

The background of the entire cover is a marbled pattern of red and blue. The red is a vibrant, slightly dark red, and the blue is a deep, navy blue. The pattern is organic and textured, resembling stone or liquid marbling.

AUSTRALIAN FRANCHISING CODE OF CONDUCT

A CRITICAL ANALYSIS
WITH CURRENT
CASE LAW

**PETER
BUBERIS**

Australian Franchising Code of Conduct

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Australian Franchising Code of Conduct: A Critical Analysis with Current Case Law

PETER BUBERIS

KHQ Lawyers, Australia



United Kingdom – North America – Japan – India – Malaysia – China

Emerald Publishing Limited
Howard House, Wagon Lane, Bingley BD16 1WA, UK

First edition 2020

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British Library Cataloguing in Publication Data

A catalogue record for this book is available from the British Library

ISBN: 978-1-83909-168-1 (Print)

ISBN: 978-1-83909-167-4 (Online)

ISBN: 978-1-83909-169-8 (Epub)



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Introduction

Overview

The Australian Franchising Code of Conduct 2014 (the Code) is recognised as one of the more comprehensive attempts to regulate the franchising industry within a nation's boundaries.

It bundles together the critical legal parameters of disclosure, relationship behaviour and disputation, supplementing them with key stakeholder rights such as 'cooling off', duties to act in good faith and mandatory mediation. These issues are often separated in other international jurisdictions and in many instances not adequately addressed, if at all.

The fact that the Code is prescriptive in seeking a more balanced relationship between the participants, with civil penalties to encourage good behaviour, has earned it the reputation of being one of the more challenging relevant laws with which franchise systems need to comply.

Since the inception of a suite of franchise regulatory measures in 1998 there has been ongoing commentary on whether the franchise industry has been sufficiently responsible in ensuring that franchisees receive adequate information before deciding whether to become part of a system. And, once they have done so, whether the franchisors they interact with continue to behave appropriately.

This has played out in media reports and investigations, in complaints to the Regulator and through the establishment of formal inquiries preceding Parliamentary consideration. The 1998 Code was reviewed and recast on a number of occasions before its replacement by the 2014 Code, operative from 1 January 2015.

Even given improvements to the governing laws and increases in possible penalties through the latest Code, instances of poor franchisor behaviour continue to be reported and franchisors are regularly the subject of prosecution by the regulator or adverse commentary by the courts.

A formal Parliamentary review was instituted in 2018 and this inquiry produced preliminary recommendations that are under consideration. These are set out in Chapter 1. No timeline for final recommendations has been published.

Notwithstanding the prospects of additional Code amendment, the importance of the Code as a regulatory mechanism justifies an updated and considered commentary on the present law and relevant judicial commentary.

I have tried to follow a logical path but have been obliged to raise observations where I believe ambiguities exist. There are still matters of interpretation that appear unresolved and there is room for improvements that should enhance the working of the Code.

To the extent that my commentary is open to different analyses I would welcome the opinions of others in the hope that a later edition may add clarity to my efforts.

Acknowledgements

I take the opportunity of expressing my thanks as follows:

To Professor Jenny Buchan of the University of New South Wales for promoting the need for this book and initiating preliminary research.

To my legal partner, solicitor Iain Irvine for considering and contributing some of the ideas incorporated in the text.

To my wife Jenny for keeping me focussed when distractions were on offer.

Finally, to my legal assistant Tina Tran, for helping with formatting and excellent legal research. She will become a fine lawyer.

Purpose of the Text

There are threads running through the Code that do not easily connect, even when dealing with the same subject matter.

The concept of appropriate disclosure and its delivery takes up the bulk of the Code and is not, in the Code format, neatly packaged for a one-time period or within one part. It is an ongoing concern needing consideration within different phases of the franchise relationship.

Certainly, pre-contractual disclosure is neatly addressed in the Code. But, adequate disclosure at one point may not satisfy the discharge of the obligation to the execution point. Events, not calling for comment as part of regular first step disclosure, may arise which need communication. This view has real practical implications which are overlaid by the pervasive obligation to act in good faith applying from commencement of the pre-execution process.

Periodic and material event disclosure also occupy a prominent place in the Code. But, on closer analysis, there are nuances in discharging the obligations associated with them. These obligations relate, not only to annual updates, but to the events of renewal, extension and change in scope of agreements. There are also subtleties in determining whether a fact or event falls into the category of a disclosure item.

The text attempts to draw these scenarios into clearer focus with issues of unresolved importance identified for possible further consideration.

Disclosure is not the only objective of the Code. It devotes appropriate consideration to relationship issues between the parties, temporal circumstances such as consideration of the proposal, cooling off, notices to rectify, renewal frameworks, dispute resolution and end of term arrangements. These also

intersect with disclosure and create another level of complexity with interpretation and discharge issues that could benefit from additional clarity.

Good faith is now a statutorily imposed obligation but its exercise needs defined parameters. Whether reasonableness has a role to play in its application is a significant consideration.

I have attempted to wade into the complexities of these relationships and issues in the hope that other practitioners may benefit but, also with a view to improving the communication of ideas which may result in better jurisprudence.

The most up-to-date decisions of the courts have been incorporated. Not all are dealt with in detail, but the application of them, when relevant, should prove useful. These have resolved some debates but also serve to raise further meaningful questions.

Methodology

While the regulatory environment may result in ongoing changes to the Code, it is unlikely to alter the ‘pillars’ around which it is constructed and described in the Introduction.

For that reason, the approach I have taken does follow a simple path giving the reader an introduction to the Code as a whole, a long period of reflection on the important and slightly dominant issue of ‘disclosure’ then a focus on more limited issues.

Among the latter is ‘good faith’ given its legislative adoption rather than continuing its status as a discretionary finding open to a court under the common law. It is now pervasive throughout the life of the franchise relationship and has assumed the position of a bedrock principle as evident from judicial interpretation in the last few years as well as it assuming a place as part of the stock armoury of the Regulator in enforcement actions.

Intellectual Property merits its own chapter. It is not easily referenced in the Code. There are few direct inclusions to it there or in the prescribed disclosure document; however, it is fundamental to defining what a franchise is and enabling the successful commercialisation of a franchise system. So much is made of its importance within the industry and amongst commentators that it would be remiss of any practitioner not to have an understanding of the basic principles associated with it.

The last chapter concerns the business issues of sale and termination of a franchised business. These are where the commercial interests of both parties come into hard focus and where self-interest is most evident.

The chapter format consistently begins with the specific terms of the Code and relevant legislative history. This is not, though, an effective approach for Chapter 2 on disclosure matters as the significant number of relevant clauses necessitate their being attached as an addendum.

In some cases, Code clauses are set out in a discreet reference within a sub-chapter. This has been done for the convenience of the reader. There are circumstances where cross-referencing with other clauses will be necessary but this is unavoidable given the interweaving of concepts across the Code.

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The legislative history of the Code and its earlier iterations sits within Section 2.2 in tracing the desire of Parliament to provide appropriate disclosure it provides of the rationale for other inclusions and changes. Proposals for further change resulting from the 2018 Parliamentary Inquiry are set out in summary form in Section 1.2.

Finally, the reader will observe that my own views and observations on issues relevant to the Code are interspersed throughout the text. I hope they will stimulate thought, debate and even where appropriate, rebuttal.

Chapter 1

The Franchising Code of Conduct 2014 (the Code)

<https://www.legislation.gov.au/Details/F2017C00182>

1.1 Introduction

The framework of the Code is made up of six sections with four substantive parts and two supplementary annexures.

The sections provide framework as to the legislative source of power as well as transitional provisions comprising:

1 Name

This is the Competition and Consumer (Industry Codes – Franchising) Regulation 2014.

2 Commencement 1 January 2015 (omitted)

3 Authority

This instrument is made under section 51AE of the Competition and Consumer Act 2010.

4 Code of conduct

For section 51AE of the Competition and Consumer Act 2010, the code set out in Schedule 1:

- (a) is prescribed; and*
- (b) is a mandatory industry code.*

5 Transitional – clause 8

(1) Subclause 8(1) of the new code does not apply if a franchisor has an existing disclosure document.

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(2) *If a franchisor has an existing disclosure document:*

- (a) *the existing disclosure document may be given under the new code before 1 November 2015; and*
- (b) *the franchisor must update the existing disclosure document so that it complies with subclauses 8(3), (4) and (5) of the new code by 31 October 2015; and*
- (c) *the requirements of subclause 8(6) of the new code apply to a financial year that begins on or after 1 January 2015.*

(3) *In this section:*

existing disclosure document *means a franchisor's disclosure document (within the meaning of the old code) that exists on 1 January 2015.*

new code *means the Franchising Code of Conduct set out in Schedule 1 to this instrument.*

old code *means the Franchising Code of Conduct set out in the Schedule to the Trade Practices (Industry Codes – Franchising) Regulations 1998 as in force immediately before 1 January 2015.*

6 Transitional – continued appointment of mediation adviser

The appointment of a mediation adviser for the purposes of Part 4 of the Franchising Code of Conduct set out in the Schedule to the Trade Practices (Industry Codes – Franchising) Regulations 1998 that is in force immediately before 1 January 2015, has effect, despite the repeal of those regulations, as if it were an appointment of a mediation adviser for the purposes of Part 4 of the Franchising Code of Conduct set out in Schedule 1 to this regulation.'

The sections are followed by the substantive parts:

- Part 1: Introduction;
- Part 2: Disclosure requirements before entry into a franchise agreement;
- Part 3: Franchise agreements;
- Part 4 Resolving disputes.

The Annexures then attach;

- Annexure 1: Disclosure document for franchisee or prospective franchisee; and
- Annexure 2: Information statement for prospective franchisee.

The format of the Code is the framework for the core issues identified as likely to assist in achieving the objective of the Code described in clause 2;

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

This purpose is promoted through:

- the provision of appropriate information by the franchisor to a franchisee, or prospective franchisee, to enable it to make an informed decision about the franchise opportunity;
- giving the opportunity to the prospective franchisee to seek appropriate advice within timeframes that are reasonable;
- providing temporal withdrawal rights before and after (cooling off) execution of a franchise agreement;
- regulating behaviour before and during the term of an agreement, and during any dispute period, through imposing a statutory duty of ‘good faith’;
- providing certain controls and guidance to apply to the relationship of the parties;
- mandating a mediation process as a necessary step before litigation or arbitration, but not as a restraint on the right to seek injunctive relief.

Of these, the most intensively dealt with is the provision of relevant information through the disclosure process, that is, the information provision requirements. For that reason, Chapter 2 provides a standalone analysis of this core issue.

Good faith is also discussed in a separate Chapter 3. It is a concept integrally bound up with ongoing analysis by the courts under the common law. Its inclusion in the Code removes any uncertainty as to its application to the franchise relationship. The Code introduces an expansion of the core principles of the Common Law through the duty being imposed in the pre-contract stage.

1.2 Code Review Proposals

The reader is invited to consider Sections 2.2 and 2.3 which provide a chronological outline of the genesis of the Code and the review processes and amendments that have occurred since its introduction in 1998.

Parliamentary Inquiry

On 14 March 2019, the Parliamentary Joint Committee on Corporations and Financial Services released its report¹ of the inquiry into the operation and effectiveness of the Franchise Code and the Oil Code of Conduct. The Report, entitled ‘Fairness in Franchising’ includes 71 recommendations.

The Report summarises its key findings and recommendations under the following headings:

- Franchising Taskforce – Following the release of the Report and in accordance with its first recommendation an inter-agency Franchising Taskforce has been

¹Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Fairness in Franchising* (2019) https://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/Franchising/Report.

established to examine the feasibility and implementation of a number of the other recommendations in the Report. It follows that many of the recommendations in the Report are not clear recommendations for change but rather recommendations that the Taskforce further examine the issues and potential reforms.

- Industry associations – The Report comments that the Franchise Council of Australia does not provide a balanced representation of franchisor and franchisee views. Government should remain aware of the risk of franchisors *capturing the policy and regulatory debate*. Franchisees are urged to form a national association.
- Disclosure and registration – Improved disclosure of financial information and marketing fund expenditure was recommended. Registration was a matter deferred to the Franchising Taskforce to consider further.
- Transparency and accountability on third line forcing and supplier rebates – Further disclosure in relation to supplier rebates was recommended.
- Whistleblower protections – The Report recommended whistleblower protections apply to franchisees reporting franchisor breaches of the Franchise Code.
- Unfair contract terms laws – It was recommended the Franchising Taskforce consider introduction of civil penalties for including unfair contract terms in franchise agreements. Cooling off period – The cooling off period should be extended to 14 days and also apply to transfers, renewals and extensions. Further, if premises are leased and the lease is not provided until after the franchise agreement is entered into, the cooling off period should not commence until a copy of the lease is provided to the franchisee.
- Fair exit rights and goodwill – The Report recommends amendment to the Franchise Code's termination provisions including by providing further notice periods and giving franchisees termination rights in special circumstances. The Franchising Taskforce is to consider changes which would recognise franchisee goodwill.
- Collective action – The Report recommends introduction of a class exemption to anticompetitive conduct laws to make it lawful for franchisees to collectively bargain with their franchisor.
- Dispute resolution and arbitration – It is recommended that the option of binding arbitration be added to the dispute resolution procedures under the Franchising Code. This would not exclude court action.
- Enhancement and alignment of Industry codes – The Franchising Taskforce is invited to consider introducing further and increased penalties for breaches of the Franchise Code. Further, consideration should be given to introducing useful provisions from other industry codes.
- No churning and burning – The Report recommends the Australian Competition and Consumer Commission (ACCC) be permitted to intervene and prevent marketing and sale of franchises by franchisors with a track record of churning (repeated sale of a single franchise unit) and burning (opening sites which are unlikely to be viable) with a view to profiting from up-front franchise fees.