of franchises, to maintain good procedures and to stay out of court, that is a strong one.
56. Clause 19 (“Current disclosure document”) provides further back-up protection to franchisees regarding obtaining the most up-to-date information available regarding the matters required to be disclosed by a franchisor. Clause 19 permits a request to

be made, not more than once in 12 months, by a franchisee for “a current disclosure document”. The franchisor must respond within 14 days.

57. Clause 20 (“Transfer of the franchise”) deals with a problem occasionally faced, namely where a franchisee is either locked into a franchise unreasonably or is threatened with being locked into the franchise unless the franchisee agrees to some other arrangement with the franchisor. The Code makes clear that a franchisor’s consent to the transfer of a franchise cannot be withheld unreasonably. There is, however, protection provided by the Code to the franchisor. Sub-clause 20(3) sets out “the circumstances in which it is reasonable for a franchisor to withhold consent”, which include:

- where the proposed transferee is unlikely to be able to meet the financial obligations under the franchise agreement;
- where the proposed transferee has not met the selection criteria of the franchisor;
- the franchisee has not paid or made reasonable provision to pay an amount owing to the franchisor;
- the franchisee has breached the franchise agreement and has not remedied the breach.

58. Perhaps interestingly, although less likely to be of practical consequence, the above identification of circumstances in which refusal of a transfer will be reasonable could, in certain circumstances, advantage a franchisor.

For example, a franchisee may be in breach of their franchise agreement, but may also think that they have valid claims against the franchisor for breach. The franchisee wants to exit the situation by selling the franchise. Clearly, the franchisee may be reluctant to take steps to terminate the franchise agreement for the franchisor’s breach, because such termination will leave the franchisee with nothing to sell. Consequently, a franchisor may well end up in the advantageous position of being able to negotiate favourable terms, because it can withhold consent to a transfer of the franchise by the franchisee. In particular, I would have thought a minimum request by a franchisor would be for the execution of a separate independent release of the franchisor regarding any alleged breaches of the franchise agreement. Whether or not the circumstance, in which the franchisor utilised this

negotiation power to extract such a release would itself constitute unconscionable conduct under section 51AC of the Act may well depend upon the circumstances. It could not, however, be ruled out.

59. Clauses 21 to 23 of the Code are also particularly important, because they provide an identification of particular requirements, obligations and entitlements relating to the termination of a franchise agreement. No method of alternative drafting of a franchise agreement can nullify the operation of these provisions.
60. An example of a case, in which the issue in dispute was whether or not the franchisor's refusal to consent to a transfer of the franchise by the franchisee, is *Lockhart v Holden* [2008] QSC 257 (Douglas J).
61. Clause 21 ("Termination – breach by franchisee") requires, in the absence of the existence of "special circumstances" (which are dealt with in clause 23), that a franchisor, which proposes to terminate a franchise agreement, must:
 - (a) give to the franchisee reasonable notice of the intention to terminate;
 - (b) tell the franchisee what is required to be done in order to remedy the breach; and
 - (c) allow the franchisee a reasonable time to remedy the breach.
62. Sub-clause 21(3) clarifies that "a reasonable time" will not exceed 30 days or, if it would exceed 30 days, the franchisor nevertheless is not required to allow the franchisee more than 30 days in order to remedy the breach.
63. Clause 22 ("Termination – no breach by franchisee") applies where a franchisor proposes to terminate a franchise agreement, before it expires, but without the consent of the franchisee and without there having been a breach by the franchisee. The only requirement imposed by this clause is that, before so terminating the franchise agreement, the franchisor must give "reasonable notice of the proposed termination, and reasons for it, to the franchisee" (sub-clause 22(3)). Sub-clause 22(4) also specifically identifies that the dispute resolution provisions of Part 4 of the Code apply.

64. Assuming that a franchisor has a contractual entitlement to termination in the manner identified above, the only real effect of clause 22 would appear to be two-fold:
 - (a) first, it compels the franchisor to provide reasons for the proposed termination a reasonable period of time before doing so, which is of advantage to the franchisee, because the franchisee may not otherwise have been entitled to an explanation for the proposed termination; and
 - (b) second, it 'compels' mediation of the dispute, thus perhaps giving the franchisee an opportunity to convince the franchisor that termination is not an appropriate response or strategy on the franchisor's part.
65. Clause 23 of the Code ("Termination – special circumstances") is probably of more practical interest than clause 22. It provides:

A franchisor does not have to comply with clause 21 or 22 if the franchisee:

 - (a) no longer holds a licence that the franchisee must hold to carry on the franchised business; or
 - (b) becomes bankrupt, insolvent under administration or an externally-administered body corporate; or
 - (c) voluntarily abandons the franchised business or the franchise relationship; or
 - (d) is convicted of a serious offence; or
 - (e) operates the franchised business in a way that endangers public health or safety; or
 - (f) is fraudulent in connection with operation of the franchised business; or
 - (g) agrees to termination of the franchise agreement.

D. "Part 4" of the Code – "Resolving disputes"

66. Part 4 of the Code sets out the mechanisms that are required to be complied with for the purpose of attempting to resolve disputes arising under or in relation to franchise agreements.
67. The practical benefits of the provisions of Part 4 are limited, as they always were likely to be. The Code does not provide a prohibition on the commencement of court proceedings in the absence of compliance with the dispute resolution procedures in the Code.

68. There would unlikely be, for example, circumstances in which a party who has been joined to civil proceedings could seek a temporary or permanent stay of the proceedings pending fulfilment of the parties' obligations under the dispute resolution procedures of the Code. Clause 31 of the Code ("Conditions") provides:
 - (1) This Part does not affect the right of a party to a franchise agreement to take legal proceedings under the franchise agreement.
69. Notwithstanding the above, where parties are reluctant to commence proceedings in relation to their dispute and therefore wish to mediate, the Code provides a standard mandatory procedure regarding that process.
70. Clause 26 of the Code ("Internal complaint handling procedure") requires that all franchise agreements entered into on or after 1 October 1998 must provide for a complaint handling procedure that complies with clauses 29 and 30. There is no need to set out in full the terms of those clauses, but it might simply be noted that those procedures involve, unsurprisingly, the communication of information between the mediating parties as to the nature of the dispute and then a broad timetable for the appointment of a mediator and the conduct of a mediation.
71. Precisely how, in practice, the mandatory complaint handling procedures contained in clauses 29 and 30 (being those required by clause 26) will be enforced is not clear. If the parties wish to mediate, but one party does not wish to adhere to the mediation procedure identified by the Code, it would presumably be open to the other party to approach a court for injunctive relief so as to compel adoption of the mediation procedure required by the Code. That step would, however, seem to be self-defeating, in that a party would be approaching a court for relief in relation to a dispute that the party may never have wanted to go to court.
72. On balance, Part 4 of the Code is unlikely to have anything more by way of a practical impact upon disputing (or potentially disputing) parties than a 'gentle persuasive' effect as to the method of discussing their issues.

PART III: ENFORCEMENT OF CODE

73. From a litigator's perspective, the obvious and important question is whether and, if so, to what extent the provisions of the Code can be enforced by a client. Further, there may arise an issue as to how to do so.

A. Mechanism for Enforcement of Code

74. A breach of the Code is, as already identified, a breach of section 51AD of the Act, which prohibits conduct in contravention of any applicable industry code.
75. Consequently, as one might envisage, the remedy for a party aggrieved by another party's breach of the Code is to bring proceedings alleging a breach of section 51AD of the Act and to seek relief pursuant to one or other of the provisions of Part VI of the Act. It being unnecessary to provide any details regarding the extensive nature of those available remedies, it is sufficient to note that the available remedies include:
- (a) injunctions, including *quia timet* injunctions against anticipated breaches of section 51AD (section 80);
 - (b) damages (section 82); and
 - (c) other orders, including orders declaring a contract to be void and an order refusing to enforce provisions of a contract (section 87 – examples of orders available identified in sub-section 87(2)).
76. Certainly prior to 2007, the orthodox view was that a contravention of the Code would result and could only result in an ability to make a claim for relief pursuant to the Act in a court of appropriate jurisdiction.
77. This view was expressed by Windeyer J in *The Cheesecake Shop v A & A Shah Enterprises* [2004] NSWSC 625. In that case, the plaintiff, which was bringing action in reliance upon the terms of the franchise agreement. The defendant sought to resist the application, at least in part, by suggesting that the plaintiff, having not complied with the requirements of clause 11 of the Code (which state that various steps must be taken before a contract is entered into), could not sue upon the contract. The argument was that the contract, being entered into in breach of the mandatory requirement of clause 11, was unenforceable by the plaintiff. The

argument did not succeed. At [40]-[41], Windeyer J identified the wide range of remedies available under Part VI of the Act in respect of contraventions of various provisions of the Act, including section 51AD. At [41], his Honour then concluded:

Section 51AD does not make contracts made in contravention of the Code illegal. The section, like s 51AC, is addressed to conduct. The matter is really determined by a consideration of Pt IV of the Act. Section 52 prohibits certain conduct; s 51AD prohibits certain conduct; s 51AC prohibits certain conduct; s 51AA prohibits certain conduct. For all breaches Part VI remedies are available, including a power to declare a contract void. If it is void as illegal, there is no need for this. The argument must fail.

78. That orthodox view of the interpretation of the operation of the Code and s 51AD was, however, turned on its head when the New South Wales Court of Appeal determined the appeal in the matter of *Ketchell v Master Education of Services Pty Ltd* [2007] NSWCA 161. On 19 July 2007, the Court delivered a judgment that gave strict force to the words appearing in clause 11(1) of the Code, namely “must not ... enter into”, such that a franchise agreement entered into without satisfaction of that pre-condition in clause 11(1) would be void as illegal. The Court drew no distinction between whether the non-compliance with the Code was serious or inadvertent, nor whether any actual loss or damage or detriment flowed from the breach. The resultant illegality was an automatic consequence of non-compliance.
79. The decision was critical in a number of ways, including to the manner in which litigious disputes between franchisees and franchisors would be conducted. Suddenly, a franchisee, who was seeking either to get out of a franchise agreement or to resist a claim against them by a franchisor seeking, for example, payment of outstanding franchise fees, had only to find a technical non-compliance with clauses of the Code such as clauses 11(1) or 11(2) and arguably also clauses 6 and 10.
80. Once word of the Court of Appeal’s decision spread, it was not long before the aforementioned arguments began being utilised. In *Civic Video Pty Ltd v Garfell Nominees Pty Ltd* [2008] NSWDC 3, Rolfe DCJ was compelled, by the binding nature of the Court of Appeal’s decision in the *Ketchell* case and upon a hearing of this discrete issue as a preliminary matter, to dismiss the plaintiff’s claim for damages of up to \$750,000. That decision was reached, as it was required by reason of the binding authority, without any reference whatsoever to the underlying merits of the position of the franchisor or the franchisee.

81. Special leave to appeal the New South Wales Court of Appeal's judgment in the *Ketchell* case was granted and an appeal was heard in early 2008. In *Master Education Services Pty Ltd v Ketchell* (2008) 82 ALJR 1322, the High Court unanimously allowed the appeal. In so doing, the Court stated at [25]:

The purposes of the scheme of Pt IVB and the Code in question are to regulate the conduct of persons in the franchising industry in order to improve business practices, to provide some protection to franchisees proposing to enter into franchise agreements and to decrease litigation. Those purposes are sought to be achieved, in large part, by ensuring that a prospective franchisee is in a position to make an informed decision about the operation of the franchise and is encouraged to take independent advice before entering into a franchise agreement. The scheme is largely directed to the franchisor, who is obliged to provide that information and advice. Section 51AD may be seen to promote compliance with the Code, by providing, in effect, that non-compliance will amount to a contravention, for which there are remedies available under Pt VI. It is no part of the scheme, and unnecessary to the purposes mentioned, to strike down a contract made by a non-complying franchisor. It is sufficient for the purpose of the scheme that a franchisor is aware of the obligations imposed by the Code and that action may be taken by a franchisee under the Act with respect to a contravention of s 51AD.

82. Just a few days prior to the hearing of the High Court appeal in the *Master Education Services Pty Ltd* case, his Honour Justice Rares delivered judgment in the Federal Court of Australia in *Hoy Mobile Pty Ltd v Allphones Retail Pty Ltd (No 2)* [2008] FCA 810. His Honour declined to follow the New South Wales Court of Appeal's judgment, citing a number of reasons, but primarily that it was thought to be a clearly wrong decision.
83. It has, therefore, now been confirmed that a breach of the Code is available to be remedied only by action pursuant to the Act⁷.

⁷ The author of this paper has been informed that an appeal against the District Court decision in *Civic Video Pty Ltd v Garfell Nominees Pty Ltd* was allowed by consent, when it became known that the High Court had delivered its judgment in the *Master Education Services Pty Ltd* case, and that the matter has now been returned to the District Court for a full hearing.

B. Requirement for a Successful Claim Under Section 51AD

84. As with any claim for relief under the Part VI provisions of the Act, a party seeking orders by reason of a breach of section 51AD of the Act is required to establish some loss, damage or detriment, or a reasonable anticipation of such detriment (for the purpose of seeking injunctive relief). That is not a novel proposition – section 51AD operates in precisely the same manner as would a claim pursuant to section 52 of the Act. Likewise, insofar as non-compliance with the Code is a factor that may be taken into account for determining whether the conduct of a party to a franchise agreement has been unconscionable, also for section 51AC.
85. It becomes critical, therefore, that any proposed action for relief under the Act be focussed upon the correct issue and seeks relief that is necessary or appropriate so as to compensate for and/or protect against proved loss (or a threat of loss).
86. In the case of breaches of the Code, that may become, depending upon the factual circumstances of the individual case, quite a difficult proposition.
87. Insofar as, for example, a franchisee seeking to obtain relief arising from a franchisor's non-compliance with the Code may be wishing to assert that the franchisee would have acted differently if the franchisor had complied with its obligations, that evidence will need to be cogent and persuasive. It is difficult enough to convince courts of the likelihood of the occurrence of hypothetical situations – it is all the more difficult when the complaint is coming from a franchisee, who may have a strong self-serving purpose for presenting an incomplete or inaccurate picture of what he or she would or would not have done. For example, a franchisee's claim for damages or other relief under the Act often arises as a response to a claim by a franchisor for unpaid franchise fees.
88. In those circumstances, a lawyer acting for an aggrieved franchisee will really need to obtain detailed instructions as to what the franchisee says would have occurred if, for example, the franchisor had disclosed accurately that the expected turnover of the franchise business was \$8,000 per week rather than \$10,000 per week. It will likely be entirely insufficient for the franchisee merely to assert: "Had I known that, I would not have entered the agreement." Easy to say – harder to prove.

89. In addition to the above comments, which really are only (and can only be) of the most general nature, it is worthwhile also not to entirely forget the possibility of obtaining injunctive relief so as to compel compliance with the Code. As it was observed earlier in this paper, however, there would seem to be relatively few circumstances where such an approach would be sufficiently useful to warrant the expense.
90. As quite accurately observed by the High Court in *Master Education Services Pty Ltd v Ketchell*, the real purpose of the Code is to reduce litigation by keeping franchisees adequately informed so as to be able to make proper decisions regarding the franchise business.

PART IV: CONCLUSION

91. The Franchising Code of Conduct, enforced via section 51AD of the Act, is an extremely important tool, both for franchisors and franchisees.
92. For franchisors, it provides a detailed and reliable guide as to the conduct that is to be undertaken in order to minimise the likelihood of expensive disputes with franchisees in courts.
93. For franchisees, it likewise provides guidance by identifying what types of conduct, including the provision of information, can be expected on their part from franchisors. Many disputes in the franchising sector in past years would almost certainly have been limited in their scope or eliminated entirely if accurate and reliable information was provided by the franchisor prior to the franchisee becoming financially committed to a disappointing business enterprise.
94. Consequently, it is not surprising, as revealed by the recent statistics identified earlier in this paper, that the operation of the Code has coincided with an apparent decrease in the level of disputation in the franchising sector.

VAHAN BEDROSSIAN
Edmund Barton Chambers
18 March 2009

Schedule Franchising Code of Conduct

(regulation 3)

Part 1 Preliminary

1 Name of code

This code is the Franchising Code of Conduct.

2 Purpose of code

The purpose of this code is to regulate the conduct of participants in franchising towards other participants in franchising.

3 Definitions

(1) In this code:

ABN has the same meaning as it has in the *A New Tax System (Australian Business Number) Act 1999*.

associate, for a franchisor, means a person:

- (a) who:
 - (i) is a director or related body corporate, or a director of a related body corporate, of the franchisor; or
 - (ii) for a franchisor that is a proprietary company — directly or indirectly owns, controls, or holds with power to vote, at least 15% of the issued voting shares in the franchisor; or
 - (iii) is a partner of the franchisor; and
- (b) whose relationship with the franchisor is relevant to the franchise system, including supplying goods, real property or services to a franchisee.

disclosure document has the meaning given by clause 6.

franchise includes the following:

- (a) the rights and obligations under a franchise agreement;
- (b) a master franchise;

- (c) a subfranchise;
- (d) an interest in a franchise.

franchise agreement has the meaning given by clause 4.

franchisee includes the following:

- (a) a person to whom a franchise is granted;
- (b) a person who otherwise participates in a franchise as a franchisee;
- (c) a subfranchisor in its relationship with a franchisor;
- (d) a subfranchisee in its relationship with a subfranchisor.

franchise system includes a business system in which a franchisor grants a franchise to a franchisee.

franchisor includes the following:

- (a) a person who grants a franchise;
- (b) a person who otherwise participates in a franchise as a franchisor;
- (c) a subfranchisor in its relationship with a subfranchisee;
- (d) a master franchisee in a master franchise system;
- (e) a master franchisee in its relationship with a franchisee.

interest in a franchise includes a legal or beneficial interest in:

- (a) a franchise agreement or a franchised business; or
- (b) shares or voting rights in a corporation, not being a listed corporation that owns a franchised business; or
- (c) units or voting rights in a unit or other trust that owns a franchised business; or
- (d) the capital or income of a partnership that owns a franchised business.

master franchise means a franchise in which the franchisor grants to a subfranchisor or master franchisee the right:

- (a) to grant a subfranchise; or
- (b) to participate in a subfranchise.

master franchisee or **subfranchisor** means a person who is:

- (a) a franchisee in relation to a master franchise; and
- (b) a franchisor in relation to a subfranchise granted under the master franchise.

motor vehicle means a vehicle that uses, or is designed to use, volatile spirit, gas, oil, electricity or any other power (except human or animal power) as the principal means of propulsion, but does not include a vehicle used, or designed to be used, on a railway or tramway.

Examples of motor vehicles

- 1 motor car
- 2 motor cycle
- 3 motorcycle
- 4 tractor
- 5 motorised farm machinery
- 6 motorised construction machinery
- 7 aircraft
- 8 motor boat

motor vehicle dealership means a business of buying, selling, exchanging or leasing motor vehicles that is conducted by a person other than a person who is only involved as a credit provider, or provider of other financial services, in the purchase, sale, exchange or lease.

prospective franchisee means a person who deals with a franchisor for the right to be granted a franchise.

serious offence means:

- (a) an offence under any law of the Commonwealth or a State or a Territory for which, if the act or omission had taken place in the Jervis Bay Territory, a person would be liable, on first conviction, to imprisonment for a period of not less than 5 years; or
- (b) a contravention of any provision of the *Corporations Act 2001*.

Note Jervis Bay Territory is mentioned because it is a jurisdiction in which the Commonwealth has control over the criminal law.

subfranchisor has the same meaning as **master franchisee**.

supply see subsection 4 (1) of the Act.

Note 1 Under subsection 4 (1) of the Act, **supply**, when used as a verb, includes:

- (a) for goods — supply (including re-supply) by way of sale, exchange, lease, hire or hire-purchase; and
 - (b) for services — provide, grant or confer;
- and, when used as a noun, has a corresponding meaning.

Note 2 the Act means the *Trade Practices Act 1974* (see the *Trade Practices Regulations*, r 2 (1)).

trade mark has the meaning given by the *Trade Marks Act 1995*.

Note A **trade mark** is a sign (including any letter, word, name, signature, numeral, device, brand, heading, label, ticket, aspect of packaging, shape, colour, sound or scent (or any combination of these)) used, or intended to be used, to distinguish goods or services dealt with or provided in the course of trade by a person from goods or services so dealt with or provided by any other person (see *Trade Marks Act 1995*, s 17).

transfer, for a franchise, includes an arrangement in which the franchise is granted, transferred or sold.

- (2) In this code, the following terms have the meanings given by the *Corporations Act 2001*:

accounting standard	listed corporation
ACN	misconduct
ARBN	officer
body corporate	proprietary company
director	registered company
externally-	auditor
administered body	registered office
corporate	related body corporate
insolvent under	small proprietary
administration	company

4 **Meaning of franchise agreement**

- (1) A **franchise agreement** is an agreement:
- (a) that takes the form, in whole or part, of any of the following:
 - (i) a written agreement;
 - (ii) an oral agreement;
 - (iii) an implied agreement; and
 - (b) in which a person (**the franchisor**) grants to another person (**the franchisee**) the right to carry on the business of offering, supplying or distributing goods or services in Australia under a system or marketing plan substantially determined, controlled or suggested by the franchisor or an associate of the franchisor; and

- (c) under which the operation of the business will be substantially or materially associated with a trade mark, advertising or a commercial symbol:
 - (i) owned, used or licensed by the franchisor or an associate of the franchisor; or
 - (ii) specified by the franchisor or an associate or the franchisor; and
 - (d) under which, before starting business or continuing the business, the franchisee must pay or agree to pay to the franchisor or an associate of the franchisor an amount including, for example:
 - (i) an initial capital investment fee; or
 - (ii) a payment for goods or services; or
 - (iii) a fee based on a percentage of gross or net income whether or not called a royalty or franchise service fee; or
 - (iv) a training fee or training school fee;but excluding:
 - (v) payment for goods and services at or below their usual wholesale price; or
 - (vi) repayment by the franchisee of a loan from the franchisor; or
 - (vii) payment of the usual wholesale price for goods taken on consignment; or
 - (viii) payment of market value for purchase or lease of real property, fixtures, equipment or supplies needed to start business or to continue business under the franchise agreement.
- (2) For subclause (1), each of the following is taken to be a franchise agreement:
- (a) transfer, renewal or extension of a franchise agreement;
 - (b) a motor vehicle dealership agreement.
- (3) However, any of the following does not in itself constitute a franchise agreement:
- (a) an employer and employee relationship;
 - (b) a partnership relationship;

- (c) a landlord and tenant relationship;
- (d) a mortgagor and mortgagee relationship;
- (e) a lender and borrower relationship;
- (f) the relationship between the members of a cooperative that is registered, incorporated or formed under any of the following laws:
 - (i) *Co-operatives Act 1992* of New South Wales;
 - (ii) **Co-operatives Act 1996** of Victoria;
 - (iii) *Cooperatives Act 1997* of Queensland;
 - (iv) *Co-operative and Provident Societies Act 1903* of Western Australia;
 - (v) *Co-operatives Act 1997* of South Australia;
 - (vi) *Co-operative Industrial Societies Act 1928* of Tasmania;
 - (vii) *Co-operative Societies Act 1939* of the Australian Capital Territory;
 - (viii) *Co-operatives Act 1997* of the Northern Territory;
 - (ix) the *Corporations Act 2001*.

5 Application

- (1) This code applies to a franchise agreement entered into on or after 1 October 1998.
- (2) For the parties to a franchise agreement entered into before 1 October 1998:
 - (a) clauses 14 (Copy of lease), 15 (Association of franchisees) and 17 (Marketing and other cooperative funds) apply to the parties on and after 1 July 1998; and
 - (b) the rest of this code applies to the parties on and after 1 October 1998.
- (3) However, this code does not apply to a franchise agreement:
 - (a) to which another mandatory industry code, prescribed under section 51AE of the Act, applies; or
 - (b) if:
 - (i) the franchise agreement is for goods or services that are substantially the same as those supplied by the

- franchisee before entering into the franchise agreement; and
- (ii) the franchisee has supplied those goods or services for at least 2 years immediately before entering into the franchise agreement; and
 - (iii) sales under the franchise are likely to provide no more than 20% of the franchisee's gross turnover for goods or services of that kind for the first year of the franchise.
- (4) Paragraph (3) (b) ceases to apply to a franchise agreement if:
- (a) sales under the franchise provide more than 20% of the franchisee's gross turnover for the goods or services for 3 consecutive years; and
 - (b) the franchisee tells the franchisor that paragraph (a) applies.

Part 2 Disclosure

Division 2.1 Disclosure document

6 Franchisor must maintain a disclosure document

- (1) A franchisor must, before entering into a franchise agreement, and within 4 months after the end of each financial year after entering into a franchise agreement, create a document (a *disclosure document*) for the franchise in accordance with this Division.
- (2) A disclosure document:
 - (a) must be:
 - (i) if the franchised business has an expected annual turnover at any time during the term of the franchise agreement of \$50 000 or more — in accordance with Annexure 1; or
 - (ii) if the franchised business has an expected annual turnover of less than \$50 000 — in accordance with Annexure 1 or 2; and

- (b) may include additional information under the heading 'Other relevant disclosure information'; and
- (c) must be signed by a director or other officer of the franchisor.

6A Purpose of disclosure document

The purposes of a disclosure document are:

- (a) to give to a prospective franchisee, or a franchisee proposing to enter into, renew or extend a franchise agreement, information from the franchisor to help the franchisee to make a reasonably informed decision about the franchise; and
- (b) to give a franchisee current information from the franchisor that is material to the running of the franchised business.

6B Requirement to give disclosure document

- (1) A franchisor must give a current disclosure document to:
 - (a) a prospective franchisee; or
 - (b) a franchisee proposing to:
 - (i) renew a franchise agreement; or
 - (ii) extend the scope or term of a franchise agreement.
- (2) If a subfranchisor proposes to grant a subfranchise to a prospective subfranchisee:
 - (a) the franchisor and subfranchisor must:
 - (i) give separate disclosure documents, in relation to the master franchise and the subfranchise respectively, to the prospective subfranchisee; or
 - (ii) give to the prospective subfranchisee a joint disclosure document that addresses the respective obligations of the franchisor and the subfranchisor; and
 - (b) the subfranchisor must comply with the requirements imposed on a franchisor by this Part.

Note A subfranchisor is also sometimes referred to as a master franchisee: see subclause 3 (1).

6C Additional information

If a franchisee or prospective franchisee who is given a disclosure document in accordance with Annexure 2 asks the franchisor for the information referred to in sections 3, 5, 6, 9, 10, 11, 14, 17, 18, 19, 21 and 22 of Annexure 1, the franchisor must give that information.

7 Layout

- (1) Information in a disclosure document must be set out:
 - (a) in the form and the order, and under the numbering, set out in Annexure 1 or 2 as the case requires (the *relevant Annexure*); and
 - (b) under the titles used in the relevant Annexure.
- (2) A disclosure document must have a table of contents based on the items in the relevant Annexure, indicating the page number on which each item begins.

Division 2.2 Before franchise agreement

8 Application

This Division applies to a disclosure document in accordance with Annexure 1 or 2 for:

- (a) a prospective franchisee; or
- (b) a franchisee proposing to enter into, renew or extend a franchise agreement.

10 Franchisor obligations

A franchisor must give:

- (a) a copy of this code; and
- (b) a disclosure document; and
- (c) a copy of the franchise agreement, in the form in which it is to be executed;

to:

- (d) a prospective franchisee at least 14 days before the prospective franchisee:

- (i) enters into a franchise agreement or an agreement to enter into a franchise agreement; or
- (ii) makes a non-refundable payment (whether of money or of other valuable consideration) to the franchisor or an associate of the franchisor in connection with the proposed franchise agreement; or
- (e) a franchisee at least 14 days before renewal or extension of the franchise agreement.

Note Subsection 9 (1) of the *Electronic Transactions Act 1999* provides that a requirement under a law of the Commonwealth to give information in writing is satisfied by giving the information electronically if it is reasonable to expect that the information will be readily accessible so as to be useable for subsequent reference, and the person to whom the information is given consents to it being provided electronically.

11 Advice before entering into franchise agreement

- (1) The franchisor must not:
 - (a) enter into, renew or extend a franchise agreement; or
 - (b) enter into an agreement to enter into, renew or extend a franchise agreement; or
 - (c) receive a non-refundable payment (whether of money or of other valuable consideration) under a franchise agreement or an agreement to enter into a franchise agreement;unless the franchisor has received from the franchisee or prospective franchisee a written statement that the franchisee or prospective franchisee has received, read and had a reasonable opportunity to understand the disclosure document and this code.
- (2) Before a franchise agreement is entered into, the franchisor must have received from the prospective franchisee:
 - (a) signed statements, that the prospective franchisee has been given advice about the proposed franchise agreement or franchised business, by any of:
 - (i) an independent legal adviser;
 - (ii) an independent business adviser;
 - (iii) an independent accountant; or

- (b) for each kind of statement not received under paragraph (a), a signed statement by the prospective franchisee that the prospective franchisee:
 - (i) has been given that kind of advice about the proposed franchise agreement or franchised business; or
 - (ii) has been told that that kind of advice should be sought but has decided not to seek it.
- (3) Subclause (2):
 - (a) does not apply to the renewal or extension of a franchise agreement with a franchisor; and
 - (b) does not prevent the franchisor from requiring any or all of the statements mentioned in paragraph (2) (a).

Part 3 Conditions of franchise agreement

13 Cooling off period

- (1) A franchisee may terminate an agreement (being either a franchise agreement or an agreement to enter into a franchise agreement) within 7 days after the earlier of:
 - (a) entering into the agreement; or
 - (b) making any payment (whether of money or of other valuable consideration) under the agreement.
- (2) Subclause (1) does not apply to the renewal, extension or transfer of an existing franchise agreement.
- (3) If the franchisee terminates an agreement under subclause (1), the franchisor must, within 14 days, return all payments (whether of money or of other valuable consideration) made by the franchisee to the franchisor under the agreement.
- (4) However, the franchisor may deduct from the amount paid under subclause (3) the franchisor's reasonable expenses if the expenses or their method of calculation have been set out in the agreement.

14 Copy of lease

- (1) If a franchisee leases premises from the franchisor or an associate of the franchisor for the purposes of a franchised business, the franchisor or the associate from which the premises are leased must give to the franchisee 1 of the documents mentioned in subclause (2) within 1 month after the lease or agreement to lease is signed by the parties.
- (2) For subclause (1), the documents are:
 - (a) a copy of the agreement to lease;
 - (b) a copy of the lease.
- (3) If the franchisee occupies, without a lease, premises leased by the franchisor or an associate of the franchisor, the franchisor or the associate who leases the premises must give to the franchisee 1 of the documents mentioned in subclause (4) within 1 month after:
 - (a) the occupation commences; or
 - (b) for the documents mentioned in paragraph (4) (b) — the documents are signed by the parties.
- (4) For subclause (3), the documents are:
 - (a) a copy of the franchisor's or associate's lease or agreement to lease;
 - (b) a copy of the documents that give the franchisee rights to occupy the premises;
 - (c) written details of the conditions of occupation.

15 Association of franchisees or prospective franchisees

A franchisor must not induce a franchisee or prospective franchisee:

- (a) not to form an association; or
- (b) not to associate with other franchisees or prospective franchisees for a lawful purpose.

16 Prohibition on release from liability etc

- (1) A franchise agreement entered into on or after 1 October 1998 must not contain, or require a franchisee to sign:
 - (a) a general release of the franchisor from liability towards the franchisee; or
 - (b) a waiver of any verbal or written representation made by the franchisor.
- (2) However, paragraph (1) (a) does not prevent a franchisee from settling a claim against the franchisor after entering into a franchise agreement.

17 Marketing and other cooperative funds

- (1) If a franchise agreement provides that a franchisee must pay money to a marketing or other cooperative fund, the franchisor must:
 - (a) within 4 months after the end of the last financial year, prepare an annual financial statement detailing all of the fund's receipts and expenses for the last financial year; and
 - (b) have the statement audited by a registered company auditor within 4 months after the end of the financial year to which it relates; and
 - (c) give to the franchisee:
 - (i) a copy of the statement, within 30 days of preparing the statement; and
 - (ii) a copy of the auditor's report, if such a report is required, within 30 days of preparing the report.
- (2) A franchisor does not have to comply with paragraph (1) (b) for a financial year if:
 - (a) 75% of the franchisor's franchisees in Australia, who contribute to the fund, have voted to agree that the franchisor does not have to comply with the paragraph; and
 - (b) either:

- (i) that agreement is made within 5 months after the end of the financial year (the *financial year for which agreement is reached*); or
 - (ii) the financial year falls within the period of 2 years after the financial year for which agreement is reached.
- (3) A franchisor is taken to have complied with paragraph 12.1 (h) of Annexure 1 if, to the extent to which the franchisor is aware of the details, the franchisor supplies the following information for the period before 1 July 1998 to the franchisee:
 - (a) the amounts of expenditure on production, advertising, administration and any other category of expenditure stated in the disclosure document for each marketing or other cooperative fund controlled or administered by or for the franchisor to which the franchisee may be required to contribute;
 - (b) the percentage that each amount disclosed in accordance with paragraph (a) constitutes of the total expenditure disclosed in accordance with that paragraph.
- (4) If a franchise agreement provides that a franchisee must pay money to a marketing or other cooperative fund, the reasonable costs of administering and auditing the fund must be paid from the fund.

18 Disclosure of materially relevant facts

- (1) If a disclosure document does not mention a matter mentioned in subclause (2), the franchisor must tell a franchisee or prospective franchisee about the matter, in writing, within a reasonable time (but not more than 14 days) after the franchisor becomes aware of it.
- (2) For subclause (1), the matters are the following:
 - (a) change in majority ownership or control of the franchisor;
 - (b) proceedings by a public agency, a judgment in criminal or civil proceedings or an award in an arbitration against the franchisor or a franchisor director in Australia alleging:

- (i) breach of a franchise agreement; or
 - (ii) contravention of trade practices law; or
 - (iii) contravention of the *Corporations Act 2001*; or
 - (iv) unconscionable conduct; or
 - (v) misconduct; or
 - (vi) an offence of dishonesty;
 - (c) a judgment against the franchisor, other than for unfair dismissal of an employee, under:
 - (i) section 127A or 127B of the *Workplace Relations Act 1996*; or
 - (ii) section 106 of the *Industrial Relations Act 1996* of New South Wales; or
 - (iii) section 276 of the *Industrial Relations Act 1999* of Queensland;
 - (d) civil proceedings in Australia against the franchisor or a franchisor director by at least 10%, or 10, of the franchisees in Australia of the franchisor (whichever is the lower);
 - (e) any judgment that is entered against the franchisor in Australia, and is not discharged within 28 days, for at least:
 - (i) for a small proprietary company — \$100,000; or
 - (ii) for any other company — \$1,000,000;
 - (f) any judgment that is entered against the franchisor in a matter mentioned in item 4.2 of Annexure 1 or item 3.2 of Annexure 2;
 - (g) the franchisor becoming an externally-administered body corporate;
 - (h) a change in the intellectual property, or ownership or control of the intellectual property, that is material to the franchise system;
 - (i) the existence and content of any undertaking or order under section 87B of the Act.
- (3) For paragraphs (2) (b), (c), (d), (e) and (f), the franchisor must tell the franchisee:

- (a) the names of the parties to the proceedings; and
 - (b) the name of the court or tribunal; and
 - (c) the case number; and
 - (d) the general nature of the proceedings.
- (4) For paragraph (2) (g), the franchisor must tell the franchisee the name and address of the administrator, controller or liquidator.
- (5) For paragraph 18 (2) (i), this information must be disclosed within a reasonable time (but not more than 14 days) after the undertaking or order is given.

Note Nothing in this code affects the operation of Part VIIC of the *Crimes Act 1914* (which includes provisions that, in certain circumstances, relieve persons from the requirement to disclose spent convictions and require persons aware of such convictions to disregard them).

19 Current disclosure document

- (1) A franchisor must give to a franchisee a current disclosure document within 14 days after a written request by the franchisee.
- (2) However, a request under subclause (1) can be made only once in 12 months.

20 Transfer of the franchise

- (1) A request for a franchisor's consent to transfer of a franchise must be made in writing.
- (2) A franchisor must not unreasonably withhold consent to the transfer.
- (3) For subclause (2), circumstances in which it is reasonable for a franchisor to withhold consent include:
 - (a) the proposed transferee is unlikely to be able to meet the financial obligations that the proposed transferee would have under the franchise agreement; or
 - (b) the proposed transferee does not meet a reasonable requirement of the franchise agreement for the transfer of a franchise; or

- (c) the proposed transferee has not met the selection criteria of the franchisor; or
 - (d) agreement to the transfer will have a significantly adverse effect on the franchise system; or
 - (f) the proposed transferee does not agree in writing to comply with the obligations of the franchisee under the franchise agreement; or
 - (g) the franchisee has not paid or made reasonable provision to pay an amount owing to the franchisor; or
 - (h) the franchisee has breached the franchise agreement and has not remedied the breach.
- (4) The franchisor is taken to have given consent to the transfer if the franchisor does not, within 42 days after the request was made, give to the franchisee written notice:
- (a) that consent is withheld; and
 - (b) setting out why consent is withheld.

21 Termination — breach by franchisee

- (1) This clause applies if:
- (a) a franchisee breaches a franchise agreement; and
 - (b) the franchisor proposes to terminate the franchise agreement; and
 - (c) clause 23 does not apply.
- (2) The franchisor must:
- (a) give to the franchisee reasonable notice that the franchisor proposes to terminate the franchise agreement because of the breach; and
 - (b) tell the franchisee what the franchisor requires to be done to remedy the breach; and
 - (c) allow the franchisee a reasonable time to remedy the breach.
- (3) For paragraph (2) (c), the franchisor does not have to allow more than 30 days.

- (4) If the breach is remedied in accordance with paragraphs (2) (b) and (c), the franchisor cannot terminate the franchise agreement because of that breach.
- (5) Part 4 (resolving disputes) applies in relation to a dispute arising from termination under this clause.

22 Termination — no breach by franchisee

- (1) This clause applies if:
 - (a) a franchisor terminates a franchise agreement:
 - (i) in accordance with the agreement; and
 - (ii) before it expires; and
 - (iii) without the consent of the franchisee; and
 - (b) the franchisee has not breached the agreement; and
 - (c) clause 23 does not apply.
- (2) For subparagraph (1) (a) (iii), a condition of a franchise agreement that a franchisor can terminate the franchise agreement without the consent of the franchisee is not taken to be consent.
- (3) Before terminating the franchise agreement, the franchisor must give reasonable written notice of the proposed termination, and reasons for it, to the franchisee.
- (4) Part 4 (resolving disputes) applies in relation to a dispute arising from termination under this clause.

23 Termination — special circumstances

A franchisor does not have to comply with clause 21 or 22 if the franchisee:

- (a) no longer holds a licence that the franchisee must hold to carry on the franchised business; or
- (b) becomes bankrupt, insolvent under administration or an externally-administered body corporate; or
- (c) voluntarily abandons the franchised business or the franchise relationship; or
- (d) is convicted of a serious offence; or

- (e) operates the franchised business in a way that endangers public health or safety; or
- (f) is fraudulent in connection with operation of the franchised business; or
- (g) agrees to termination of the franchise agreement.

Part 4 Resolving disputes

24 Definitions

In this Part:

complainant means the person who starts the procedure under clause 29.

parties means the complainant and the respondent in a dispute arising under a franchise agreement or this code.

respondent means the person with whom the complainant has a dispute.

25 Mediation adviser

A mediation adviser is to be appointed for this Part by the Minister.

26 Internal complaint handling procedure

A franchise agreement entered into on or after 1 October 1998 must provide for a complaint handling procedure that complies with clauses 29 and 30.

27 Code complaint handling procedure

A party to a franchise agreement who has a dispute with another party to the franchise agreement may start the procedure under clause 29.

28 Choice of procedure

A party to a franchise agreement who has a dispute with another party to the franchise agreement may, at any time, choose to use the procedure under clause 26 or 27.

29 Procedure

- (1) The complainant must tell the respondent in writing:
 - (a) the nature of the dispute; and
 - (b) what outcome the complainant wants; and
 - (c) what action the complainant thinks will settle the dispute.
- (2) The parties should then try to agree about how to resolve the dispute.
- (3) For mediation under a franchise agreement:
 - (a) if the parties cannot agree under subclause (2) within 3 weeks, either party may refer the matter to a mediator; and
 - (b) if the parties cannot agree about who should be the mediator, either party may ask the mediation adviser to appoint a mediator.
- (4) For mediation under this code, either party may ask the mediation adviser to appoint a mediator.
- (5) Subject to subclause (5A), the mediator may decide the time and place for mediation.
- (5A) Mediation under this code must be conducted in Australia.
- (6) The parties must attend the mediation and try to resolve the dispute.
- (7) For subclause (6), a party is taken to attend mediation if the party is represented at the mediation by a person who has the authority to enter an agreement to settle the dispute on behalf of the party.

30 Mediation under the code

- (1) The mediation adviser must, within 14 days after referral under paragraph 29 (3) (b) or subclause 29 (4), appoint a mediator for the dispute.
- (2) After mediation under this code has started, the mediator must tell the mediation adviser, within 28 days, that mediation has started.

30A Termination of mediation

- (1) This clause applies if:
 - (a) at least 30 days have elapsed after the start of mediation of a dispute; and
 - (b) the dispute has not been resolved.
- (2) If either party asks the mediator to terminate the mediation, the mediator must do so.
- (3) Subject to subclause (2), the mediator may terminate the mediation at any time unless satisfied that a resolution of the dispute is imminent.
- (4) If the mediator terminates the mediation of a dispute under this clause, the mediator must issue a certificate stating:
 - (a) the names of the parties; and
 - (b) the nature of the dispute; and
 - (c) that the mediation has finished; and
 - (d) that the dispute has not been resolved.
- (5) The mediator must give a copy of the certificate to:
 - (a) the mediation adviser; and
 - (b) each of the parties to the dispute.

31 Conditions

- (1) This Part does not affect the right of a party to a franchise agreement to take legal proceedings under the franchise agreement.
- (2) The parties are equally liable for the costs of mediation under this Part unless they agree otherwise.
- (3) The parties must pay for their own costs of attending the mediation.