

Kim Rosenwald,

4<sup>th</sup> September 2008

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

Dear Mr Chairman,

I write to you in respect to the current inquiry that is underway into the Franchising Code of Conduct. This is a private submission, and the views / opinions expressed are mine alone. Recently, a significant incident occurred in Western Australia which resulted in a franchisee of KFC, Competitive Foods Australia Pty Ltd (CFAL) being forced to close an outlet in Rockingham, Perth, Western Australia. This closure resulted in the loss of employment for up to 40 employees.

This loss of employment did not occur due to any operational, financial or decision mismanagement of the franchisee, but was the direct consequence of not being protected by legislation within the Franchising Code of Conduct.

It is the intent of this submission to provide to the inquiry the need for regulatory change to the code and the Trade Practices Act, specifically s.51AC. In providing support for the above, it is relevant to incorporate the background of CFAL, the importance of franchising to the Australian economy and necessary change recommendations.

CFAL has operated the franchise for KFC in Western Australia (WA) and Northern Territory (NT) since 1969 and as such is one of the oldest franchisees in Australia. In addition to the KFC franchise, CFAL also operates the Hungry Jacks brand throughout Australia, which makes it also one of the larger Franchisee / Franchisor's in this country. Numerically, this equates to over 300 outlets, employing over 15'000 people.

It is also important to consider the large number of businesses and subsequent employee livelihoods that are directly involved in the supply chain process of this organisation, not to mention those that have an indirect relationship with this company. Should repetition of the above incident continue and the inquiry fails to achieve the necessary outcomes, many livelihoods will be detrimentally affected.

In order to highlight the impact of Franchising on the Australian economy, the following is prudent to this submission. By definition, franchising is a business format model in which the franchisor allows the franchisee the right to use a business name and trademark, operating systems and knowledge to run their

own business. This right comes with certain conditions and stipulations. In return for this, the franchisee is obligated to pay initial start up fees and ongoing fees or royalties whilst using the brand.

Research conducted by the Franchise Advisory Centre (fac) shows that the number of franchisors in Australia has “increased by approximately 58% in 10 years from 693 in 1998 to an estimated number of 1,100 in 2008”. According to the study this represents one franchise system for every 19,454 Australians. In comparison to the USA, which many believe to be the home of this business model, where one franchise system for every 97,666 Americans.

This reflects a system density that is 5 times less than Australia. Franchising can plainly be seen to be an increasingly adopted method of running and owning a business and as such its importance in the Australian economy grows.

Relevant too is the franchising sector’s contribution to GDP, I quote from the transcript of the then prime minister, the honourable John Howard MP, at the Franchise Council of Australia’s 2005 convention “On one estimate the franchise sector now contributes 10 per cent of Australia’s GDP and provides employment to approximately 600,000 Australians”. Figures from the Australian Bureau of Statistics, reflects that GDP in Australia for the financial year, ending June 2005 was AUD \$896,568,000,000.

Although an employee of CFAL, therefore having obvious self interest in the outcome of the inquiry, the nature of the incident that unfolded in Rockingham also has ramifications for, as established, an increasingly growing and important sector of the Australian economy and community.

Further to this, the intent of this submission would also endeavour to prevail upon the inquiry, a broader perspective. The fact that under current legislation, a franchisor can without good cause, enact a decision that causes major disruption in Australians and Australian families livelihood, certainly appears to go against the great Australian ideal of giving and receiving a “fair go”.

**The “fair go” concept is a cliché, but it is a very powerful one. Most of us would be hard-pushed to come up with a clear definition, but it retains enormous symbolic significance because of its association with Australian national identity. The right to a “fair go” is the thing almost all Australians put at the top of their list when it comes to values. A survey released recently shows 91 per cent of people believe a “fair go” is important.**

Indeed, the importance of this concept to Australians is further promoted and used by Australian governments and politicians. In respect to the former, I quote one of the Australian Labor Party (ALP) objectives “ We value fairness and equality and believe in a **fair go** for all—we believe that a nation should be governed in the broader interests of all, not in the sectional interests of a few”.

And for the latter I quote, the Honourable Treasurer, Wayne Swan, then as Opposition Community Services Spokesperson “I sense a deep frustration among ordinary Australians that they are losing the Australian ethos . . . We are at real risk of being “two Australia’s” . . . An Australia that has the very rich and then the rest of us. The Howard government simply doesn’t believe in a **fair go**.”

In application of this principle to the current situation, awareness of the issues and problems facing franchisees in Australia must be addressed. The problem that is of most concern is that which is known as “Franchisor Opportunism”.

“Franchisor Opportunism” is the name given to predatory conduct and bullying tactics by franchisors which depends upon the exploitation of a pre existing power relationship between a franchisor and franchisee, which makes the franchisee vulnerable or an “economic captive” to the demands of the franchisor. This definition, in relationship to the incident involving CFAL resulted in the franchisor, ██████████ Australia, not renewing the franchise agreement for KFC Rockingham.

If permitted, ██████████ Australia has given clear indication that this trend will follow for all outlets operated by CFAL. Closer analysis of this strategy indicates that ██████████ Australia intends to force the franchisee, CFAL, out of business, purely and simply to set up its own business at the same location and thus profit exclusively from the goodwill built up by the CFAL without having to compensate for it. Even with this threat in hand, ██████████ Australia can exploit the CFAL in the acquisition of the CFAL’s business or assets at significantly below market value.

### **The question this submission puts to the inquiry is, is this fair?**

Franchising in Australia has been the subject of many inquiries and committees, the most relevant being the 1976 Swanson Committee, the 1979 Blunt Committee and the 1997 Reid Committee. All three recommending varying degree of changes and clauses to address and protect franchisees from wrongful non-renewal and wrongful termination of franchise agreements and licences. The Reid Committee in particular acknowledged “on-going problems with franchising and recommended protection against “unfair conduct”.

More recent inquiries have been conducted by Australian State Governments, including the Botham Inquiry of Western Australia and the Picolo Inquiry of South Australia. From my understanding, both state inquiries acknowledge the importance of franchising in Australia and recommend “Good Faith” clause inclusions among other things.

Continuing with the concept of a “fair go” and its application to franchising, the inclusion of a “Good Faith” clause in the Trade Practices Act satisfies this submissions intention of incorporating fairness into the Franchising Code of Conduct in Australia.

Specifically, this submission recommends the following outcomes that will ensure fairness;

1. Obligation upon a franchisor to renew a franchise agreement, or fair compensation in lieu of non renewal, unless the franchisor had a good faith reason to justify non-renewal.
2. Appropriate time limits for notification of the franchisor’s decision about renewal/non-renewal prior to expiry of the agreement, together with the provision of reasons to the franchisee in the event of non-renewal.
3. An ability for the franchisee to enforce its right to renewal, or fair compensation in lieu with the onus being placed on the franchisor to justify its “Good Faith” reason for deciding not to renew the agreement.

Precedent for this type of regulatory change can be seen in the USA, where courts and legislators in various US states have taken the view that “because franchisors usually have the upper hand, and in recognition of the typical franchisor’s superior bargaining power, some statutes and case law seek to intervene in the relationship and protect the franchisee by imposing upon franchisors an obligation of good faith, including

a duty not to terminate franchises except for "good cause."(Emerson, Robert W. Publication: American Business Law Journal).

In light of the importance and significance of franchising in Australia and the problem currently encountered by my employer. It is my sincere hope that this submission results in the necessary regulatory changes that not only protect this organisation but also the other existing and future franchisees of this country.

Regards,

Kim Rosenwald