

Joint Standing Committee on Corporations and Financial Services

Inquiry into Franchising Code of Conduct

12 September 2008

I thank the Committee for the opportunity to submit to this inquiry. I worked with my husband on a submission to this inquiry and was greatly disappointed when advised that an entire section was to be censored. I would offer a revised version of that section as I believe it is important that the Australian public are informed.

Today I visited the Franchising Expo in Brisbane where a representative from Business.gov.au advised me that I needed to speak to the FCA as they "controlled franchising" and "looked after everyone in franchising" in Australia. This is untrue and it left me wondering how many people are given similar inaccurate information.

FCA represents franchisors. FCA does not represent franchisees or franchising. Anecdotal evidence from many franchisees from many networks and my personal experience confirms that FCA does not entertain complaints from franchisees. FCA plays a vital role in securing business for law firms, brokers, lenders and other providers to franchisors.

*"The other parties who propose that there is not a problem, that nothing needs to be done, the present measures work, are the very same parties who so rigorously and comprehensively opposed Minister Beddall's amendments back in 1992. The same arguments were trotted out, the same thing. Their purpose in all truth is to deflect and defer and hope another 24 years will go past before anything has to happen."**

*Michael Delaney, MTAA, *Transcript of Evidence*, p. 335. Reid Committee 1997

"The Franchise Council of Australia purports to act for franchising eg franchisors and franchisees. This is akin to corporations representing unions."

Howard Bellin, IF International – The Australian Financial Review, 7 July 2008 page 59

The FCA constantly advertises that it is the peak body for franchising representing both franchisors and franchisees. While FCA has cultivated a close relationship with the ACCC this is clearly not accurate where of the suggested 70,000 participants in franchising, FCA represents far less than 1,000.

Stephen Giles is senior partner at Deacons Law Firm and National Chairman at Franchise Council of Australia where he has handled the portfolio of Industry Regulation and Government Relations since 1997. Deacons Lawyers list amongst their clients a number of the franchise networks referred to in this and in both the South and the West Australian inquiries.

Importantly I ask the Committee to bear in mind that the Franchise Council of Australia, and their predecessor FAA, has repeatedly advised governments that there are no endemic problems in franchising. A string of inquiries suggests otherwise. I would ask the Committee to consider the current wave of personal horror stories and submissions to previous inquiries that, like most inquiry participation, represent only the tiniest tip of the iceberg.

Earlier this year the Chairman of the ACCC, Graeme Samuel, admitted that franchisee churning existed in Australia*. On the same day the FCA's Richard Evans continued to deny it was possible *"because it was against the law"*.*

*2UE Radio – Glenn Wheeler Weekend Show - Franchising – 9 February 2008.

FCA member standards do not include any declaration that a serious breach of the Code or law will be referred to the ACCC or an appropriate authority. A member may lose membership but FCA report no such instance.

FCA has maintained that it welcomes industry review while constantly opposing any change at all to existing laws stating there is currently no disadvantage to franchisees. Both state inquiries and expert academic opinion indicate otherwise.

The following rebuttals are to key FCA arguments in its submission;

The Franchising Code of Conduct requires a comprehensive disclosure document prior to a franchisee signing a franchise agreement and the format is simple, detailed and working well within healthy regulation and the potential to be breached should a franchisor stray.

State Inquiries, anecdotal evidence from franchisee victims and submissions to this inquiry offer absolute reason to conclude that disclosure requirements fail miserably.

The recent changes to disclosure requirements will definitely assist in the due diligence process however and as will be outlined there is critical information not supplied regarding franchisor experience, rebates, lease arrangements etc.

Further, since there is effectively no penalty for breach of these requirements and since the ACCC will not pursue it, the only time it would be of relevance is in the unlikely event that a franchisee could fund a private legal action.

The Code requires franchisees to obtain legal, business and accounting advice, or certify they have been told they should do so but have elected not to obtain advice.

Franchisees who elect not to gain advice or who often gain such advice from professionals without franchising experience are in the majority.

Prospective franchisees deal with experienced franchise salespeople and they make foolish and emotional decisions. Many succeed because of the quality of the franchise model; when they fail they damage the reputation and future potential of franchising when they often lose everything.

Various Code requirements govern the operation of marketing funds, prescribing a process for transfer and limiting the grounds for termination**.*

*Marketing funds are reported internationally as an enormous temptation for rogue franchisors. ██████ offers an insight into how misappropriation can occur and be outside of the reach of the regulator.

These are often multi-million dollar funds controlled by an audit requirement that does not authenticate charges to advertising funds. The audit merely verifies the invoice *process*, the cost of various categories and the balance for the fund.

Where the franchisor or a third party associate company to the franchisor can provide exorbitant invoiced charges to the fund and where franchisees can be refused access to detail must be eliminated.

With reference to [REDACTED], the ACCC did suggest to [REDACTED] that "had the Code meant a summary audit they would have said a summary audit", but they then did nothing about it.

**Opportunist franchisors utilise an ability to refuse the sale of a franchise on concocted grounds and neither the Code nor the ACCC have dealt with those occurrences. Refusal has proven to be a useful tool when the franchisor's intent is to win the franchise back for a pittance by ensuring the franchisee will fail while unable to sell.

The rogue's preferred outcome in this instance is the financial collapse of franchisees while avoiding Code grounds for termination to conceal this practice.

The mediation based dispute resolution procedure set out in the Code has been extremely successful, with over 80% of disputes being successfully resolved while the cost of mediation is minimal.

Mediation continues to allow a rogue franchisor the ability to use the process to further drain the finances of a franchisee and where the opportunist franchisor can flaunt that there is no requirement to abide by any agreements made in mediation.

Mediation is only successful where franchisees and legitimate franchisors participate in good faith and where an 80% success rate represents very few that involve rogue franchising and those franchisees that don't bother.

The Trade Practices Act s52, and supplemented by 51A prohibits misleading or deceptive conduct and ensures that a franchisor must be able to prove it had reasonable grounds for making any representation as to a future event.

Under the regulation of the poorly funded ACCC the financially weak victim of opportunism must contest such claims and provide evidence that typically isn't offered in hardcopy by the rogue franchisor.

Within the TPA, s51AC prohibits unconscionable conduct and suggest that a well-resourced regulator – the ACCC – has extensive powers of investigation and prosecution to oversee the industry.

Courts and the ACCC are on record as having great difficulty pursuing unconscionable conduct. State inquiries and anecdotal evidence suggests that the ACCC requires dedicated funding and greater power to effectively investigate and prosecute franchising complaints.

This is typically and deliberately misleading where every review of "unconscionable conduct" definition has confirmed the enormous difficulty associated with pursuing such action.

Any aggrieved franchisee can, at no cost, seek to have the ACCC investigate any matter where there has been an alleged breach of the Code or the Trade Practices Act. The ACCC is well resourced, is duty bound to investigate all claims where there is a breach of the Code or the TPA, and has a strong track record of taking enforcement action where necessary.

Submissions to both state inquiries and to this inquiry detail attempts to have the ACCC effectively deal with complaints. The ACCC's hands are tied because of a lack of funding, a lack of effective law and I suspect a lack of interest. The ACCC record is clearly abysmal with very few franchising complaints resolved, franchisors rarely prosecuted and all within a regulated industry where casualties are enormous.

"Because there are so few major market opportunities in Australia, the likelihood of brand failure there is greater than the American experience. Mistakes can't be buried in the large numbers in Australia like they can be in America. When the IFA [International Franchise Association] is finished with the Australian government, it will have either no franchise regulation or it will have regulation so weak as to be a ridiculous charade."

Richard Solomon – Franchising Attorney Houston, Texas – "Australian Franchise Law: Assurances of Protection or Just More Christians Thrown to the Lions?"- www.bluemaumau.com - 27 Jun 2008.

The majority of franchisees in Australia are in healthy franchises and do not appreciate the need for a national representative body. Franchisees in dispute are usually in financial difficulty and unable to support such a representative association.

I would ask that Government consider funding an independent organization to ensure an effective level of franchisee representation.

Yours faithfully



Cheryl Borradale

12 September 2008