

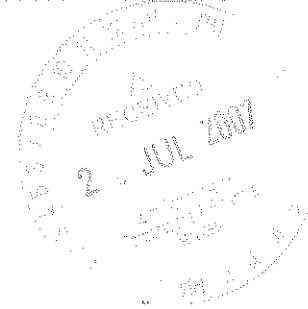


Government of Western Australia

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Minister for Corrective Services; Small Business

Our Ref: 09425



Secretary  
Parliamentary Joint Committee on Corporations and Financial Services  
Department of the Senate  
PO Box 6100  
Parliament House  
CANBERRA ACT 2600

Dear Committee Secretary

**SUBMISSION TO THE INQUIRY INTO THE FRANCHISING CODE OF CONDUCT**

Thank you for the opportunity to provide a submission to the Federal Parliamentary Joint Committee on Corporations and Financial Services (the Committee) Inquiry into the Franchising Code of Conduct and related matters (the Inquiry).

Franchising provides a unique opportunity for individuals to establish and run their own business providing important products and services to the consumer under a recognised brand. This is the case when the franchise system and the relationship between the franchisor and the franchisee are sound and mutually beneficial. The franchising sector has recently been plagued ongoing and increasingly bitter disputations, franchise business failings, high profile litigation, and significant negative press.

Given this situation, and the fact that there is an inherent imbalance in power between the franchisor and franchisee, concerns were raised with the Government of Western Australia late last year regarding fairness in franchising operations. In response, the Western Australian Government initiated an Independent Inquiry into the Operation of Franchise Businesses in Western Australia (the WA Inquiry) to examine issues in the sector and to recommend measures to enhance the franchising business environment.

The terms of reference for the WA Inquiry were to:

1. Review the adequacy of existing legislative provisions, both State and Federal;
2. Identify whether emerging trends in the franchising industry disclose patterns of unconscionable conduct that may not be covered under existing laws;
3. Examine whether existing remedies available to franchisees are adequate and, where appropriate, recommend changes; and
4. Review existing practice in other jurisdictions, Australia and internationally, on unconscionable conduct and renewal of licences.

The WA Inquiry was chaired by Mr Chris Bothams. Mr Bothams has been an accomplished and respected franchisee who had twice been awarded the Western Australian Franchisee of the Year, as well as the National Franchisee of the Year in 2002. The Western Australian Government's specialised small business agency – the Small Business Development Corporation – provided secretariat support to the WA Inquiry.

A Background Paper to the WA Inquiry was released in December 2007 and public submissions were called for. Additionally, public hearings were held in Perth and Bunbury (in the South West of Western Australia) during February 2008. In total, 93 written and eight oral submissions from interested stakeholders from around Australia were made to the WA Inquiry.

The WA Inquiry heard from franchisors, franchisees and ex-franchisees, franchise service providers and academics from around Australia. Numerous submissions made allegations of improper franchisor conduct, including that of franchise churn, and many included accounts of personal loss and financial hardship. It is important to note, however, that the WA Inquiry was not an investigation and was therefore unable to determine whether such allegations were systemic within franchise systems.

In addition, the WA Inquiry engaged the Centre for Advanced Consumer Research at the University of Western Australia to research and advise on the fourth term of reference. This was undertaken to examine whether legal precedents in existence elsewhere could address issues to do with unconscionable conduct and end of agreement arrangements in franchising in Australia. The research examined common law and, where applicable, statute addressing unconscionable conduct and franchise agreement renewal in Australia, the United States, common law nations (the United Kingdom, New Zealand and Canada), the European Union, and Asia.

The final report of the WA Inquiry was publicly released on 28 April 2008. The report was then tabled in State Parliament on 6 May 2008 and considered by Cabinet on 19 May 2008.

A copy of the final report of the WA Inquiry is attached for your consideration.

### ***Report Findings***

Public submissions to the WA Inquiry raised concerns regarding the franchising sector in relation to franchise education, disclosure and due diligence, end of agreement arrangements, dispute resolution, and enforcement.

The WA Inquiry concluded that, while existing legislative provisions serve the franchising sector adequately, there is scope for improvement to be made to the disclosure provisions of the Franchising Code of Conduct (the Code), its monitoring and enforcement, and its overall understanding, particularly by prospective franchisees. Importantly, the WA Inquiry did not recommend separate State legislation, but rather, regulatory changes to the sector should be undertaken by the Commonwealth Government given that franchising often involves national brands operating across Australia.

Briefly, the findings of the WA Inquiry are as follows:

1. *Franchise Education*: The importance of pre-entry education for franchisees cannot be underestimated. Presently, many prospective franchisees are unaware that education is available nor do they understand how important it is to inform themselves about their rights and responsibilities under a franchise agreement.

This is particularly critical in undertaking relevant due diligence when considering the risks involved in entering a franchise agreement. The report's recommendations in relation to this area seek to address issues relating to lack of awareness and reach of franchise education, as well as the desirability of franchise participants being kept informed on an ongoing basis of relevant developments in the sector.

2. *Disclosure and Due Diligence*: Franchising regulation in Australia is premised on the disclosure of relevant information by franchisors to prospective and renewing franchisees. The Code prescribes what information is required and in what format. Currently, the Code does not require franchisors to specifically disclose what franchisees' entitlements and responsibilities are at the end of an agreement. A number of other concerns regarding the current disclosure provisions were also identified which were not addressed by the recent changes to the Code.

Compliance with the disclosure requirements also needs to be improved. The report's recommendations in relation to this area seek to improve the disclosure of relevant information, particularly in regards to rights at the end of an agreement, and compliance with the Code in order to improve overall transparency in the sector.

3. *End of Agreement Arrangements*: A particular focus of the Inquiry was on issues relating to non-renewal of the franchise agreement and expiry of

the contract. The existing regulatory framework for franchising in Australia does not specifically address end of agreement arrangements. In the interests of making an informed business decision and undertaking appropriate due diligence, prospective and renewing franchisees should have a clear understanding of what their entitlements and responsibilities are, or are not, at contract expiry prior to entering into a franchise agreement. The report's recommendations in relation to this area seek to improve end of agreement disclosure and transparency in contract negotiations in order to provide franchisees with greater clarity and certainty in relation to their rights and responsibilities.

4. *Dispute Resolution*: The Code prescribes a mandatory process of dispute resolution through mediation. Problems associated with mediation include the difficulty in getting parties to attend and resolve their disputes in a timely fashion and the lack of enforcement of mediated outcomes. An earlier and more flexible system of intervention is required. The report's recommendations in relation to this area seek to improve the current mediation process in order to provide a better system to resolve disputes in the franchising sector.
5. *Enforcement*: The conduct of franchising participants is regulated by the Australian Competition and Consumer Commission (the ACCC). It is the role of the ACCC to monitor and enforce compliance with the Code and the TPA. The ACCC currently has a formalised process to investigate breaches of the Code and allegations of misconduct. In many cases, the ACCC has not been able to respond adequately to franchisee complaints in a timely manner. The report's recommendations in relation to this area seek to improve the monitoring of compliance with the Code by franchising participants in order to better enforce conduct and behaviour in the franchising sector.

In total, the WA Inquiry report made 20 recommendations under these five key areas to improve the franchising business environment.

### ***Western Australian Government Response***

As indicated previously, State Cabinet considered the WA Inquiry report at its meeting on 19 May 2008 and agreed to support all recommendations, with the exception of recommendation 1.2 (i.e. that the Commonwealth Government provide funding to State and Territory Governments to cooperatively develop an effective marketing strategy to facilitate the promotion of the information and advisory services available to both franchisees and franchisors). This recommendation was not supported as it was considered that the education of franchising participants is a role for both Commonwealth and State Governments.

Additionally, in the review of international practices relating to unconscionable conduct and renewal of franchise agreements, the WA Inquiry report discussed in detail a proposal for the concept of "good faith" to be introduced

in the performance and enforcement of contracts. The report notes that good faith generally embraces:

- an obligation on the parties to cooperate in achieving their contractual objects;
- compliance with honest standards of conduct; and
- compliance with standards of conduct which are reasonable having regard to the interests of the parties.

According to the report, there is currently no uniform acceptance within Australian jurisdictions of a coherent, separate legal concept of good faith in contract law.

Noting the report's discussion of the concept, as well as the Commonwealth Government's pre-election commitment to support good faith obligations under the Code, Cabinet agreed to request the Commonwealth Government to continue to consider the introduction of a well defined obligation for parties to bargain and negotiate in "good faith" as part of the Code.

### ***Small Business Ministerial Council Response***

On 23 May 2008, I tabled the report of the WA Inquiry at the annual meeting of the Small Business Ministerial Council (SBMC). Small Business Ministers from around Australia, including the Federal Minister for Small Business, the Hon Dr Craig Emerson MP, noted the key issues emerging from the WA Inquiry and the recommended measures to address these concerns. Additionally, the report of the South Australian Parliamentary Inquiry on Franchises was also noted.

The issue of good faith in franchising arrangements was also discussed, and the SBMC agreed to:

*Note that the Australian Government will, consistent with its pre-election commitment, consider the introduction of a well defined obligation for parties to bargain and negotiate in "good faith" as part of the franchising code of conduct.*

### ***Conclusion***

The measures recommended by the WA Inquiry seek to improve the franchising business environment for all participants, particularly for franchisees (who are generally small business operators). The WA Inquiry concluded that the high costs associated with business failure, individually and across a franchise system, would outweigh any additional impost on the franchisor as a result of added compliance obligations.

The recommendations seek to improve franchise education, disclosure and due diligence, end of agreement arrangements, dispute resolution, and enforcement of the franchising sector. If adopted, the franchising business environment will be one where franchising participants are better informed,

are more likely to succeed, enjoy greater equity and, should the need arise, have more timely and efficient access to dispute resolution.

I commend the Committee for undertaking this inquiry into the very important franchising sector of Australia.

Yours sincerely



**Margaret Quirk MLA  
MINISTER FOR SMALL BUSINESS**

18 JUL 2008