COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

JOINT COMMITTEE ON CORPORATIONS AND FINANCIAL SERVICES

Reference: Franchising Code of Conduct

WEDNESDAY, 5 NOVEMBER 2008

MELBOURNE

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JOINT STATUTORY COMMITTEE

ON CORPORATIONS AND FINANCIAL SERVICES

Wednesday, 5 November 2008

Members: Mr Ripoll *(Chair)*, Senator Coonan *(Deputy Chair)*, Senators Arbib, Boyce, Marshall and Mason and Ms Grierson, Mr Keenan, Ms Owens and Mr Robert

Members in attendance: Senator Mason, Mr Ripoll and Ms Owens

Terms of reference for the inquiry:

To inquire into and report on:

The operation of the Franchising Code of Conduct. The Committee is to identify where justified, improvements to the Code, with particular reference to:

1. the nature of the franchising industry, including the rights of both franchisors and franchisees;
2. whether an obligation for franchisors, franchisees and prospective franchisees to act in good faith should be explicitly incorporated into the Code (having regard to its presence as an element in paragraph 51AC(4)(k) of the *Trade Practices Act 1974*);
3. interaction between the Code and Part IVA and Part V Division 1 of the *Trade Practices Act 1974*, particularly with regard to the obligations in section 51AC of the Act;
4. the operation of the dispute resolution provisions under Part 4 of the Code; and
5. any other related matters.

WITNESSES

Committee met at 9.00 am

CHAIR (Mr Ripoll)—I declare open this public hearing of the Joint Committee on Corporations and Financial Services, part of a series of public hearings that the committee is holding to inform its inquiry into the Franchising Code of Conduct. The committee is to report on the operation of the Franchising Code of Conduct and to identify, where justified, improvements to the code. The focus of this inquiry is on addressing broad structural procedural issues relating to franchising agreements in Australia, rather than the details of individual disputes. The committee is investigating deficiencies in the operation of the Franchising Code of Conduct and related legislation and ways in which they might be improved.

I welcome participants here today. I remind everyone that witnesses giving evidence to the committee are protected by parliamentary privilege. Any act which may disadvantage a witness on account of their evidence is a breach of privilege and may be treated by the parliament as a contempt. It is also a contempt to give false or misleading evidence to a committee. Witnesses should be aware that if in the giving of their evidence they make adverse comment about another individual or organisation, that individual or organisation will be made aware of the comment and given a reasonable opportunity to respond to the committee.

The committee prefers to hear evidence in public, but we may agree to take evidence confidentially. The committee may still publish confidential evidence at a later date, but we would consult the witness concerned before doing this.

[9.01 am]

EVANS, Mr Richard David, Executive Director, Australian Retailers Association

CHAIR—Would you like to make some opening remarks?

Mr Evans—The Australian Retailers Association would like to thank the committee for the opportunity in presenting further to the inquiry. Whilst we believe that the franchise sector is perhaps overstudied by parliaments, we also believe your considerations to be very important, and we wish you well in your deliberations. It is our belief that you will generally find the sector to be working successfully and the recommendations to change the code will be perhaps limited. However, there remains ongoing angst from some on the peripheral of the sector.

It is our view the code does not address certain behaviours within the sector which cannot be codified and which need addressing. We support your deliberations and hope that you will use the collective wisdom of the sector to help in the difficult task in drawing up your recommendations.

To provide you with some background on the basis that you are not aware, prior to my current role as executive director of the Australian Retailers Association, I have had significant experience within the franchise and retail leasing sector, having been a shopping centre manager, a franchisee, a commentator on small business and franchising matters, an author of a franchise book called *The Australian Franchising Handbook*, the former CEO of the industry body in which I initiated the Franchise Academy and introduced a members' standards code and initiated a complaints process. I have served on the World Franchise Council and the Asia Pacific Franchise Confederation, which allowed me to study other methods in other countries. I have also been the chair of the fair trading inquiry in 1996, which led to the Reid report.

I introduced my background to provide support for a number of things that I am about to say, not least of all my observation within the sector. Whilst it is true there are agitators for a change, it is my view that the Australian franchise regime is mostly sound. A closer look at the issues raised by regular agitators indicates that their issues have been previously addressed and changes to the code have been made. Unfortunately the blunt truth for a lot of these folks is that their business decisions may have contributed to their business predicament. Failure happens in the market and we cannot legislate to ensure success in franchising. Having said that, I agree there are some issues that need addressing.

Your hearings have drawn out many of the issues, and I do not want to rediscover those discussions. I would rather draw your attention to five points. The first is consultants to the sector that provide advice, yet have no limitations to their operations, ethically or otherwise. The second issue is pre-entry education for both the franchisee and indeed franchisor, which still exists within the sector. The third issue of goodwill needs defining and greater explanation within the franchise agreement, and perhaps a disclosure document. The fourth issue is the need for an arbiter that sits between the regulator, the ACCC, and the mediation process. The fifth issue is that there need to be clear sanctions for either party for a breach of the code.

On the issue of consultants, both franchisors and franchisees require advice and help to enter the franchise system. With franchisors the consultant becomes a valuable support and their advice can mean the difference between success or otherwise, yet there are no ethical caveats upon those that can advise within the sector. Of course lawyers and some accountants have ethical considerations, but the vast majority of consultants advising the franchise sector are not so limited. Consultants write the franchise agreement and, indeed, the important operations manual. If there is no correlation between both documents then perhaps non-compliance will ultimately happen. The fact that there are many anecdotes of franchise agreements being cut and pasted, no matter the system, is a worry. In other words, advisers can be lazy and just use one written agreement for one system and the same agreement for another, when both systems are very different.

If the franchise agreement is not compliant to the code, then the likelihood of non-compliance arises. I had one potential franchisor advise me about 12 months ago that he had spent $60,000 on the preparation of documents which had proved to be non-compliant, thus a waste of money and he had to start again. Yet there was no structure of redress for that franchisor and the adviser continues to trade. If that franchisor had entered the market with incorrect documents he could have unwittingly been liable for sanction, yet the consultant is not linked or indeed sanctioned.

Another issue about these consultants includes those that are marketing firms that sell on behalf of various brands. These consultants ask for substantial deposits up front, and retain the moneys as a form of commission. These salespeople are not required to meet standards, nor indeed the code, and can virtually mislead at the expense of the franchisor, for it is the franchisor that retains responsibility.

There is evidence of false and misleading advertising being used to attract both franchisors and franchisees, yet the code or indeed any other ethical standards do not apply to their behaviour. This is an issue I ask the committee to give serious consideration to.

There has been a lot of discussion in this inquiry on the issue of pre-entry education, but there has not been much discussion on the responsibility of the franchisor towards training and teaching franchisees on how to comply with the operations manual. The operations manual is the franchise system, yet in many systems it is my experience that these manuals do not comply with the franchise agreement. Thus, if the operations manual does not comply, and the franchisee alters the operations manual due to poor induction, then a dispute over non-compliance may exist, particularly if the franchise is sold to a more diligent franchisor. We have heard stories from franchisees who are non-compliant, for various reasons, yet if we studied the reason it could point back to the operations manual and the adequate or inadequate training and maintaining compliance to the operations manual.

The franchise agreement is all about the franchisee complying, yet when it comes to ensuring the franchisee does comply, via the support of the franchisor, the franchise agreement generally remains silent. The code refers to the franchise agreement and the agreement is mostly about the franchisee compliance, yet nothing within the franchise regulatory sector stipulates what the franchisor must do to ensure they indeed comply with the intent of the business arrangement. Indeed, if the franchisor does not comply there is little support for the franchisee. Adjusting the code will not change the method of support from the franchisor. Ensuring the franchisee is capable of complying is the very first tenet of the relationship, yet it seems many franchisors

neglect this essential activity. It is, therefore, incumbent upon the franchise system that they are thoroughly trained and the incoming franchisee is across all systems, yet many franchise systems do not apply compliance training. I am not sure how the committee can improve this process, and I suspect legislation or regulation cannot, but the industry can, via a best practice standards model.

On the issue of goodwill, I believe that goodwill exists whilst you have an agreement, such as a retail lease or a franchise agreement. When the agreement ends, so does your goodwill. Within the franchise I believe goodwill is retained by the brand, yet there does seem to be some support for recognition of the work done by a franchisee in establishing a brand in a particular location. There is an argument that the end of term needs to be clearly articulated, but I also suspect there is an argument for a responsible distribution of end-of-term funds, in other words, a sharing of the value of the franchise outlet between the franchisor and the franchisee. This percentage will need to be negotiated and articulated prior to entry, so it is clear for all parties.

Lastly, the ARA believes that almost 75 per cent of disputes are resolved, but some disputes require an arbiter. These are disputes that do not breach the code or the TPA and cannot be resolved in mediation. We see merit in having a non-judicial tribunal added to the current regulatory system which is similar to the VCAT that operates in Victoria. However, we strongly suggest that this arbiter exists in a dispute after mediation has failed, is relatively inexpensive and sits outside the court structure with limited appeal processes. I would also suggest that this process will encourage greater resolution at mediation, and a recalcitrant party at mediation will have their behaviour considered within the arbitration process.

We also agree that clear articulated sanctions for breaching the code would help the market and perhaps reduce deliberate breaching of the code based upon minimal risk required. Any action in this area would have the ARA support, for our view is that those who breach the law should be sanctioned.

We again thank you for the opportunity in addressing you and I am happy to answer any questions.

CHAIR—Thank you for your submission. I would like to run through your executive summary and flesh out a couple of issues that you have raised. In the first paragraph you say that the ARA retains the view that retail franchising is over-regulated, although you are supportive of the regulatory environment. Can you explain to us where it is over-regulated?

Mr Evans—There are two aspects to retail franchising. There is franchising and, of course, retail leasing. In retail leasing we have different regimes in different states, all having different laws. We also have an over-pinning franchise legislation and the Trade Practices Act. To have certainty in the marketplace there are a number of issues that need to be addressed for retailers. They need to have certainty of tenure, which they do not necessarily have under a retail leasing arrangement. For a franchisee, they need to have certainty of tenure with the brand.

CHAIR—I understand that, but where is it over-regulated?

Mr Evans—What I would say to you is that it is regulated enough and does not need any more.

CHAIR—That does not really help me. You cannot say it is over-regulated, and then I say which bits of regulation, not which bits of retail leasing, tenancy agreements and all the rest of it; that is not regulation, that is arrangements and contracts. Which bits of regulation, either the Trade Practices Act or the code? Where can we make improvements? Where can we remove things to make it regulated properly?

Mr Evans—Specifically in franchising you cannot, but specifically in retail leasing you can.

CHAIR—Whereabouts in retail leasing? That is more state based.

Mr Evans—Correct.

CHAIR—We are not talking about something that the Commonwealth can do in that particular area.

Mr Evans—The Commonwealth can do a couple of things. It can bring a code of behaviour in for the Retail Leasing Act.

CHAIR—Do you want more regulation?

Mr Evans—No. What you can do is have a standard template for retail leasing across Australia, which will improve the systems across Australia because each state operates independently and differently. There is one particular issue and that is the code of behaviour which was recommended for the federal government to do back in 1996, but they did not act upon it because of the state legislation. The other area that really hurts a lot of retailers is the issue of disclosure of turnover figures.

CHAIR—That is not required in the detail. There is still commercial-in-confidence. People are not required to publicly disclose commercial-in-confidence figures.

Mr Evans—Not publicly, but they do to their landlords.

CHAIR—You have to know. How else would you make—

Mr Evans—The landlord does not have to know what your turnover figures are. It is a requirement under each of the state based laws that they have to disclose.

CHAIR—Thank you for that. You mentioned in there that you share a genuine desire to ensure that fairness prevails. I will pursue that in a couple of areas. In your submission you have talked about fairness in terms of franchising. Can you explain what the ARA sees as fairness in franchising?

Mr Evans—Franchising is a very interesting method of brand distribution in the marketplace. What it brings is two investors together. We have a major investor being a franchisor, and a minor investor being a franchisee. A franchisee is attracted to it because it provides a business model which they can invest in from which they can get a return on investment during a required period. There is a relationship. You have been told before by other witnesses that there is a major relationship between the franchisor and the franchisee, and indeed one of your press releases

said that it was not an equal relationship. The reason why it is unequal is that there is greater risk for the franchisor than the franchisee, and there is greater investment for the franchisor as opposed to the franchisee. But both are working for the needs of the brand. Both are working for a win-win, which means that both are successful and both are making money. That is where the fairness aspect comes in.

CHAIR—You say that there is a greater investment made by the franchisor rather than the franchisee. I do not understand what you mean by that. It is the franchisee who actually pays the fee. It is the franchisee that puts in all of their capital. As we have heard right across the sector, it is often their whole life savings and in fact they invest everything they have. The franchisor risks their brand, if you like, but that is not technically an investment in the same sense of the risk factor. If you have a bad franchisee you get rid of them and get a new one in. In terms of an investment how would you say the franchisor has a bigger investment compared to the franchisee?

Mr Evans—It depends on how they start. If they start as a corner store themselves they develop their IP. That development of the IP requires a development where in fact it can be replicated in another location. There is an investment required in developing that IP. It is the investment of establishing that business in the first place. You also have the investment of getting the appropriate documentation done so it complies with the Franchise Code of Conduct, the investment of support staff and the investment of education.

CHAIR—I understand all of that. If you are saying this I will pursue it because I am trying to determine how you make that judgement. It is the franchisee that puts up the capital.

Ms OWENS—You are talking about two different things.

CHAIR—No, we are not. I am very clear on what I am talking about.

Mr Evans—With respect, I do not think we are. The franchisor has a major contribution. It is a major investment financially and also in intellectual property. It is greater than the franchisee. The franchisee invests into that IP and invests in that location, but it is not as great as the franchisor.

CHAIR—I will take it as what you say. If the franchisee invests all of their life savings—

Mr Evans—There is no reason why the franchisor could not be investing their life savings.

CHAIR—Let us say that they have an equal investment.

Mr Evans—I do not know whether it is an equal investment. If a brand has 700 stores then surely the investment by the franchisor is greater than someone with a single store.

Senator MASON—That may be in absolute terms, but not in relative terms.

Ms OWENS—With respect, you are talking about different things. The chair is talking about the marginal costs for this particular franchise, and you are talking about the overall costs or the

fixed costs. There are two different discussions going on. Would you be including the global advertising, the HR costs and the legal costs?

Mr Evans—Yes.

CHAIR—Which is all paid for by the fees of the franchisee, and the royalties.

Mr Evans—That comment means that there is no development of the brand in the first place. The comment you have just made indicates that the franchisee is equally contributory to the brand. If the brand has been going for 20 years and someone comes in 20 years later, have they contributed to the development of the brand, or have they invested into the brand? The franchisor has a much more significant investment than a franchisee.

CHAIR—You say in the ARA's view that the law concerning franchising is adequate, but does have some weaknesses. You have mentioned a couple on the way through. Can you elaborate on that? Where are the biggest weaknesses? Where can we make improvements?

Mr Evans—Consultants are not obliged to meet anything under the code. It is all franchisor and franchisee discussion. That is a significant issue.

CHAIR—I will just pursue that. If we are going to deal with that then we have to understand what that means. Consultants have the same laws applied to them as everybody else in the marketplace and in business, and the code is essentially just about disclosure. It is about ensuring that there is disclosure of information between the parties. How does the Trade Practices Act or normal law apply to that? You say consultants, but in the end what you mean is lawyers, accountants and other advisers.

Mr Evans—It is the other advisers in the sector.

CHAIR—What laws are they breaking? What is it that they are doing wrong?

Mr Evans—They may in fact be advising incorrectly about the franchisor's requirements under the law. For franchisees, they may be building over-expectation.

CHAIR—And nobody else does this, just consultants?

Mr Evans—I need a little bit more information. What do you mean by that? Do you mean lawyers and accountants?

CHAIR—All of them. I am just using your words: consultants, advisers or whatever you want to call them, the people who give advice. I am assuming you give advice. I am assuming that you are in the same basket. The ARA is a membership type body and you give advice. What laws would you like to be governed by in relation to that advisory role? You state:

It is the ARA's view that the law concerning franchising is adequate, but it does have weaknesses surrounding perhaps a range of things.

In particular, you refer to consultants, advisers and so forth.

Mr Evans—The code is meant to monitor or manage behaviour.

CHAIR—I do not understand. How does it manage behaviour? It is about disclosure.

Mr Evans—That is true, but that is behaviour. It is basically asking franchisors to disclose everything they have about their system. It is really overcoming the issue of giving false hope and false expectation through the use of words. You cannot do that. It is here in black and white in our disclosure document and this is our system. If someone is on the peripheral over here giving advice about it being a good deal, a bad deal, this is what you should be doing and this is what we can do, then they do not come into the code, if you like, of managing their behaviours. Indeed, there has been a lot of poor behaviour associated with the development of documentation within the franchise sector, which has been developed by people that should know better.

CHAIR—Yes. I am not sure that you are giving us any help. Prior to the voluntary code you really just had the Trade Practices Act and other fair trading laws. That still applies now. The code is really just about disclosure, about making sure that people have access to information that they otherwise may not have. If that is on the table, let us say it still does not manage behaviour.

Mr Evans—It did.

CHAIR—It manages the behaviour in terms of providing information, but it is the post-contract behaviour that seems to be the biggest issue, not so much the pre-contract behaviour. Pre-contract, people make a decision as to whether they want to sign up or not, but what manages the behaviour afterwards? You cannot lay all the blame and say, 'It was just the consultants. They should not have advised you to take this on.'

Mr Evans—I am not laying the blame for the entire issues of the franchise sector on the consultants, but I am suggesting to you that there are many who are practising in the sector that have no requirement to tell the truth.

CHAIR—That is interesting.

Mr Evans—I just happen to have an example here of someone who submitted a submission to you and has said on their website that they have worked at a franchisee level, launched a franchise system and provided PR marketing service. What they are doing is attracting franchisees and franchisors to them so they can advise them. This particular person said he was a winner of a franchise system of the year in 2004, but he was not. He also claims he was the winner of a Franchise Council of Australia Contribution to Franchise Award, but he was not.

CHAIR—I know where you are heading with that. I am not sure that is what this particular inquiry is about.

Mr Evans—But that is fundamental, because if someone comes to this particular consultant who is or is not an expert and they are taking advice from that person who is not expert then ultimately they may—

CHAIR—There are laws to prevent people from providing deceptive and misleading information and so forth.

Mr Evans—Correct, but there is no management of that within the franchise sector.

CHAIR—I accept that. It is interesting that you say there is no management of that because in your opening remarks you said: 'The Franchising Code of Conduct and the Trade Practices Act provide important protection for franchisees, and the Australian Competition and Consumer Commission has been a highly effective industry regulator.' I was going to ask you by what measure, but you have explained to me that there is not a highly effective regulator. Whose job should it be?

Mr Evans—I disagree.

CHAIR—Who should be dealing with that issue that you have raised?

Mr Evans—The ACCC is a very effective regulator, but many people come to the ACCC wanting it to resolve issues that perhaps do not fall under the ACCC's regulation bona fides. The Office of the Mediation Adviser was developed to help resolve disputes, but in my view there are disputes that fall between those two areas. That can either be picked up by an arbiter or by the industry. The industry has tried to do it. They had a complaints process, which I am sure the industry will talk about later. They have also tried to set up an accreditation system for their consultants, which they have been doing for the last 12 to 18 months. The accreditation process would help with the consultants, but you do not need to be an accredited consultant to trade within the franchise sector.

CHAIR—You have put a lot of weight in your submission on the issue of consultants and pre-contractual advice. I think pre-education is a very important part of that. Given the fact that franchise agreements are all standard form contracts and that there is no negotiation that takes place, you either take a contract or you do not take it—you do not get to negotiate what is in it—how important is that advice? As you said before, if there is a 20-year franchise system that is out there and there are hundreds of franchise systems, if you decide to take one of those up, would you expect that the advice would be the same on all of them? They are all the same contract. I am just trying to find the point of difference that a consultant would make, given that there are hundreds of them out there. They say, 'It is the same as all the others. There is nothing new or different to anyone else's in this contract. You either want in or you do not. Take it or leave it.' What difference does that make?

Mr Evans—There are a number of differences. One is that the person actually advises about what their expectations are and what you can actually realise out of the operation whilst you are there. A lot of folks go in believing that they have a franchise agreement forever. Who gives them that advice? I do not know. Their franchise agreement does not say that. The disclosure document probably does not say it.

CHAIR—Is that what you are driving at? Are the expectations the core of the problem? I am trying to find where there are legal problems and problems we can fix. We are certainly exploring expectations, but regardless of where that expectation came from, what are we supposed to do about that?

Mr Evans—It is difficult. The code asks franchisees to seek out advice and understand the expectations prior to going in. A lot of folks do not.

CHAIR—Through this inquiry we have received a lot of evidence as submissions and the people that I have found that have disputes are the ones that were the most educated, put in the most time and understood it better than most. That is why they do have a problem because they have discovered something within the system that really was not what was described in the original contract or the manual. You mentioned earlier about the problems with the manual. The more you know at the beginning does not seem to really help you at the end or when there is a dispute.

Mr Evans—That is true. You have now moved into another issue, the issue of non-compliance with the operations manual, which is probably at the core of a lot of issues.

CHAIR—This was not about non-compliance. This was about unreasonable requests, demands or life being a little bit more difficult. It is certainly not contained in black letter law in the contract. Contracts are fairly simple, even with disclosure. It just provides a whole heap of information. If you pare that away, again it does not provide you with a great deal. It is a standard form contract. Everyone has the same contract yet some people will have a dispute and others will not. How do we manage that better? How do we regulate in a more efficient manner?

Mr Evans—The question is: why do you want to?

CHAIR—It would just seem to be an obvious thing that you try to improve things and make the sector better and, if there are disputes—

Mr Evans—There are 60,000 people already operating in the system and there are probably less than 1,000 disputes.

CHAIR—That is not the reality, though. We have got some raw data and we have actually got evidence on the *Hansard* record from the department that looks after this, including the Office of the Mediation Adviser, that those figures are meaningless and do not reflect what actually goes on. That is from the department itself and the people who manage it. When I asked them on the record about the level of disputation that is recorded and the outcomes I was told in the end it meant absolutely nothing. If you are using that to say, 'Look, there are no problems in the sector' and then ask why are we pursuing it, it is to try to make it better because—

Mr Evans—Are you asking me that if someone is frustrated with the franchise system after, say, 12 months or two years or so—

CHAIR—I am not asking for a philosophical view. We are having an inquiry. I know from your submission you are not particularly keen on us having the inquiry, although you accept it—

Mr Evans—That is not true.

CHAIR—That is what it says in your submission. We are not after a philosophical view. We are trying to determine where we believe there are some issues and how we can make efficiencies. You say for example, 'We are over-regulated.' I ask you, 'Where? Where can we be

more efficient?' You say there are problems with consultants and I ask you, 'Where can we do better there?' That is what I am asking. I am not asking for philosophical positions.

Mr Evans—I am not trying to give you a philosophical answer. You were saying to me that there is greater dispute within the sector provided by the department. I have asked you, 'Where is that?' You are saying the figures provided by the ACCC and the OMA do not actually give us a disputation within the system. Therefore, it is a philosophical question you are asking me.

CHAIR—No, I am not. I will start again on that one. Forget the disputation levels. Let us not have a debate over how much disputation there is. There is disputation. That is the fact. In fact, so much so that there needs to be a code, regulation and an Office of the Mediation Adviser to deal with the disputation, and the ACCC is the regulator. We have established that there are disputes. Now that there are disputes, we are trying to establish how we can reduce the number of disputes; how do we make the system more efficient and better, perhaps to give your organisation less work. I am sure that is probably not what you want. In what areas can we make it better as a system, rather than debating on whether there are 10 or 12 disputes?

Mr Evans—We should make the issue of the operations manual more compliant with the franchise agreement. We should help the franchisors somehow to train their franchisees to be compliant with the operations manual.

CHAIR—We need to put a bit more weight on franchisors perhaps setting a higher bar and making sure they do train people more effectively. It is a tough area.

Mr Evans—I do not know whether you can do that legislatively—

CHAIR—Exactly.

Mr Evans—The industry is trying to do that. But I will give an example. The previous government asked for accredited training to develop and they developed a thing called the frontline management which they invested back into the sector and our sector developed the training programs associated with that. They put money to training organisations to do that. They then asked the franchise sector to develop a diploma and cert IV, cert III, and cert II of franchising, and we did that. But then they did not provide any adequate funds—in fact zero funds were provided—to develop those training modules. So here we are trying to train franchisors and franchisees to be more compliant and the government wanting us to do that in terms of a code, in terms of wanting us to have accredited training, but the government is not providing any funds at all back to the industry to in fact support that. How do you make it more effective? You get the operations manual compliant with the franchise agreement and help the franchisors train their franchisees to be compliant to the operations manual.

Ms OWENS—I found it really interesting that you said in your submission that franchising is actually a rental agreement. That was the first time I had ever actually heard it described that way, that a franchisee actually rents the brand for a period of time. Would you just expand on that a little more?

Mr Evans—It is my view that if you go into a lease, whether it be a domestic lease, a business lease or a retail lease, at the end of the lease you either renew it or you do not. You have

no certainty of tenure and therefore the agreement ends. In a franchise agreement it is much the same. You are in fact renting a brand basically over a period to work that brand to return some funds for yourself. Your investment into the brand is the entry factor. There are other costs associated with that and it varies per franchise, but at the end of term my view is that there is no goodwill. However, I said in my opening statement that there is an argument that perhaps on a certain location there could be a sharing of goodwill by the brand and also the franchisee.

Ms OWENS—As to the failure rate of franchises, to a large extent small business fails in its first year. Do you know the failure rate for franchises?

Mr Evans—For the first year?

Ms OWENS—Yes.

Mr Evans—No.

Ms OWENS—Do you know whether it is higher or lower than other forms of business?

Mr Evans—I would have thought it was lower.

Ms OWENS—My sense is that it is lower.

Mr Evans—There is no evidence to suggest the failure rate of small business. Although there is this urban myth going around the place that the failure rate of small business is about 80 per cent in the first three years, I doubt whether that is correct. There have been no accurate studies done on the failure of small business. The rates of failure are done by Griffith University. I think that is probably the most academic view, but even that study could be questioned.

Ms OWENS—Your sense in your role is that the franchise failure rate is quite—

Mr Evans—It is low. I would say it is low because you are buying into an operating system and it is in the best interests of the franchisor to in fact support the franchisee to be successful. It is in their best interests.

Ms OWENS—It seems that a lot of your submission is about the lack of common perception at the entry point caused by either inadequate advice, or whatever you want to call it, or a lack of training. Are you recommending that there be accredited franchise training courses for franchisees?

Mr Evans—There are already accredited training courses. If we had an accredited say cert III or cert II—cert III particularly—some of the franchisors that I have spoken to would say, 'We do not want to see you until you go and do this course.' That is what a lot of franchisors would ask to happen. However, cert III courses need to be funded. They are funded mostly via an employment arrangement and that funding by the government is not available for all the people moving into business. I think there is probably an argument for people moving into a franchise business to at least get the cert III training in franchising.

Ms OWENS—If we were to push for a greater synergy between the operations manual and the franchise agreement, where does the training issue apply there? Is that just with the consultants or is that with the franchisors as well?

Mr Evans—It is mostly with franchisors. The chair was talking about investment before. Franchisors have the right intention about training their franchisees. A lot of franchisees say, 'No, I know how to fry a doughnut so therefore I do not need the training.' But it is not just frying the doughnut; it is actually about managing the business and managing the operations manual. I am happy to listen to the industry dispute it, but it is my experience that a lot of operations manuals are non-compliant to the franchise agreement. If a franchisee comes in in the early days working to the manual and decides, 'Oh, that is wrong. I will just do it this way', and the franchisor tightens up the compliance aspects to their operation and they then say, 'But I have been doing it this way for five years', or four years, or whatever it might be. 'You have not asked before. Why now? This is successful for me.' They are then told, 'No, you have to comply. Here is the franchise agreement. You have got to comply.' They have been working something associated with the operations manual. It does not seem to me within the sector that there is a requirement that the operations manual is compliant with the franchise agreement. There may be—

CHAIR—Wouldn't that be more complicated?

Ms OWENS—What would we have to change to make that happen?

Mr Evans—I do not think you need to change any laws about that. They just need to have a standards process within the sector. Is it a five-star franchise, is it a three-star franchise or is it a one-star franchise in terms of the standards associated with it, so that they have got a training program that helps with compliance? A lot of the disputation I would imagine is in non-compliance. Why are they non-compliant—because they are not following the operations manual?

CHAIR—You are posing some really interesting stuff: trying to rate franchise systems with one star, two stars, three stars—

Mr Evans—This is the stuff for the industry. It is not for legislators—

CHAIR—I was going to say it is definitely not for us.

Mr Evans—It is really something for the industry to get involved with. That is why I am saying it is very difficult now for legislators to in fact start changing the code or indeed applying other law on operational matters.

Ms OWENS—On that comparison issue, if I were considering taking on a franchise as a franchisee I would want to be able to compare the success of my brand to other brands in that way. In your suggestion that you should be able to say, 'That deserves three stars in terms of providing this', or whatever, that would be a valuable thing for franchisees to help make the choice.

Mr Evans—Nothing will overcome good advice but it would be an indicator, or a direction, if you like.

Ms OWENS—Are there other things, too, like the failure rate in a particular franchise brand that would—

Mr Evans—The Matthews inquiry said that the franchisor must include all franchisees for the last three years. I believe it is incumbent on a franchisee to go and talk to franchisees currently in the system and previously in the system to understand what it is about, what the requirements are, how it is going to affect their family life, and what they can and cannot do in terms of their own personal expenses et cetera. I do not know, but anecdotally I do not think a lot of franchisees do this because they have expectations built in them and they want to go into a business and are very excited about this and they do not necessarily want to be dissuaded from it. Matthews said: 'Go and talk to these franchisees. Here are the listings of all of the ones that have left the system. Go and find out why they left.'

Ms OWENS—That would still only give you the information within the brand that you were considering?

Mr Evans—That is true, but if you are talking about going into a business where there is a massive investment—we are not talking about a $5,000 investment; we are talking about a massive investment—then you should go and do that due diligence. A lot of folks go in with the view that they have given it due diligence and a lot of folks are successful, not having in fact spoken to a lot of other people. But the point is that some folks do not and one of the reasons probably why they do not is because they are non-compliant with the operations manual.

Ms OWENS—We have had examples here of franchisees who have been told within the franchise agreement that suddenly instead of holding 30 days worth of stock they have to hold 90 days worth of stock. There have been basic changes to the business model within the period of the agreement. Is that a common thing or is that unusual?

Mr Evans—It is not unusual, but I would not have thought that it was common. Good franchise systems communicate with their franchisees and discuss these things with their franchisees, and franchisees understand why a decision is being made. Perhaps even in some systems it may even have been suggested by a franchisee. Good systems are like that. As to other systems, it depends on the franchisor and it depends on the amount of pressure upon them and if they need to get a change through they may in fact force the franchise agreement because it is part of the franchise agreement, 'I am forcing you to do this.' The franchise agreement is all about relationships and good communication. Some people do it well; others do not. How can you legislate for that? You cannot.

Ms OWENS—You referred a few times to sanctions. What would those sanctions look like?

Mr Evans—I think there should be a penalty for a breach, both for the franchisor and the franchisee. I do not think that is articulated anywhere at the moment?

Ms OWENS—There would be a penalty for example if your operations manual and your franchise agreement were so at odds with each that you could not find—

Mr Evans—If the ACCC, or whoever it was, determined that there was a breach there, then there should be a sanction.

Ms OWENS—There should be sanctions?

Mr Evans—I agree. If anyone breaks the law, let's punish them.

CHAIR—What happened to the freedom of contract?

Mr Evans—What do you mean?

CHAIR—You are saying that with regard to all these things that the two need to comply with each other, but is that not all part of the freedom of contract?

Mr Evans—I would not have thought so. You are going into a franchise agreement. You understand that you are going to meet that franchise agreement and part of that agreement is the operations manual. You must comply with the operations manual. If the operations manual does not comply or you are not shown how to comply with that operations manual in the first place, ultimately there could be a dispute.

Ms OWENS—You are really saying here that there are some situations where a franchisee simply could not comply with both documents, that really it is not possible for it to be a relationship—

Mr Evans—Anecdotally my advice is that there are many of those.

Ms OWENS—I am still trying to find the path for us to make that better. Would it involve better education of the franchisees, which would probably mean that they would not enter into that agreement?

Mr Evans—Better education of franchisors.

Ms OWENS—Better education of franchisors which we—

Mr Evans—And accreditation of consultants.

CHAIR—When you say the operations manual does not comply, comply with what?

Mr Evans—The franchise agreement.

Ms OWENS—It is not possible to comply—

CHAIR—I have had a look at a number now and I would say they all comply because you, as the franchisor, can write in there whatever you like. The normal clause that is contained in the contract basically says, 'You will comply with the operations manual full stop.' And then the operations manual says, 'You will comply with it, no matter what it says.'

Mr Evans—That is true.

CHAIR—That is exactly what happens, so when you say it complies with—

Mr Evans—I will give you an example. I have come across an operations manual for a lawn-mowing franchise that said, 'Do not forget to turn your hairspray cans every two weeks.' This was in an operations manual for a lawn-mower.

CHAIR—Yes, good point. But there is no breach or anything else?

Ms OWENS—Can you give us some more examples.

Mr Evans—I cannot off the top of my head, but I can provide you with some—

CHAIR—There are obviously some big problems in the sector, so we need to be doing a lot more work than I thought.

Mr Evans—No, I think the problems with the sector are—

CHAIR—You are describing some very unusual problems.

Mr Evans—There are some problems with the way consultants actually draw up documents. There are problems with the way—

CHAIR—Shouldn't the franchisor fix that? It is their system. Who is running the system? Who is running the show?

Mr Evans—You have said in evidence yourself that you have franchise agreements this thick. A lot of folks in business do not necessarily read a lot of documentation; they trust their advisers to be doing the right thing. They trust their advisers and if their advisers are not doing the right thing then you have got some problems. That is the point I am trying to make. In a franchise agreement it is, 'Thou shalt do this', to franchisees. If the franchisor does not help the franchisee to do that there is no comeback against the franchisor. That is not a legislative comeback. I do not know. There might be a sanction comeback I guess. I do not know. It is all about the franchisee, which it should be, but if the franchisor is not helping with the compliance of the operations manual with their franchise agreement, then you have got potential disputation.

Senator MASON—You will have to excuse me, I have only joined this inquiry today, so I am new to the issue and perhaps somewhat ignorant, although enthusiastic. Do you seek to represent franchisees as well as franchisors?

Mr Evans—Both.

Senator MASON—I ask that because the weight of the submission seems to be pretty much in favour saying that the system is okay and that business failure is primarily predicated upon the franchisee making bad business decisions and so forth.

Mr Evans—The amount of franchisees—

Senator MASON—The weight of your submission.

Mr Evans—The amount of franchisees I have spoken to, and I have spoken to many—and indeed I have written a book on it—say that if you follow the system the likelihood of success is high. If you do not follow the system the likelihood of success is not high. Other problems associated with business may be that franchisors are very good at training their franchisees in how to fry a doughnut. They are very good at that. They are not necessarily that good about helping them comply with other legal requirements such as industrial relations law, other trade practices law and consumer law. They are not necessarily that good at showing them how to do that. A lot of franchise agreements say you must comply with federal and state laws. It is probably a paragraph this big.

Senator MASON—The laws are this big, aren't they?

Mr Evans—Industrial relations law, for instance, is a very difficult one and a lot of franchisors do not support their franchisees within that area of law. Helping them as much as possible is an area that I think franchisors are moving into, but the franchisee needs to attain a certain amount of entrepreneurialism, if you like, to be able to run that business. But franchisors need to be doing more in training their franchisees on how to run a business—when not to buy the BMW. Just because you have got a lot of cash does not mean you go out and buy the BMW. You have got to teach them about cash flows, profit lines and a whole range of different things. They are not necessarily trained for that going in. They are very good at frying a doughnut but they are not necessarily that good at running a business.

Senator MASON—That is a fair point. In relation to your oral submission you make a couple of points about accreditation of consultants and goodwill. Can I just touch on those two issues briefly? You want to accredit consultants, and that is terrific. But would that again establish a new bureaucracy? Are we again putting more and more red tape on this, or do you think this is something that really would assist industry? How would we do it?

Mr Evans—The industry has got it right. The industry runs itself. They have started doing it with their CPD program, but they have got to manage it and ensure that—

Senator MASON—Do you have accreditation agencies and so forth? If you are going to accredit people, you have to have accreditation agencies and examinations and all that sort of thing? Can that be done?

Mr Evans—If you work on the CPA model, the industry does it themselves. You have to teach the sector to only deal with accredited consultants. How do you get accreditation? You go through the training programs and you tick off all those boxes.

Senator MASON—The model would be CPA, or something like that.

Mr Evans—A CPA model.

Senator MASON—I am not saying it is a bad policy, as I am new to the area, but my only reservation is that it is establishing another regulatory framework which—

Mr Evans—No, the industry can do it. Whether or not they are helped with government grant funding to help them establish it—

Senator MASON—Maybe so. In relation to goodwill, I think you said the work of the franchisee should be recognised?

Mr Evans—My personal view is that there is no goodwill. Goodwill remains with the brand. However, there is an argument for franchisees sharing in that goodwill if they have established that particular location over a period of say five or 10 years—

Senator MASON—And they have done a very good job?

Mr Evans—They have done a great job, so there should be a sharing of that goodwill. The problem is what value you would put onto it. My view is that if you are going to share goodwill it should be articulated in the agreement and it should be agreed to at the start—

Senator MASON—That is the problem. You say it should be negotiated prior to entry into the contract, but in a sense you cannot. That is contrary to normal practice where of course you negotiate goodwill when you sell your business. If you are negotiating prior to entry into the contract you do not know if they are going to do a good job or not, which makes it very problematic.

Mr Evans—That is absolutely true. However, who has the goodwill? Does the brand have the goodwill? My view is that the brand does. But do you recognise—

Senator MASON—Does it have all of it? I am not saying you are wrong, but does it have all the goodwill? I suppose that is my point.

Mr Evans—My point is: do you recognise the work that the franchisee has done over the last five years? My thinking is that perhaps you should, but is it fifty-fifty? No, it is not.

Senator MASON—I am sort of with the chairman on this. I note at the bottom of your executive summary you have written that the question then should be raised that while 'there continues to be a willingness to investigate these claims at a parliamentary level, uncertainty within the sector will prevail reducing investment confidence.' In other words, there will be less investment confidence because of continuing parliamentary oversight. You may even be right—

Mr Evans—Would a potential franchisor establish a brand or develop a system in an area that is constantly being investigated?

Senator MASON—You might be right, but what we have learnt over the last 12 months is that when something fails like the banking sector, do you know who everyone runs to for assistance—the government. In the end it is not you and not the franchisors; it is us that people will run to. That is why we are always questioning. That is what happens.

Mr Evans—Having been there and done that, I understand what you are talking about. What I am saying to you is that we have very strong trade practices laws in Australia. We have the—

Senator MASON—I am just saying that in this sense the buck always stops with the parliament. In the end, if we do not ask questions particularly in response to community concern—and there is some—then we are not doing our job.

Mr Evans—I absolutely respect that, understand that and agree with that. But when you have members of parliament standing up in the chamber not quoting both sides of an argument and calling upon the parliament to have an inquiry into a dispute that has already been investigated, then we need to consider that and have some balance in it. If you are constantly investigating a sector then not only do the banks start wondering if they should invest in that sector but also potential franchisors wonder, 'Well, should I be investing in that sector?'

Senator MASON—I understand. Parliamentarians always look at both sides of the argument, don't they?

CHAIR—Yes.

Mr Evans—Parliamentarians do a lot of great work, and I am sure this committee will come up with some fantastic recommendations.

CHAIR—Can I suggest to you that even though that is your view that in fact in the last 10 years with all this massive weight of investigation and inquiry the franchise sector has actually flourished, according to your organisation and every other organisation I can find. Can I just ask you a simple question before we pull it up?

Mr Evans—If that is the case why are we having an inquiry?

CHAIR—I think we agree with you as to the need to have good systems. We need to have systems that actually do work. With all the best training, all the best systems and all the best pre-education, unfortunately there are just some unscrupulous operators—

Mr Evans—Franchisees or franchisors?

CHAIR—Just unscrupulous people. We are not biased in this. We are actually very unbiased. What we are saying is what do we do about the unscrupulous operators? Whether the manual is the best manual in the world; whether there is best practice and all the rest of it, there are still people who do the wrong thing. What do we need to do to try to remedy that?

Mr Evans—There are no articulated sanctions. Fine them. Jail them, if you must. If they break the law, come hard at them.

Ms OWENS—We have seen some franchise relationships which look to me like they are really licence agreements rather than proper franchises. Do you have a definition of what the bottom line is as to when it is a franchise relationship or when it is a licence relationship?

Mr Evans—There is a definition in the code. I think I would say the ACCC has some difficulties sometimes in people going around that system and saying that they are not a franchise. I think if that is the case then what you might be suggesting to me is: is there a case for registration? I have a lot of difficulty in registering franchise systems. Who is going to do it?

What is the cost? What are the implications associated with it? That would ultimately give it a proper definition between a licence and a franchise, but as the chair said there are always unscrupulous people around trying to get around the system and they will always be there. The question to ask is whether the laws are good enough at the moment? I believe they are. I think they are the best in the world in terms of franchising but I think the weakness is that we do not punish hard enough the ones that breach it.

CHAIR—The ARA say that they are opposed to the insertion of good faith in the code or any reference to good faith, although you do recognise that it is obviously another piece of legislation, that it is implied within the Trade Practices Act and contained in other areas. Why is franchising different that good faith should not apply?

Mr Evans—Franchising is not different and good faith is just difficult to define. They have tried to do that with 51AC. 'Good faith' has a different meaning to many different people. If you are going to use 'good faith', then you would have to clearly define it.

CHAIR—Everyone understands what good faith is. I do not think there is any difficulty anywhere understanding what good faith is. Everyone has a view of what good faith is and what it means. It is up to the courts to then decide the application of it. Again, if it is good enough for everybody else in business, it just seems to me that in certain submissions there is very much this anti good faith view. Why is it different in franchising? Good faith is implied in every contract and every business negotiation. It is actually written in law in a whole range of—

Mr Evans—I believe the parliament considered this back in 1997 and 1998 regarding 51AC and whether or not to call it good faith or unconscionable conduct. The arguments you are putting forward to me now are the same arguments as back then, in that they determined it was better to call it unconscionable conduct and therefore point to a number of factors that a court should in fact refer to as opposed to calling it good faith. Is it a semantic debate? I do not agree that it is a semantic debate. I believe good faith implies different things to different people, and that section 51AC is there primarily to protect folks going into a franchise agreement. It has not been tested that much, though.

CHAIR—Finally, rather than talk about goodwill, because I think perhaps there are complications in the use of that word, I think we all agree that there is a value to any business and that it can be transferred. A franchisee can sell their business on the open market and realise their gain. They can build up a business over a number of years, realise their gain, transfer it or be bought out by a company, which just says, 'We'll buy it off you.' Call it what you will, there is a value to that business, and it is more than nothing. I will not put a figure or percentages on it. It is worth something. Therefore, at the end of an agreement, should the franchisor have the right to reduce the value of that business to zero purely by the power they have within their contract?

Mr Evans—That is interesting? Should they have the power to reduce the value to zero? If the outlet or the franchise is saleable on the market, the answer is, no. The franchisee should in fact share some of that sale cost. I am not sure as to the percentage.

CHAIR—We could argue all day about percentages. That is not the point. The point is that there is a value, that value is real and it can be transferred and realised. On the day the franchisee buys it it has a certain value, and if they are very good at their job—some are better than

others—they will build that business and it will grow in value. They can then sell it on the open market, with the permission of the franchisor, and realise that capital gain.

Mr Evans—Without question I absolutely agree with you. If you do this for franchising, you must do it for retail leasing.

CHAIR—Perhaps that is another inquiry.

Mr Evans—You need to consider it, because that is a significant issue for retailers.

CHAIR—I was not sure that the ARA or anyone else was happy about having more inquiries. Thank you very much.

[10.06 am]

GILES, Mr Stephen, Legal Committee Chair, Franchise Council of Australia

MELHEM, Mr Tony, Franchisee Forum Chair, Franchise Council of Australia

O'BRIEN, Mr John, Chairman, Franchise Council of Australia

WRIGHT, Mr Steve, Executive Director, Franchise Council of Australia

CHAIR—I call the Franchise Council of Australia.

Mr Wright—Thank you for the opportunity to present to the committee. I welcome the new deputy chairman on board. We have four representatives here from the FCA. We represent franchisees, franchisors and suppliers/service providers in the sector. Mr Giles is probably the most experienced service provider in the sector, an author, a partner at Deacons, chair of our legal committee, and highly regarded across the sector as the foremost legal authority in franchising. Mr O'Brien is our chairman, a past master franchisee and franchisor. He is CEO of PoolWerx, a successful Queensland based company. Mr Melhem is the chair of the Franchisee Forum, which is the instituted franchisee representative group represented on the FCA board. Mr Melhem is from New South Wales. We are going to begin with some opening remarks by Mr Giles, which might also pick up a couple of the issues mentioned in the previous session.

Mr Giles—We are very supportive of the role of the committee in the deliberations. It is an extremely difficult thing that you are doing. You are having to read all of the submissions and are getting a million people throwing 12 million ideas at you, generally without a solution sometimes or, alternatively, there are certainly some solutions without problems. We are trying to be helpful. Part of our purpose today is to try to answer some of the questions. We do not want to spend a lot of time going through our submission, which I am sure you have read. We had the opportunity also of talking in Canberra.

I would repeat one or two points. Firstly, in the context of the current regulatory framework it is worth remembering that it is the most comprehensively regulated anywhere in the world. In addition to the Franchising Code of Conduct—which is common in most countries, and I practice internationally—we have the misleading and deceptive conduct provisions in the TPA, and the unconscionable conduct provisions as well. No other country has that combination.

Secondly, there have been some changes in recent times, particularly in March 2008, and they have had a significant impact on the sector. I do not think that has particularly been recognised, and indeed most of the submissions that I read were from issues that well predated those matters. I will give you a couple of examples. The requirement to list past franchisees was a new requirement and that made a significant difference. Similarly, the requirement to provide information on territory history, so that if the territory or site had been previously franchised that now has to be specifically provided in a separate document, and also the tightening up of some of the financial areas so that the financial disclosure provided by franchisors now extends in a

group sense as well. They were significant changes, which have potentially been lost, to some extent, in the current debate.

The other thing to note is that the regulatory framework in Australia is admired around the world. There are two keys to it. The first is responsible franchisor behaviour, which has been the subject of many submissions. The second important pillar upon which that is built is effective franchisee due diligence. You cannot legislate against business failure. This is not a consumer contract. This is a business transaction. People are investing a significant amount of money and with that comes responsibilities. The code framework is built around assisting people in their due diligence, which means providing information, disclosure documents and so forth.

One of the things we have commented upon in our submission is the temptation every time an issue comes up to add to the size of the disclosure document. I am sure you have seen the size of some of those documents. Sometimes there is so much information there. That then impedes the franchisees obtaining advice because of the cost of obtaining advice. It is a bit of a double-edged sword. You double the size of the disclosure document and potentially you will take a whole lot of franchisees away from getting advice.

What we are saying is that education that has come out of the South Australian and Western Australian reports is probably the key recommendation in terms of consistency, yet it has a cost associated with it. We have some ideas about how we could work with the government to perhaps implement cost-effective educational campaigns, because at the end of the day people are entering into a business decision. The franchisor does not come back and say, 'I didn't expect you to make a million dollars out of this business. I thought you might only make half a million. Can I have the other half million back?' It is a business transaction and it has to be treated like that. As soon as you start to move it into a different prescriptive process you will kill off the entrepreneurial activity on both sides of the fence.

We would say that franchising is just a way of doing business. You can have licence agreements, distribution agreements, agency agreements, even employment, and what has given franchising its real zing in the Australian market is the way Australia has uniquely approached it. I do a lot of work in the United States and have travelled there two or three times a year for the last 10 years. In America franchising is essentially an adversarial relationship and there is a massive amount of litigation in the courts, and unfortunately there are thousands of franchising lawyers who just make a living out of suing each other.

When we talk about dispute resolution people talk about mediation, but one of the statistics that is worth noting is that there is very little litigation on franchising in Australia. Notwithstanding the fact that there is a comprehensive array of regulation, there is actually not a lot of litigation. In the United States they do not have the same legislation, but they have more litigation. This tends to indicate to me that we are getting it fundamentally right in a conceptual sense.

There are a number of reasons for that. The franchising relationship in Australia is essentially between small businesses. It is not big corporates. Yum v Competitive Foods-type cases are unusual. You have a major public corporation franchisee and an international franchisor. Most of the relationships are between small business. The franchisor needs to have a successful franchisee or group of franchisees to be successful. Ninety-eight per cent of franchisors in

Australia are small businesses, and because of that there is not this mythical great inequality of bargaining power in a lot of circumstances. It is a bit like—in a sporting context—a team sport. You have the coach, the franchisor, who has certain responsibilities, including saying, 'Here is the team plan. Here are the rules. You have to follow them.' There is a more prescriptive role there. Then you have the franchisee, whose role is fundamentally operational. In a conceptual sense that is worth noting.

The Australian sector is generally best practice in a number of areas, but there are areas for improvement. We are struck by the fact that you want to make a difference, which I can understand. If we can help in any way, then that is what we would like to try to talk about today. There have been some issues that have been raised previously that we would like to talk through.

We would like to distance ourselves from the comments of the ARA. With something like this you have to be wary of anecdotes and academics. At the end of the day it really is about the practitioners. We have two here today, a franchisor and a franchisee, for you to question. Similarly we need to make sure that we get the facts on the table.

I would like to lead on to the ACCC briefly. The ACCC has copped a lot of flack. In our view they are a tough regulator and we have seen quite a number of instances where they have gone in and have taken on franchise systems, and effectively in a number of cases put them out of business. There would be four or five that we could name. One franchise proprietor is going to jail over fraud. It is not true to say that the ACCC does not act. The biggest frustration the ACCC has is that people do not necessarily follow through on their complaints. They will lodge a complaint with the ACCC, but then the ACCC will ask for more information, which is not necessarily provided. Alternatively, as in a recent case where they had to come out publicly, with all the emotion of the situation the facts are actually not true. The franchisees—passionate as they are—are making some statements that are contradicted by objective fact. We have put in our submission why that is, namely, the breakdown of a business is a very traumatic situation. We did some work on this because we were struggling to find it as well. People would come to us with very passionate articulation of their situations, and then when we checked them we would find out that it was not quite so. Our psychologist tells us that is just a fundamental human coping mechanism. In the context of a traumatic situation like that, if people can find someone to blame, they will blame them. It is a bit like a marriage; people never blame themselves for the marital breakdown, it is always the spouse. It is a business marriage and that does help to sometimes explain the unexplainable, as you would see it, where you almost see two completely contradictory sets of facts.

We have looked at all of the other submissions, and I could summarise a lot of them by saying that there are a lot of personal experiences there, which we would be happy to talk through. There is one submission from an academics that has 21 or 22 recommendations as to what franchising should be like. To us, they are solutions in search of a problem. There is no particular evidence on a lot of the academic stuff about some of the things that they are advancing. If you want us to answer any of those we can, but we do not propose to do so today. What we are really looking to do is find out what the problem is, what the issues are, where the areas of improvement are and how we can help.

CHAIR—You will need to hurry up, Mr Giles, otherwise you will be the only person speaking and I have a lot of questions for you.

Mr Giles—Can I just touch on a few, because I think they might be some of yours. Let us touch on your legal contracts question. You raised the issue of take it or leave it contracts. In our view and experience, yes, there is a standard form template that typically starts up the process, but in most situations there is a degree of negotiation. The second situation is that the franchise agreements are detailed, but they are not necessarily unfair or particularly onerous and they need to be seen in the regulatory context. Also, there is a duty of good faith and fair dealing implied into the franchise relationship already. In our submission we quoted the McDonald's case as effectively the authority for that. I wanted to touch on that.

You probably want to ask some questions, so I will just lead you to one thing. We provided a supplementary submission on the issue of good faith, and you may well some questions on that. There were effectively two points that we wanted to make out of that. This is on the issue of what some people describe as good faith. I have a spare copy if you would like to see it.

CHAIR—Yes. We could table that and add it to the record.

Mr Giles—The point was to try to provide some basis for this. The first point that we want to make is that the current legal situation is clear and certain. Whatever you may think of it, it is in fact clear. It was a High Court decision that specifically states:

On expiry or termination of the agreement, the franchisee has no right to continue operating the business and no right to share in any goodwill that may have accrued to the system during the franchise's tenure.

That was in the Ranoa Oil case. That was in a case specifically about franchising in the oil industry and that was the High Court's view. Whatever view you may take as to the situation, any change that you make is overruling a High Court decision, if you were to make a change in the law. The second point to note is that that case was decided seven or eight years prior to the 1998 franchising inquiry. The point we are making is virtually every existing franchise agreement in Australia will have been negotiated in that paradigm. If a change is to be made, we would say that it would need to be prospective to give everybody—both sides of the fence—the opportunity.

We included some rough calculations in there about what the potential economic impact might be of that. We do not claim to be magnificently scientific, but there is at least some information for you to look at to see what the impact of this might be, and we worked on the upfront franchise fee as being a potential measure of that and extrapolated that out. We came up with some pretty large numbers as to the potential value transfer if you were going down that track. I am going to take your invitation and let you ask some questions.

CHAIR—I appreciate your further submission and thank you for that. In your opening remarks in your submission in terms of good faith you make a couple of points. You state:

… endeavouring to cloak as 'good faith' an explicit right to perpetual renewal of franchise agreements or compensation at the end of the franchise term.

Can I suggest to you that you are building on to good faith a construct that is not there?

Mr Giles—We are not talking about your construct, but some of the people who made submissions commenting on good faith will then go on to say things that are really not good faith at all.

CHAIR—Perhaps we can establish at the start that there are a whole range of submissions and people will say and submit whatever they like. That is fine. We accept all of that. But that is not what good faith is defined as or as others may see. You seem to take a contrary position, though, in saying that good faith is already implied, the courts have made rulings on good faith and what good faith is all about.

Mr Giles—That is right.

CHAIR—You explicitly are opposed to having good faith anywhere directly pertaining to franchising. The question I asked the ARA is: why is franchising different in that good faith should not apply? You very clearly state that.

Mr Giles—Firstly, you are talking about introducing good faith into franchise legislation but not into retail tenancies or any other legislation. In fact, you are making potentially the distinction—

CHAIR—Right at the start, I am talking about franchising. Let us not cloud it or confuse it with others. In terms of franchising, it already is implied. It already is the basis of all law. It is written in black letter law in a whole range of areas, but in your submission in terms of franchising you say that you do not want it to apply. Why not?

Mr Giles—The first reason is that until now we have had no clarity about what people mean and people have been using the term 'good faith' in a wide array. It is comforting for us to hear that you are saying, 'No, we're only talking about it in its current'—

CHAIR—I am just talking about good faith. I am not trying to add bits to it. That is why I am asking you very specifically about good faith.

Mr Giles—That is the first point. The second point is that it is already implied into any franchise agreement. For example, if you have the right to refuse—

CHAIR—You are right; it is implied. We are not trying to be fancy or clever here. Franchising systems work generally well. We accept what has been presented to us, but there are some rogues in the industry. We perhaps can weed those out, which would help everybody in the system, good franchisors and good franchisees, by having it more than just implied, that is, by having a stronger sense of good faith. It is the basis for the agreement in the first place. Why is that a bad thing?

Mr Giles—What is the stronger sense of good faith?

CHAIR—By having it more than implied; having explicit wording.

Mr Giles—But would it be defined?

CHAIR—I am open to suggestion. You tell me what you think it should be. I am not asking you how we think it is defined. In your submission you say you are against it. Tell me why you are against it. But give me some real reasons and not about retail leasing and a whole heap of other stuff.

Mr Giles—The first reason is that we are concerned that the definition is appropriate. If, for example, there were simply a reiteration of the current implied position so that it were said that in the conduct of the franchise relationship the parties will act in good faith, or something like that, then that is just a repeat of the current state of the law. If you are asking, 'Would the FCA object to repeating the current state of the law and the statutory framework?', I think the answer to that would be, no. Our concern is extending it. I think there have been disingenuous submissions to you. We have seen it even recently in respect of unconscionable conduct as well, where people have tried to define it. In WA a specific change to the law was proposed by someone to define unconscionable conduct. There is conduct in there that is clearly not unconscionable. It is really that stretch factor.

CHAIR—In your view, or in your opinion.

Mr Giles—Yes, in my opinion.

CHAIR—You are not the definitive last say, though, in what is conscionable and unconscionable.

Mr Giles—No.

CHAIR—This is your view?

Mr Giles—Yes.

CHAIR—That is fine. But we need to establish that. In the end you do not really have a problem with good faith?

Mr Giles—I think I have answered your question.

CHAIR—I do not have a clear direction as to why people seem to be opposed to it, yet not opposed.

Ms OWENS—Two people have now mentioned the lack of good faith bargaining in the retail tenancy relationship. If it was added to the franchise law and not to tenancy law how would that affect you?

Mr Giles—Take a retail shopping centre where the landlord leases to, say, the franchisor and the franchisor subleases to the franchisee. That is not always the situation, but you can take that hypothetically. In one contract you would have a good faith obligation, and in the lease it is not necessarily so.

Ms OWENS—You have vertical contracts and different laws apply?

Mr Giles—Yes. If someone chooses to distribute goods and services—

CHAIR—Is that not already implied, though, in retail leasing?

Mr Giles—I would not make too strong a point of this. In terms of a philosophical objection, we think there are bigger issues than this issue.

CHAIR—Good faith just seems to be a stumbling block in your submission and others.

Mr Wright—In one sentence I would sum it up by saying that it invites legal argument.

Ms OWENS—Unless it is uniform.

Mr Wright—Introducing something new creates a platform for people to argue about it, because it is implied in legislation already.

Senator MASON—It creates more uncertainty.

CHAIR—It is not new, though, is it? You say it is new. Again, it is this having a bet each way. I am still not getting a clear direction. If it is implied already what is the problem? How does that make it more confusing?

Mr O'Brien—I am a little concerned in making comments about this. It is like the fox being in charge of the chicken coup, a lawyer talking about changing the law pertaining to franchising. As a practising franchisor over 27 years and a franchisee also, what we are talking about is creating uncertainty. We already have a certainty with regard to good faith. We have certainty with regard to unconscionable conduct. We have certainty with regard to other aspects of the law pertaining to franchising. We have High Court decisions and other case law. Franchisors that are operating in the space or are coming into the space can do so with certainty. What you are talking about is possibly introducing a legislative solution to good faith, which in a way wipes out the precedent values that we have regarding franchising. That creates uncertainty and a feeding frenzy for my colleagues Mr Giles and his friends. I do not want to go paying lawyers any more than I have to.

CHAIR—Thank you. In relation to dispute resolution, obviously there are times when people need to resolve their issues, and regardless of how much pre-education or how good the pre-education is before you go into due diligence and so on, there will be times when people have disputes. In your view, what are the biggest problems associated with dispute resolution? Where could we improve matters there?

Mr Giles—Making it mandatory would help. There are a number of cases we have seen where franchisees in particular have refused to attend mediation. There have been other instances where franchisors have used technical arguments to potentially avoid mediation. The ACCC has a number of examples of that. Indeed, we have gone out to educate our members, as a result of discussions with the ACCC, who are saying to embrace the concept of mediation in theory and do not necessarily stick to the hard line of the fact that it might technically not be a dispute that is capable of being mediated.

Mr O'Brien and other franchisors are introducing other dispute resolution systems themselves, because no-one profits out of a dispute. It takes up a massive amount of time. There is cost. The fundamental value in a franchise system, franchisor or franchisee, is intellectual property and the one way of damaging that is to have a dispute or a breakdown in the relationship. Mediation has dramatically improved the situation from what it was. Getting it perfect will be a real challenge. With our system, for example, with the Franchise Council member standards we have other interim steps. If there is a complaint against the franchisor where the franchisor has done the wrong thing, we try to implement some peer counselling or some interim practical steps at an industry level. Nothing can really be done in a regulatory context. It is a difficult question.

CHAIR—Yes, it is. I accept that. That dispute is there. Where a dispute arises on either side, for whatever reason, where there is some disagreement there seems to be a hole in terms of how that is resolved in the true sense of resolution. It seems to me that there is a big difference between what would either be the education side of things and then the management of behaviour. In a perfect world everyone does the right thing, does their due diligence and all the rest of it. None of that will protect you from somebody who is being unscrupulous or who will behave badly. That is why we have regulations and laws. It is not about creating uncertainty. It is not about anything else. It is about trying to manage those who will do the wrong thing. The reality is they do exist.

In your submission you touched on very strong code requirements administered by the ACCC, but in the end who registers the system and with whom? If you have a franchise system no-one really knows. We know what actually takes place. No-one registers their system. No-one has their system checked. The agreement and then the operations manual can change at any point in time, which leaves a wide open gap for anything to take place. Even though there is a Trade Practices Act and so forth, the cost of going down those paths is very high. Following on from what Mr O'Brien said, we do not want to create a lawyer's paradise, but obviously sometimes people have no other option, so how do we deal with unscrupulous behaviour?

Mr Giles—I will address a couple of things. For a start, in terms of cost, the ACCC will investigate free of charge any complaint for a breach of the TPA. There is a zero cost option there to start with. That is significant. If we compare that with the American situation, the Federal Trade Commission does not take anywhere near the same level of detailed involvement. The second situation is that in the context of the relationship there are various other things that happen as well. Most systems have formal or informal franchisee advisory councils and mechanisms for resolving those sorts of disputes. In other words, the marketplace has come up with various solutions. If we try to legislate every aspect of franchising then none would take place. It is like business generally. It is an entrepreneurial activity and the marketplace has certain ways of dealing with certain things. Franchising is highly competitive in terms of finding franchisees. The process of listing all existing and past franchisees, people will be doing comparison.

There was mention before about franchisees in take it or leave it situations. The conversion rate from a franchise inquiry to actually signing as a franchisee is something like three per cent to five per cent. In other words, 95 per cent of people are going through and making a decision not to proceed. That to me is indicative of the fact that the system is working. Can it be improved? Maybe. What we do not want to see is just another tribunal set up. All that will do is

add cost. The mediation process is good because it forces the parties to sort it out between themselves.

CHAIR—You say it forces them, but in the does it really? What it gets them to do is basically turn up or not turn up. They are just coming to the table, as it were. But they do not have to do anything.

Mr Giles—No, but it is interesting.

CHAIR—Back to the unscrupulous one, we know that some of them will say, 'I am bigger than you are. In the end you are going to do exactly what I say whether it is reasonable or unreasonable. It makes no difference. I'll outlast you.' In the end, what do we do about the unscrupulous ones? Is there a better way than the mediation process now, which is just for those who really want to participate?

Mr O'Brien—You are going to a very important point. What you guys are wrestling with is the number of constituents who are coming through, the members, with complaints.

CHAIR—I can tell you that is not the case. That is not what we are doing.

Mr O'Brien—I certainly see that when we look at *Hansard* and the comments that are coming through. We are all concerned about the number of franchisees that have issues. Let me move to your point. What I have not heard in the inquiry or from any witnesses is some of the operational viewpoints.

CHAIR—If you could give us some, that will help.

Mr O'Brien—There are two issues with regard to your question. We hear a lot about when it gets to mediation, but what Mr Giles was alluding to is that there is evolving in world's best practice and in best practice franchising in Australia pre mediation steps that happen within good franchise systems. It is just starting to emerge now as best practice. It is cutting edge in Australia. There are a whole lot of early warning systems. There is a whole lot of best practice that can step into play very early when there is a problem occurring in a franchise system between a franchisee and a franchisor. I will not bore you with the detail of that, but it is now being followed by systems, shared by peers, and we are looking to do a lot more training and sharing of that information. It is starting to be built into franchise agreements. Ours has it and Fastway Couriers has it, for example. I believe that would help alleviate problems before they blow out of proportion, because it is often that a molehill becomes a mountain before they even get to external mediation.

The second point is that we note with interest in the ACCC's submission that they are suggesting something along the lines of field audits. Where they get a bit of a sniff and with their experience they know what to look for they are, in fact, doing friendly audits of franchise systems and, if they find issues, giving those systems, depending on the severity of the issue, advice, training, referring them back to us, peer support, further training and whatever it might be. We support that. We think that is very proactive.

Mr Giles—Our view would be that we want one regulator for the sector. If the committee's view is that the regulatory framework is not working, then it is a discussion that should be held with the ACCC to say, 'We need you to do these extra things.' The ACCC, on several occasions, has taken what you might say is heavy-handed action very early in the code. Arnold's Ribs & Pizza is a good example where they effectively put that system out of business. Synergy Business Systems is another one, then there was Simply No-Knead. They came in very heavily there. There are opportunities for them to come in earlier. What Mr O'Brien is saying is correct. At the moment the ACCC needs to wait on a complaint before they can investigate. We support the audit power. We have talked to them about it and we think that makes sense. What that will do is drive better disclosure documentation and better processes. We all know that we are going to get a tax audit one day, and similarly every franchise system will know that they will be audited at a point in time.

CHAIR—Do you think that there needs to be a bit more expertise within the ACCC? Do you think they need a specialist body or for there to be some attention towards franchising? I understand the arguments between the ordinary business world and then the franchising world, which is a smaller segment of business generally. There are over two million businesses registered in Australia, and a lot fewer franchises.

Mr O'Brien—Going to that point, one of the things I applaud the ACCC for is that over six years now, on a quarterly basis, they have engaged with franchising with their franchise advisory panel. There must be about 15 people on that advisory panel. They have been operating for six years. There is a teleconference every quarter, and they have members from throughout the franchise sector, including motor trades, retail traders, franchisees, franchisors, industry sector, their own people and ourselves. I applaud them for that, because that is one of the reasons the ACCC is coming up in their submission with some very positive and proactive steps. So, do they have specialists within their organisation? I think their franchise-specific knowledge is pretty savvy.

Mr Giles—Let me follow on with a suggestion. The ACCC will possibly still be focused on whether there has been a breach of the law. And there may not have been. Going forward, under our collaborative relationship with the ACCC, what if we had a problem with one of our members that we have disciplined and, as a consequence, that member sued us. As an industry body we do not have statutory protection. We have been talking to the ACCC about how we can work more closely with them to do the things that government has asked us to do, which is to sort out the consultants and those sorts of things, because there are Trade Practices Act implications with those. It seems to me that one of the things that you are saying is that, if the ACCC gets a complaint, which might not be a breach of the law but might be a bit of sharp practice, it would be good if they could just refer that to us and we could have a collaborative process where, in a peer counselling sense, Mr O'Brien or someone could—if it is a franchisor—sit beside that franchisor and say, 'Listen, that is not the done thing. That's not what you do.' It is a less formal process. It is hard for the committee to put their hands on what that might be, but the key is that it has to go under the ACCC and maybe with more of a direction to get more involved in problems with a view to necessarily finding a solution, as opposed to necessarily—

CHAIR—We might have come to where a big problem exists, and that is whether something is technically a breach of law or an abuse of power. The two are not the same thing. A lot of the problems exist within the abuse of power. For example, it is not a breach of law to terminate

somebody's franchise agreement with seven days notice just because you feel like it; you might be having a bad day.

Mr Giles—It is. It is a breach of the code.

CHAIR—It is not. No, it is not. It is in the contract agreement. People can be breached, in the end, for pretty much anything and their contract can be terminated. It is in all of the contracts. It is not necessarily a breach of law.

Mr Giles—The Franchising Code of Conduct gives a prescriptive process for termination.

CHAIR—That is right.

Mr Giles—It says what has to happen. It says that you have to give notice, opportunity to remedy—a whole process.

CHAIR—Back to the unscrupulous operators, we are not talking about the ones that do the right thing. The ones that do the right thing always do the right thing. They are fine. They are great people. They have really good successful businesses and systems. I am talking about the unscrupulous ones that get up on the wrong side of the bed in the morning and decide, for whatever reason, or any reason, they are going to use the power they have and abuse that power to terminate someone because they no longer like them. That can be a successful franchise. It is not a breach of law.

Mr Giles—It is, because it is a breach of good faith and fair dealing.

CHAIR—Did you say good faith?

Mr Giles—Yes. The implied duty for good faith and fair dealing applies. You cannot terminate a franchise agreement for an improper purpose. If you do not like someone you cannot terminate a franchise agreement. That is not true. Similarly, the code has a detailed process around that. It has been fairly comprehensive. I hear where you are coming from on this. It is a difficult—

CHAIR—Has this never happened? There are no situations where some unscrupulous operator or somebody who just does the wrong thing? I am not saying it is system-wide, either. I am sure within systems there are really good people within those systems and there are one or two who, for their own reasons or whatever, abuse that power. You talk in your submission about an equal amount of rights and an equal amount of power, but in the end contracts are fairly one sided. They have to be. In the end the franchisor has the power to terminate. Don't get me wrong. I am not saying they should not. I am trying to get some guidance from you about what you do in those situations where somebody does abuse their power?

Mr O'Brien—I could go again to a very realistic and operational response to that. It goes right to your question of abuse of power. Franchisees—Mr Melhem is one and I have been one—have enormous power. When I was a franchisee I organised considerable resistance to my franchisor, Cadbury Schweppes, with enormous success. In fact, I remember that you were on the other side. The point is that let us say the franchisor does get up on a bad hair day and does

something that is inappropriate but perhaps not outside the law. Eventually enough franchisees will get jacked off with the system that they will sell out of the system. You will find it difficult to attract good-quality franchisees because when they do their due diligence in ringing up those past franchisees they will not necessarily be talking well about the system. Over time you will get fewer franchisees applying, you will get fewer conversions, poorer quality franchisees and eventually you will kill your own system.

Senator MASON—Market repercussions.

Mr O'Brien—Yes, market repercussions.

CHAIR—That is fair enough. That might take a long time. It might not be realistic to say that, either. There are some brands that are so large it is just not going to matter. We have had evidence from some of your own people and others that in the end it does not matter who you have in there, because the brand is so big and powerful. Joe Bloggs is the franchisee and it does not really matter what their view is on anything.

What I am driving at is that there will always be some good and there will always be some bad. This is about trying to come to an understanding about where there is abuse. The reality is there are cases of abuse. You can come at it from either end, but there will always be the franchisee who shirks their responsibilities and does not provide properly within the system. There is a remedy for that. The franchisor has an enormous amount of weight within the operations manual, and in the end can terminate. That is a very powerful act. There is power there. Where a franchisor decides to go off the rails and decides that they are going to terminate someone and use bullying tactics for whatever reason—they might want to bring that store back in house and not pay for it, and there have been circumstances of that happening—how does that play? This does happen. This does exist.

Mr Melhem—I can only talk about my experience as a franchisee, as the chairman of the national Franchisee Forum, from experience of the survey and the conversation I have had with Mr Rees outside of here. I will talk firstly from the survey. We surveyed over 350 franchisees from across about 50 systems. We sent it out to all of the franchisors and asked them to send it out to their franchisees. I do not know whether every franchisor sent it out, but we do know that we got responses from about 50 systems and we had 350 franchisees responding. All of the issues that franchisees raised were about communication and working on profitability. There were never any issues about abuse of power.

CHAIR—Are you saying it does not happen or it does not exist?

Mr Melhem—No, I am not saying it does not happen or that it does happen. I do not know. I can only speak from my experience, and I can tell you about a conversation that I had with Mr Rees. If it does happen, the full weight of the law should come down on those people if they are doing the wrong thing.

CHAIR—Is that not the problem I have described? They have not breached any law?

Mr Melhem—I will just explain what has happened from my experiences. From the franchisees that we surveyed that was not an issue. I am not speaking for every other franchisee

in the country, because they did not respond. As to my experience within systems, I have operated with three Gloria Jean's stores and two Harry's Cafe de Wheels; we just opened one at the international airport yesterday. I have never had a problem or never had a franchisee in those systems who has been terminated or where the power has been abused by the franchisor. In fact, it is the other way around. I have had my franchisor—and I did say this to you before—bend over backwards to help me out when I have been in some financial difficulty.

CHAIR—I am sure there are plenty of good cases like yours. I completely accept that. I am talking about the ones that are not and what we need to do about it.

Mr Melhem—Absolutely. I was speaking to Mr Rees earlier outside, and from what he told me he has a genuine concern. I am not a legal expert to be able to complain about it, but in the majority of cases, in all my experience—other than in speaking with Mr Rees—I have not seen that as an issue.

Mr Giles—I wanted to take one point with you concerning an unscrupulous operator who has not breached any law. That is your potential contradiction in terms. If there is an opportunity for someone to be unscrupulous, surely that is going to be unconscionable, misleading or deceptive and a breach of the code. In addition, you have the franchisee association process where basically the trade union of franchisees will gang up and sort it out. You have the fact that the franchisor then has to disclose that termination in next year's disclosure document. That is a bit of a black mark. You have the ability for the incoming franchisees to ring that person up and say, 'What happened to you?'

CHAIR—In other words, you are saying you do not believe the problem exists?

Mr Giles—No. I am saying there are marketplace solutions for your problem. I challenge you on your fundamental presumption that they have not breached any law.

CHAIR—I just said 'may'.

Mr Giles—No. I am saying that the Trade Practices Act is very broad with unconscionable conduct. I think that is now broader as a result of the recent decision in Ketchell's case.

Ms OWENS—Do you see that there is any way that you can stop intentional lawbreakers with more laws?

Mr Giles—I do not think so.

Ms OWENS—Where it appears that there is unconscionable conduct is the support system for the other party adequate at that point?

Mr Giles—There are potential resourcing issues, such as a Legal Aid type of thing, and access to justice. There is a legitimate argument, and we would be happy to work with government to figure out some sort of solution. People should not be denied the right to attend mediation because they cannot afford the cost of mediation. I am aware of several instances where the franchisor has paid the franchisee's costs and so forth to actually attend. The second point I would make is that I do think that the point Mr O'Brien made before about the ACCC audits will

be significant. You will get further behavioural improvements in the sector, because franchisors will know that they are going to be potentially audited each year. I think that will do it. In terms of access to justice across business, what about in retail leasing? I know you do not want to hear about this.

Ms OWENS—I am happy to hear about it.

Mr Giles—That is a good example of another access to justice issue. It would be fantastic to have Legal Aid for franchising. We would see that giving franchising a competitive advantage, because it would give people more comfort in knowing that, if they have a dispute, there is a funding resource available for them. Does that answer your question?

Ms OWENS—Yes, it does. Is there sufficient work being done in terms of people on both sides who are unintentionally breaking the law because they are not terribly competent or not informed?

Mr Giles—As an industry body we think there is not. We would love to do more and more. If you compare it to where it was five years ago, it is a lot better and hopefully in five years time it will be even more. We continually educate our members on best practice and on ideas that are well beyond the law. That is the role of the industry body. The great difficulty in this process is that most people who enter franchising as franchisees have never been in franchising before, so they are hard to get to. They could be your next-door neighbour who is not necessarily in a system to educate. The South Australian and in particular the Western Australian governments were very keen on pre-franchise education. Even in the context of registration—if you are going to go to that step—there is an argument to register franchisees as some Asian countries do. To get a registration they have to demonstrate that they have gone through a course, read material or something like that. But do you want to get into that level of prescriptiveness in a small business marketplace? That is the real question that we juggle with every time.

Mr O'Brien—That worries me a lot. I love the idea of every potential franchisee having done a course, as was talked about earlier. In a real world, franchise inquiry rates are at a 15-year low at the moment. One of the biggest issues in this industry is attracting new franchisees, because we are in a full employment economy, and now we have got a double whammy where people cannot get access to finance. The problem with having prescriptive prior training for potential franchisees is that it will raise the bar to attracting new franchisees.

Ms OWENS—I was not suggesting that. I asked the question because I wanted to hear your response. If those courses were available, then you, as a franchisor, could decide whether you required it and when you required it. It need not be prescriptive. With the regulation as it is now, given that it is the most comprehensively regulated franchise system in the world, are there areas that are not necessary? Are there areas where a good franchisor and a good franchisee are bumping against the law unnecessarily?

Mr Giles—The biggest challenge that you have is just the sheer cost for a franchisee of obtaining advice. That is just a barrier to entry, just like franchisors have the compliance cost. Our view is that there are incremental changes. One thing we have not talked about, which is mentioned in our submission and which is allied to this, is the ACCC producing a risk statement

rather than every franchisor producing individual ones. The bottom line is that the risks are the same.

CHAIR—Can you expand on that? For example, a risk statement would say what, that getting into franchising carries a risk?

Mr Giles—Yes. For example, the ACCC, in collaboration with us perhaps, could produce a document saying: 'Don't buy a franchise and assume that you're guaranteed success. Understand that there are various risks.' People do buy a dream or a vision and that is not always necessarily realised.

Senator MASON—Or shares.

Mr Giles—Yes, that is right.

CHAIR—There are different understood risks, though, when you buy shares as compared with when you buy a business.

Mr Giles—That is right. This is like the issue of goodwill at end of term. We argued before and showed before that the current state of the law is crystal clear, but maybe not everybody understands that at the end of the franchise term if it is over then it is over. We commented in our supplementary submission that the industry average franchise agreement term is five years, but franchisees are typically in for seven years. In other words, franchisees in 98 per cent of cases are actually getting that extra term. We think that is an area that is being driven by a commercial dispute, and presumably you do not see your role as trying to arbitrate a commercial dispute between two corporations. The bottom line is whether there is an endemic industry issue in relation to non-renewal, and we would say, no. Are there any other areas? I think at the end of the day the sector has learnt to live with this regulatory framework. The size of the disclosure documents is a concern, but on balance we would see that as a barrier to entry and similarly the cost of getting advice is a barrier to entry.

Ms OWENS—There is a new system for disclosure documents, but they seem to be getting very complex already.

Mr Melhem—You asked before whether there were any areas that could be improved where there is a good franchisee and franchisor. Disclosure documents for me as a franchisee are massive. I see the need for them where there is a bad franchisor or as a protection for a bad franchisee. Where you have a good relationship between franchisee and franchisor I think it is almost unnecessary, because it costs me thousands of dollars every time I see someone like Mr Giles. The document is so thick and there is so much information there that I honestly do not read it. I give it to my lawyer and say: 'Here you go. Just sign off on it.' It has become crazy. The reality is I do not read it because I know I have a good relationship with my franchisor.

Ms OWENS—Mr O'Brien, with the disclosure documents I would assume that, if the law is right, most of the material that you would need to provide would already exist because you are a good business. You would know your failure rates. Is there anything required in the disclosure documents that a good business would not have easy access to?

Mr O'Brien—The thing that most people do not realise and does not come out in the data is that the average Australian franchise system has somewhere between 15 and 30 franchisees. The average Australian franchise system is in fact a very small business. Going right to your point, naturally in my system and any other major brand that you could imagine it is easy to lay your hands on that data because it exists in a spreadsheet or somewhere. But for the majority of Australian systems it is quite burdensome to comply with the existing disclosure document—to keep track of what happened in every franchise you have sold in the past, your past franchisees, and give them a chance to opt in and opt out. For the large brands it is not a problem; the data is available. To comply with the current disclosure document is quite timely and expensive. In fact, somewhere in our documentation we have estimated that the average cost of compliance with the new disclosure document in March was $30,000.

Ms OWENS—Could those very small businesses be a very good franchisor and a very good business without having access to those types of figures?

Mr O'Brien—It would be very simple to say, no, they could not. The reality is, having started off driving a soft drink truck in Canberra 25 years ago and building my business up to 150 soft drink trucks before I sold it, I did not have time to do those things. I had to do what small businesses do and live from hand to mouth. The reality is that it is difficult.

Ms OWENS—How many franchisees do you have now?

Mr O'Brien—I have about 300.

Ms OWENS—Are they all on existing contracts?

Mr O'Brien—I do.

Ms OWENS—If there were changes to the regulation that required changes to the contracts, assuming that they were made not retrospective, how would it impact on you to have two different sets of laws applying?

Mr O'Brien—I can give you a very real example. We just rewrote our franchise agreement this year for the first time in 10 years. It has taken one staff member dedicated for all of this year to get half of my franchisees across to the new document. I have lost the effectiveness of a full-time person. The cost would be mammoth to me. That is only to me. That is not counting my franchisees' time and for them to go and get advice from their solicitors. It would be significant.

Ms OWENS—How would it affect you if it were applied only to new ones?

Mr O'Brien—Again, we are getting into operational issues. If there were a change to the franchise agreement most franchisors would offer it to existing franchisees, too. Most franchisors try not to have people on multiple agreements. You then have multiple agreements within your system and then you have errors. I do not want to get into too much operational stuff.

Ms OWENS—Thank you.

Mr O'Brien—Keep it simple, please.

Mr Melhem—I have a question about the government perhaps appointing some sort of person to assist franchisee mediation. That is something I would like, as the chair of the national Franchisee Forum. It would be very welcome if the government could put up someone or some sort of funding to have that sort of person for franchisees.

CHAIR—You just raised a whole new area for me, which is interesting to say the least. You focused most of your attention on pre-education and disclosure as being the critical part of getting it right. I do not think there is any dispute about that because it has come from a whole range of areas. At the same time you say disclosure is too onerous. You do it, but it is a little bit too much, difficult and costly for franchisees. Mr Melhem, you are the chair of the national Franchisee Forum. You are the representative from at least your organisation, but you say that you do not even read them yourself.

Mr Melhem—I have read the first one and, to be quite honest, I don't have time to go back and read every single one. I have to run my businesses. If I was to deal with every bit of document and paperwork in my business I could not run my business. I have to work on my business and not in it. Mr Chair, have you ever run a business before?

CHAIR—Mr Melhem—

Mr Melhem—I just want to ask you a question. You need to understand what it is like to run a business.

CHAIR—Thank you, Mr Melhem. What I am trying to do is link with the FCA the bits that you are saying to try to put this together. If it is all about pre-education, disclosure and due diligence, then is it critically more important to have access to information in order to do your due diligence?

Mr Giles—That is right. The current regime may well be imperfect, but please do not change it because we are all used to it now. There is substantial cost with any change. Even the March 2008 changes had very significant costs to franchise systems. Ms Owens, I would like to pick up on your point. There is one area that would be worthy of attention, and that is the continual disclosure for people who are not franchising. In the subfranchising context, if you read the section of the code particularly affecting international franchise systems, which come in here and grant one master franchise. It is fair enough that they do a disclosure document then, but should there be a requirement for them to do an annual disclosure document when they are effectively out of the market? For example, 7-Eleven in Australia has hundreds of stores, yet their parent has to do a disclosure document every year. We are working with the ACCC on those sorts of things. There are certainly significant opportunities to reduce the compliance burden by just having better wording in the code and having a clearer explanation of what is required so that people can even start to do their own disclosure documents.

Ms OWENS—That is what I was getting to. There seems to be a common thread that those disclosure documents, even in one year or less than a year, are getting thicker and thicker.

Mr Giles—Now you have to attach every single document that is related to it.

Ms OWENS—I understand that.

Mr Melhem—I would like to clarify this and put it in context for you, Ms Owens and Mr Chairman. The question was asked by you: are good franchisors and good franchisees bumping up? That was the context to it. I absolutely see the benefit of and the need for having an onerous disclosure document to protect franchisees from bad franchisors. I absolutely support that. I just want to put it in context, because that was the question.

CHAIR—There is no problem with it; it is good. Mr Giles referred a number of times to entrepreneurs and franchisees. It is an entrepreneurial relationship. There is obviously a heap of meaning in terms of what an entrepreneur is. You are not just renting or leasing a business, brand or a licence. When you are an entrepreneur that clearly means you are building that business in partnership. I have had a look at your website and what you say on your own website promotion into the marketplace, which is basically, 'You're not buying a job, we're in this together, and you're building a business with us.'

Mr Giles—Yes.

CHAIR—Therefore, if you are building a business you own that business in a partnership, a relationship, a franchise relationship, and it has a value. I do not want to use the word 'goodwill'. I will just refer to it, but I do not want to use the word 'goodwill'. There is a market value to that business, which is understood, whatever that value might be. Is it satisfactory or whatever other way you want to describe it that the franchisor at some point has the opportunity to invoke the 'drop-dead clause', to walk away, terminate, or end the contract? We have heard it plenty of times, 'End of contact is end of contract. Five years, see you later.' Doesn't the entrepreneur who built that business have some entitlement to the value of the business they built?

Mr Giles—Whatever view you take as to that, if you take any view other than there is no entitlement, you are changing the law. That is the first point to be made.

CHAIR—Which law says that you have no entitlement to market value?

Mr Giles—The High Court decision.

CHAIR—I am afraid you are wrong, though. The High Court did not say your business has no value. You can go to it, but I have read it and I know what it says.

Mr Giles—You have an authoritative High Court decision that says something as a matter of law. You have asked me as to the question of fairness. I think they are different questions. Let us talk about how this works in practice. If you look graphically at the value of a franchisee's goodwill, in theory it would go like that over a five-year term.

CHAIR—That is going to be hard to see on the *Hansard* record.

Mr Giles—What I am saying is that mid-term of a franchise agreement, in pure economic theory, you would say that the goodwill is at its highest because the franchise—

CHAIR—Yes, I have got all of that.

Mr Giles—What works in franchising which is different from any other area is the economics; the market sorts the situation out. As a parliamentarian, you are perhaps sitting here thinking, 'How do I find a legislative solution to this potential unfairness?' What we are saying is that in 98 per cent or 99 per cent of the cases the problem does not arise at all. Secondly, the fact is that the last thing most franchisors want to do is actually end the relationship there, because they have to find a new franchisee, which is at the world's lowest level at the moment. They then have to train them, recruit them and get funding. Why in your right mind would you do that—

CHAIR—There are some people who are not in their right mind. That is the answer. What do we do about the unscrupulous—

Mr Giles—That is the Competitive—

CHAIR—No, it's not. Let us not confuse it.

Mr Giles—It is. At the end of the day a lot of the submissions have been driven by the Competitive Foods argument, and we have seen a lot about that. That needs to be transparent.

CHAIR—Let us leave them to one side. Let us just deal with the issues that we are talking about, rather than somebody else's issue. As we have heard from yourself and others, the end of the contract is the end of the contract. The expectation for me would be at the two-and-a-half-year mark I would start to run my business down so that it has zero value by the end of the it, because I am not going to have a renewal. Mr Melhem, if you say no, then you are saying that there is an expectation of it continuing. Where does that expectation come from?

Mr Giles—I think from the relationship.

Mr O'Brien—This is an operational answer, because sometimes that makes these things easier. As an entrepreneur, and a proud entrepreneur, the last 12 months I have spent as the first Australian to ever be chairman of the World Franchise Council.

CHAIR—Congratulations.

Mr O'Brien—No, this is not about me. It is actually a compliment to Australian franchising and how it is held in esteem around the world. In doing that it gave me a great opportunity to see best practice around the world. One of the terms I was very interested in is that franchisees are now being coined as intrapreneurs. It is a very nice explanation of your point. The franchisor is the guy who invented a vision, say, saw something in France, brought it back and created something from nothing. Further to your point, a franchisee has not done that—and I know I was one. He has seen an existing business and invested his home, his family and his hard earned toil in that. There are significant differences and risks. Greg Nathan, the psychologist in franchising wrote the key book on Australian franchising—and is a global authority—called *Franchise Relationships*. I can quote from his book. The first half-day of training I do for every single one of the franchisees that has ever joined our business is with regard to the relationship between us. We are in a partnership, but we are in an unequal partnership. We have different levels of risk

and we have different levels of involvement. It is very clear up front, and that is pretty much across franchising. I have never seen in my time in franchising where anybody is in any doubt about the fact that on the norm they have a five plus five-year agreement with the option normally with the franchisee to renew the second term. They know, very clearly, that I will work the butt off my business in the first term. I will get an automatic renewal at my option for the second term. I will go into the seventh year and I will then sell my business for the remaining portion. I will work hard to make an income for my family to get an ROI during that period of time, and the return, if there is any goodwill, will be a market force return when I sell my business at year seven to a new franchisee.

When I sat in on the inquiry in Brisbane, one of the other members of this committee used a very good question. He kept using the pub test, and I like that having grown up as the son of a publican. If I was in a pub test and somebody said to me, 'I've been renting this house for 10 years and I have been mowing the lawn, fixing up the insinkerator and putting a bit of paint here and there, and my landlord has come to me today and said that he is going to sell the house. I reckon I should get a share of the sale price.'

CHAIR—With respect, that is nothing to do with this.

Mr O'Brien—It goes to the absolute essence of the agreement.

CHAIR—I do not think anyone who rents a house expects to share in the sale of the house and gain a profit from it.

Mr O'Brien—Not a single franchisee that I have ever known or contacted in my 27 years, including my franchisees, are in any doubt that that relationship is all that different using the pub test.

Mr Giles—We talk about franchising as if it is homogenous. In actual fact it is not. There are franchise systems where there are no premises. Someone is just in a vehicle. Sometimes they own their own vehicle, sometimes not. Sometimes it is a trailer. Sometimes the franchisor has the head lease and sometimes it is the franchisee. The whole issue and the complexities that you are raising here for consideration are legitimate, but if you are looking at the current situation, which you may say seems harsh or tough, at least there is certainty. As soon as you change it, the amount of uncertainty that you are introducing is significant. Our recommendation in our submission is to be even more up front about this issue in the disclosure document. Put it in capital letters. Make it very clear to anyone who might have gone in with the wrong expectations. I read Competitive Foods' submission to this inquiry where they said, 'We would never have gone into this arrangement had we known.' That is not true. You cannot simply suggest that is the case after 30-odd years. The whole process, the whole structure of our regulatory framework is built on those two pillars.

Senator MASON—You mentioned before the two things that we have to be aware of are anecdote and academics. I am a former academic; I am still feeling unloved. My question is just about the law. I know Ms Owens and the chair have raised education, consultants and so forth. They are all very important, but I would like to restrict a couple of questions just to the law. The two pressure points are negotiating the contract and of course potentially renewing it at the end. The chairman has again touched on the issue at the end of contract and potential renewal. I will

put that aside. I am looking just at the beginning of the relationship. Tell me whether this is a fair conceptualisation. Mr Wright, are you the lawyer?

Mr Wright—No, Mr Giles.

Senator MASON—Mr Giles, can you tell me whether this is a fair conceptualisation? This relates to both the franchisor and the franchisee, but for the sake of this committee it is the franchisor that we are talking about. He will have to comply with good faith and fair dealing. He cannot mislead or be involved in deceptive conduct. As Ms Owens has drawn out this morning, there is a duty also to disclose various things and so forth. On the one hand, all of those things are what the franchisor has to disclose and uphold to the standards and the law. On the other hand, potentially the franchisee has to promote due diligence. In effect, they have to go out and do their homework. They need to read the documents, do their homework and prepare themselves. Is that right? Is it, in a sense, that the franchisor does all of that and the franchisee does that?

Mr Giles—That is right.

Senator MASON—That is the tension, is it not? When someone fails, the franchise will say, 'There was deceptive or misleading conduct. I was not told about A, B, C and D.' What the franchisor will say is, 'No. You're just lacking due diligence, hard work and perhaps you did not do your homework.' Is that right? Is that the principal tension?

Mr Giles—No, the tensions are not quite like that. The real tension is that the franchisee might say, 'You misled me', and the franchisor will say, 'No, I did not.'

Senator MASON—That is exactly what I am saying.

Mr Giles—It is actually an allegation or argument of fact.

Senator MASON—Yes, that is what I am saying. In other words he will say, 'You misled me. There was not good faith. There was not fair dealing. You did not disclose certain things to me.' That is what the franchisee will say. Is that right?

Mr Giles—Yes.

Senator MASON—The franchisor will say, 'No. We did. The bottom line is you have not done your homework. You have not done your due diligence and so forth.' Is that right?

Mr Giles—Yes.

Senator MASON—Is this the point of tension or has all the morning's evidence gone over my head?

Mr Giles—Conceptually you are right. I do not think a franchisor would often say, 'You did not do your due diligence.' At the end of the day the franchisor would accept that the franchisee did the due diligence. The real tension is a mismatched expectation. The franchisee has the

dream and the franchisor has their understanding. It is just that mismatched expectation which causes the tension.

Senator MASON—Rather than homework, due diligence, lack of education or lack of hard work?

Mr Giles—What drives it is that there is nothing that kills of expectation like facts. If a franchisee reads the disclosure document and gets advice, they will have an accountant or a lawyer sitting there saying, 'Have you read this bit here and have you seen the financials?' Or the lawyer will point this out. Or they will speak to the existing franchisees and they will say, 'No, here is how it all works.' The framework is there. What due diligence does is bring the expectations closer, and that is an important thing.

Senator MASON—My point, though: a franchisor will say to a franchisee, 'You didn't do your due diligence.'

Mr O'Brien—No, I agree with Mr Giles.

Senator MASON—I thought you were just agreeing with me. Or are you saying that manifests itself differently?

Mr Giles—Yes.

Senator MASON—It manifests itself not in those words or that perception but rather that the dream, in a sense, did not relate to the reality?

Mr Giles—Yes. The franchisee satisfaction survey of a few years ago showed that the highest cause of franchisee dissatisfaction was long working hours.

Senator MASON—I mentioned that.

Mr Giles—There were three or four factors. Misrepresentation was four or five on the list. It was the expectation of being in business compared with the reality of being in business. It is a lot tougher. You then have extended trading hours and those sorts of things.

Senator MASON—It is not just due diligence. It is these sorts of emotional factors on top.

Mr Giles—Yes, because a lot of these people come from being in employment sometimes to being in a business, and that is a big jump.

Senator MASON—So, they are the inherent tensions. Is there anywhere in the common law world where there is a better precedent than the current arrangement in Australia, which is less litigious and more transparent?

Mr Giles—I cannot think of any. If you look at the major systems, the US is less protected. They do not have section 52, misleading and deceptive conduct. Plus section 51A, which supplements that by saying—

Senator MASON—The tensions will be the same wherever we go.

Mr Giles—Yes, exactly.

Senator MASON—The tensions will be the same, but the law will not be.

Mr Giles—We are beyond the US. In Australia, if a franchisor makes a statement as to a future event, for example, 'I think you could earn $10,000 a week out of this store', then that reverses the burden of proof and gives the franchisee an even stronger case, effectively as a matter of law, to take that on. That is where a lot of the cases have been run. In the States they do not have that. New Zealand is completely deregulated as we speak. Singapore is the same. The UK is completely deregulated. The Australian model really does lead the way.

Senator MASON—You think it is the best balance?

Mr O'Brien—There are examples in Europe, particularly in France, where they have gone to a much more prescriptive and higher level.

Senator MASON—I am just talking about common law. It is different. That is fine. So, we agree on the inherent tensions and you said the best legal precedent is the Australian structure.

Mr Giles—Yes.

Senator MASON—Thank you.

Mr Giles—That is not to say that there cannot be improvements. We are really open to have those discussions.

Senator MASON—We discussed education and many other things. I just wanted to make sure that was clear.

CHAIR—Thank you for your extensive submission. We have run substantially over time.

Mr Melhem—Finally, as to my practical experience, I have sold a couple of stores and I have been in tough times where we have had street upgrades and we have lost half of our sales. My franchisor has actually come to the party and relieved me of my franchise fees and supported me with marketing and everything else. At that time my wife and I sold our townhouse and lived in the granny flat at the back of my parents' house. We ended up getting through that and sold that business for a substantial profit. We are currently selling another business at the moment. As to what drives us to decide to sell a business, the way our business, Gloria Jeans, works is that you sell it for a multiple, three and a half times, of your net profit. That is the value or the goodwill of your business. We decide to sell our stores not to do with the term of our franchise agreement but to do with the term of our lease agreement. Depending on how far you are into your lease agreement, if you have got two years to go, the banks will not loan against that. If you have two years left on your franchise agreement it is a different thing. I decided to sell my business based on how long I have got left on my lease. That is where the value of my business is, because that is something that is a lot harder to renegotiate or renew, especially with Westfield. The

experience we have had with other franchisees is that they have jacked up the rent by 100 per cent if you do well. I just wanted to add that comment in, if that helps.

CHAIR—It does. Thank you very much.

Mr Wright—I would like to say something very briefly.

CHAIR—I am being overly generous here. We have gone way over time.

Mr Wright—We appreciate your indulgence, and thank you again. We are absolutely open to any further discussion that you wish to have. We are looking for a path forward to deliver simplicity and effectiveness in disclosure. While we think the remedies are right for those who do not play by the rules of the game as well as they should, we are absolutely keen to try to find ways to improve both the price of access and effectiveness of mediation available to franchisees in particular. We are working already on the education angle as hard as we can. Last Friday we had our first ever pre-entry seminar. We had a good turnout and got a very strong response. We did that in concert with the ACCC and with Small Business Victoria. That is something that we will take out probably to every state around the country.

CHAIR—Thank you. We will adjourn for a short break.

Proceedings suspended from 11.20 am to 11.32 am

Evidence was then taken in camera but later resumed in public—

[12.11 pm]

KERR, Mr Ian, Chief Executive Officer, Post Office Agents Association Ltd

McGRATH-KERR, Mrs Marie, Chairman, Post Office Agents Association Ltd

CHAIR—Welcome. Would you like to make a brief opening remark?

Mrs McGrath-Kerr—Thank you for inviting us to appear before the committee. POAAL represents the owners of licensed post offices and franchised post shops as well as mail contractors and community agents. Our members are small business operators in the postal industry and rely on their industry association, POAAL, to look after their business interests. There are about 3,000 licensed—that is, privately owned—post offices across Australia making us probably the largest franchise network in Australia.

In our submission we have made a number of recommendations. However, our top three recommendations would concern a disclosure document, good faith and dispute resolution. We fully support the concept of franchising which is attractive to many small business people. We also support the Franchising Code of Conduct. In fact we have supported it from its conception onwards. I have a copy of our submission here and I am happy to take any questions.

CHAIR—Just on those three issues that you have raised, maybe you could talk about good faith first and we will explore that and then move onto the other two issues. That would be great. Could you give us your view on good faith and why it should be explicitly either in or not in?

Mrs McGrath-Kerr—Quite often good faith is non-existent under certain circumstances, so it is hard to demonstrate good faith when it does not exist. We believe quite strongly that franchises work most effectively when there is good faith on the part of both the franchisor and the franchisee, although it is fairly clear when a franchisor does not show good faith, it can work the other way as well. We are quick to own up to that. Good faith or lack of good faith shows in all aspects of a franchise agreement: in the way it is managed, the way the network is managed and the way the representatives of the franchisor deal with the franchisee.

CHAIR—Do you believe that including the obligation to act in good faith in the code for example would make a material difference to behaviour?

Mrs McGrath-Kerr—We believe it would because it would give the franchisee something to point to.

CHAIR—That would be a stronger outcome than just having it implied in the Trade Practices Act and going through the legal system, the courts and so forth?

Mrs McGrath-Kerr—I am not sure that it would be stronger but it would be more immediate and it would certainly be cheaper.

CHAIR—Can you give us one example of where there has been an issue with acting in good faith within the post office agents?

Mrs McGrath-Kerr—Just one?

CHAIR—Just anything. Just give me something?

Mrs McGrath-Kerr—We were a little bit constrained. When we got our submission back and noticed all the crossings out, we did not know today whether we were actually allowed to say the name of the—

CHAIR—In terms of your role, just from your experience, give us some idea of how you think it would practically work better to have good faith included in the code rather than just being implied and then relying on the courts? What difference would that make? How would that make a difference?

Mrs McGrath-Kerr—I will give you one example that is fairly common, and that is that many people who work for the franchisor prefer to deal verbally. They will ring a franchisee and give instructions, issue orders or put constraints on the franchisee, but will not put that in writing. Our recommendation to our members, the franchisees, is to retrospectively put it in writing back to the franchisor because they will usually be pretty quick to get back to you when they do not view it as accurate.

Many things can be changed. For instance, a floor plan of a post office can be agreed at a meeting between the franchisor's representative and the franchisee but when the franchisee tries to put it into place the franchisor will say, 'No, we did not say that at all.' And there is nothing to prove it. Good faith shows up largely in early interviews that are done with someone wanting to be a franchisee and they are told lots of things that encourage them to take up the franchise that quite often do not come to pass afterwards.

There is an increasing issue, as you are probably aware, with franchisees who come from a non-English speaking background who do not necessarily understand the wording of certain documents as easily as they might. We have expressed those concerns to the franchisor, in our case, and we are hoping that they will be picked up, but that is a real issue, and good faith could be seen to be lacking in some of those instances. Although, you could put it down to misunderstanding.

Mr Kerr—There are other instances of the franchisor not negotiating in good faith. For example, certain payments that are made to licensed post offices are what they call negotiated payments. They are payments that reflect the operational requirements of that outlet. The franchisor comes to the negotiating table with no intention to negotiate. Rather, they have an original point of view to which they will stick and they will not move from that position and insist that the franchisee eventually comes to accept that position.

Senator MASON—In your submission you say that POAAL notes that advice from the ACCC about the conduct of Australia Post towards its licensees and mail contractors would not have met the test required under the Trade Practices Act relating to unconscionable behaviour to a level for a prosecution to succeed. I understand what you are saying there. Although this is

only my first day at the inquiry, the parameters of the issues are starting to emerge. Isn't the constant problem of this inquiry that what you or the franchisee might see as unconscionable behaviour is simply a franchisor seeking business advantage? How does a legislator somehow seek to regulate that more clearly when it would seem—I think the evidence thus far is—that the law itself is pretty clear? I am not saying it is perfect, but it is pretty clear? How is a parliament supposed to overcome that innate tension?

Mrs McGrath-Kerr—Do you mean unclear with regards to good faith or unconscionable conduct?

Senator MASON—Unconscionable conduct.

Mrs McGrath-Kerr—We have just done a submission to inquire into unconscionable conduct.

Senator MASON—You might say it is 'unconscionable'. I might say, 'No, I am just seeking business advantage.' There is nothing wrong with that.

Mrs McGrath-Kerr—In our case the franchisor has some corporate outlets. About 25 per cent of the outlets are corporate and 75 per cent are franchisees. However, the franchisor will restrict certain products to corporate outlets, thus reducing the income made by franchisees and disadvantaging customers who obviously find it a lot easier to access the 75 per cent rather than the 25 per cent—

Senator MASON—Sure. But if they tell you that in advance, what is wrong with that?

Mrs McGrath-Kerr—It is not usually told in advance.

Senator MASON—Clearly if it is not, it should be.

Mrs McGrath-Kerr—I could not agree more.

Senator MASON—Isn't it?

Mrs McGrath-Kerr—No. New products are being developed all the time—

Senator MASON—Hold on. We are at cross purposes. What do you mean? Do you mean new products coming onto the market are not given to you? What part of their contractual obligations is not being met?

Mrs McGrath-Kerr—I do not have a copy of the LPO agreement here with me but it says that both parties will work to mutual advantage. It does not say in the LPO agreement that the franchisor will keep from the franchisee certain products. It does not say that in the disclosure document, either.

Senator MASON—It will not necessarily say that. It might simply say that products will be given to franchisees at the discretion of the franchisor, and that is still fine. You see my problem—

Mrs McGrath-Kerr—But it does not say that, either.

Senator MASON—You have to point out to me that there is something in the contract which, if it is not being upheld, then there is a legal action. Either there is a cause in law or there is not. What we have heard so far is that there is not much dispute about what the law says; the problem is the enforcement aspect which is difficult for franchisees. I accept that. It might be very expensive to take an action in court, et cetera. Maybe there needs to be mediation, an ombudsman or something else, but if you are asking us to look at what the law says, is there any problem with what the law says?

Mrs McGrath-Kerr—I hear what you say and I think I understand what you are saying. But there are two issues here. There is the law and there are processes that can happen before you get to court on something. As you noted just then, it is very costly for a franchisee to take anything to law.

Senator MASON—It is expensive for everyone to take something to law. I used to be a lawyer. I know it is. It is appalling. We all know that. I am not suggesting that is wrong. But our problem is looking at what the law is. As the chairman has said, there may at times be disreputable people and rogue people. It is sometimes hard to legislate to catch them. My point is if you can point to something where a contract has been broken, fine. It is very hard for legislators to in a sense divine in any particular case what you think is unconscionable and what another party simply thinks is tough business practice, or at least an attempt to secure their own business advantage. It really comes down to people understanding their legal rights.

Mrs McGrath-Kerr—If a contract is broken—

Senator MASON—Fine, there is an action.

Mrs McGrath-Kerr—We do not view it as fine.

Senator MASON—No, I am not saying that is fine. I am saying it is fine in terms of we know where we stand legally.

Mrs McGrath-Kerr—The LPO agreement, which is a legal document, has certain processes within it so that the franchisor can lodge a default notice against a franchisee. There is a dispute resolution process which can be initiated by either party. However, when it is initiated by the franchisee the franchisor does not—and I have never known it in 15 years—have to adhere to the time frame of the dispute resolution process. To me, that is not acting in good faith—

Senator MASON—If they have not acted within the time frame set out within the contract, they have broken the contract—

CHAIR—No, it does not work that way. I am sorry to interrupt, but it has nothing to do with the contracts. The contract is just a simple document which says the two shall enter into an agreement to operate a franchise—

Senator MASON—Do you mean the actual—

CHAIR—Then what happens is there are operational manuals and a whole heap of processes—

Senator MASON—Okay. Are you talking about the operation manual, are you? This is my first day in the inquiry? Can you explain it to me?

Mrs McGrath-Kerr—It could indeed be the contract itself or it could be one of the—

Senator MASON—Where is the problem? Can you tell me where the problem is? Is the problem with the law or its enforcement?

Mrs McGrath-Kerr—We would rather not get to the law because what we are hoping—

Senator MASON—So, it is enforcement.

Mrs McGrath-Kerr—is that things get resolved before they get to the law.

Senator MASON—I hope that, too.

Ms OWENS—You have a lot of members, 3,000 or so.

Mrs McGrath-Kerr—We have.

Ms OWENS—Are there are a lot of problems? Is there an endemic problem, do you think, or are there patchy problems?

Mrs McGrath-Kerr—We are in the fortunate position that we negotiated the LPO agreement with Australia Post back in 1991-92. It predated the Franchising Code of Conduct but we insisted that it have a dispute resolution process in it, bearing in mind that our members had been operating under a variety of different contracts before that. So we drew them all into one, which made a very impressive contract which has only had two changes since then, one of which was necessitated by the introduction of GST. It has been a strong document which has stood the test of time. We knew from experience that the dispute resolution processes had to be strong but they also had to be quick and they had to be inexpensive because no franchisee can afford to spend too much time away from their business. Finding someone else who is competent to run your business that you trust implicitly and who indeed will not breach your contract while you are aware from the job is in itself a cost. Quite often the dispute may be heard in a far, distant place. If you were running a business in Bourke and you had to travel to Sydney for a dispute resolution process, you can add at least two days onto it for travel plus you have got accommodation expenses and so on. We recognised that and we tried to have things resolved at the lowest possible level. However, it did not take very long for Australia Post managers out in the field to realise that they could actually string out the dispute resolution process, which has been done. Some dispute processes which should have taken two or three months at the most have taken three and four years. This is just not good enough.

Senator MASON—Is the problem the actual enforcement and the actual practice?

Mrs McGrath-Kerr—Yes. But there is no enforcement as such—

Senator MASON—I understand that. I understand your point.

Ms OWENS—Yes, and that is my question. When that starts to happen, what kind of support system should there be? What kind of mechanism do you need; what changes do you need?

Mrs McGrath-Kerr—We believe that there should be penalties against a franchisor who does not adhere to a process that is timed unless both parties freely agree to an extension. There is provision for that within the dispute resolution process that we use which precedes that which is under the Franchising Code of Conduct, which of course is the OMA.

Senator MASON—In other words there are penalties against both the franchisees and franchisors?

Mrs McGrath-Kerr—I do not see why not, as I have never known a franchisee to break it, so I think we could safely say that.

Senator MASON—But you are saying it should cut both ways?

Ms OWENS—The code does not have sufficient enforceable sanctions; is that what you are saying?

Mrs McGrath-Kerr—I am sure there would be enforceable sanctions were the franchisee prepared to go to court, but the matter might be over something that might not even involve money. Let us say it involved whether you wore a uniform on a certain day or it might have been a matter involving $250. You are not going to spend $5,000 on a one-day mediation to prove something like that. And the franchisor knows that. Having said that, the people at the top of the tree in the franchise operations say all the right things. They speak the right language. They talk the right talk. But when it actually gets out into the field to be implemented, there is probably a lack of training with certain people. There is certainly a lack of understanding. Most of them are a tad too bureaucratic for our liking. We would like to see the franchise as a whole take on people who were franchisees, who have left the business, and take them on as a network capacity, or something like that, to help because there is a big gap in understanding between the people who are managing a franchise and the franchisees themselves, who are small business people.

CHAIR—Can you give a view as to the most critical area that you see with your post office agents and Australia Post as to what would be the simplest remedy for dealing with disputes and getting on with the business of what you do? What would be the most critical way for us to address some of those existing issues?

Mr Kerr—It comes back to what we were discussing before as to good faith. At present when Australia Post comes to negotiate, for example, a payment. I will take that example because it is easy to conceptualise. There is no obligation to negotiate in good faith. Similarly, when we come to the resolution of disputes, it can very easily be that the franchisor can come to a dispute resolution with a set position and be unwilling to engage in any sort of genuine mediation. When I say ‘genuine mediation’, I mean the push and pull that might occur between the two parties. There is certainly no moving the immovable object. When a franchisor decides to be an immovable object they set out themselves to maintain that position knowing full well that they

have deeper pockets than the franchisee, it usually results in either the franchisee walking out, as has happened, or the franchisee accepting a position that is not to their advantage at all.

Mrs McGrath-Kerr—When the parties come together at the beginning of a mediation, it is absolutely vital that both representatives have the authority to make a decision and have the authority to be flexible. When in our case a franchisee deals with a franchisor representative who comes with a stated position and will not move from it, the whole deal becomes pointless. That would be something that would be an absolute major benefit not just for our members but for all franchisees if at mediation there were flexibility.

CHAIR—In summary, really you are saying there should be good faith; a better mediation process which compels people to actually negotiate in good faith; a proper dispute resolution mechanism and more power in terms of the ACCC to actually deal with those issues before they get to a court would go a long way towards assisting the system?

Mrs McGrath-Kerr—It would. Also, as we noted at the beginning which we have not touched on, there is disclosure documentation. We believe very strongly that the disclosure documents should be more specific to the outlet itself. We do not want the pile to get bigger, as an earlier speaker said, but it is very, very important that the disclosure document is outlet specific.

CHAIR—Thank you very much.

[12.34 pm]

PICCOLO, Mr Tony, Member for Light, Parliament of South Australia; member, Economic and Finance Committee, Parliament of South Australia

CHAIR—Welcome. Would you like to make a brief opening statement?

Mr Piccolo—I am authorised to speak on behalf of the parliamentary committee of which I am a member. I have prepared a small table summarising the issues that may help the committee members to outline the argument I wish to put today. I thank the committee for making the time to hear me. By way of introduction, I wish to reaffirm that it is my committee's view that franchising is an important part of the Australian economy and that is why it is extremely important that we establish a legal framework that allows it to prosper. That underwrites my submission today. Having said that, it is also important to provide the necessary safeguards to protect any abuse of power within that industry.

The franchise relationship is different to a normal small business relationship and, as such, it needs its own framework because the power relationship and the relationship itself is different to a normal small business enterprise. It is my contention and also the contention of our committee that in context franchisees have fewer protections and safeguards than an employee would in an industrial environment. Having said that, it is important any changes to law, whether it is the code or the Trade Practices Act, should not unnecessarily interfere too much with the fundamental contract law. We appreciate that this committee should make recommendations to improve their regulation of industry but at the same time we appreciate that you cannot change contract law to an extent that would actually undermine the fundamental principles of contract law in a democracy like ours.

It is also true that we do not want an industry equivalent to the sub-prime industry in America which was left unregulated and has caused chaos throughout the whole economy. The proposed changes by my committee will importantly deter rogues and charlatans from entering industry and equally will perhaps force out those rogues and charlatans so that we have an efficient, effective and competitive industry. That is our aim: to have an efficient, effective and competitive industry. In the main, most franchises operate ethically and well, but equally it is that smaller number that could actually undermine industry beyond their numbers.

It is also important to note that ultimately you cannot protect people from making bad decisions. If a franchisee makes a bad decision you cannot do much about that. What franchising is about is making an investment. Our other contention is we have so much law and regulation protecting people who invest in share markets, et cetera, yet we do not have similar legislation protecting people who invest in small business. Sometimes the amounts people invest in franchising are a lot more than people would invest in the share market, yet they have less protection.

Equally, a franchisee should be able to rely and act on information provided to them in the same way as securities law protects investors from misinformation. They are the introductory

comments I would like to put on the record. Feel free to interrupt me at any point if you would like me to clarify anything or ask any questions?

The documentation I have provided summarises some of the key points which my committee made. I have broken it up into different parts of the relationship because they have different elements. In terms of the pre-contract arrangements, in other words the industry generally, our view would be that the recommendation at page 35 of the report about better disclosure would actually enhance decision making by potential franchisees. The benefit of having a better disclosure document does not necessarily mean a bigger document but it goes to issues which are important to the franchise of that industry and ensures that they are disclosed—

CHAIR—In relation to disclosure, let us call it 'better' information, not 'more'. What would it actually do to have better information? Give us an example? What would be better disclosure that would better inform and perhaps mean that a person wanting to get into a franchise system actually does not go through with it? Because they have been given more information—better information—they go, 'No, this is not for me.'

Mr Piccolo—I have actually worked with a number of franchisees who have had difficulties. That is how the South Australian committee actually arose. The franchise documents I saw said very little about how you deal with when the franchise relationship goes bad. What is it you do and how do you part in a way which is fair and equitable? They are just silent on that. A person goes into this agreement not really understanding if the thing goes sour how you extricate yourself from that. That document had a lot of other things but did not actually make provisions about what happens when the relationship breaks up.

It is no different to family law. That is why we are now moving to pre-nuptials. When things go bad you have some guidance as to what happens when you depart. We would argue that the sorts of things that securities law have should also be in this sort of code because people are making an investment. It does not matter how you dress it up; whether you invest in shares or you invest in a business, people are investing to make a return on their money. It is a different format but the same principles underlie that. That is one example.

It is important also that the franchisee should understand the reasonable risks involved. You cannot predict a lot of things, but a franchisor who enters a market knows what the risks are to their business. There should be some discussion around the risks in terms of actually just highlighting those issues a franchisee should think about and put their mind to before they sign a document.

CHAIR—Let us say we have better disclosure which deals with how things terminate or end. Would that not be a material change of existing contracts? We have got contracts in place; people have signed agreements; they have got a bargain in place. Do we introduce through the code the requirement for people to disclose a process at the end? I am sure some contracts do disclose that and others do not. Some systems do have a detailed description of how to terminate or how they end. Would setting a blanket better disclosure which would deal with that end up modifying the behaviour or do you still end up with the same problem that there are still rogues out there who use other factors?

Mr Piccolo—I think I know what you are trying to say, and you are quite right. My view would be that good franchisors have those sorts of provisions in the existing documentation already and there is no problem with those. It is the ones that do not, and I think we need to identify those. You are not changing the contract at all, because there are things in most contracts that would say that. For whatever reason, some franchisors in industry choose not to have these provisions in their documents. We would recommend that it be mandatory so everyone is on a level playing field. In other words, everybody knows what the product is that they are buying. A lot of them do not actually know what they are buying, because you do not know what you are going to get at the end of the contract. With most ordinary contracts, say, you are building a house, you pay X amount of money and you know what you get. You get a house at the end of the contract. A lot of these agreements do not have those provisions.

CHAIR—Would knowing better what you are actually buying prevent disputes?

Mr Piccolo—It is a case of minimising the risk. I am not going to suggest today that any proposals we have are going to be 100 per cent foolproof. I am not even suggesting that. What I am suggesting is that people understanding what they are getting into may help them make a better decision. In other words, 'Okay. This is what I get at the end. I am not sure. This is a bit risky for me. I choose not to enter this franchise.' It is about improving the decision making mainly for the franchisee. Some franchisees should not be in franchising. They are there because they have been sold by some motivational speech: 'You can be your own boss. You can work your own hours.' They do occur. My office has received those phone calls. We have had people trying to sell a franchise to my office. I am not sure why they rang me, but they did. I was invited to one of these motivational talks. That is how they sell them. The adverts say 'No experience required', which is just not correct. It is a lot of hard work to make a business work. It will not eliminate it, but it will hopefully assist in the process of minimising the damage to individual lives and to industry itself.

In terms of the documents, we believe that the disclosure documents should be registered for two key reasons. Firstly, it enables a regulator to make sure that it complies with the code. That does not mean it has to be a good business or a bad business. It just means it has to comply with the statutory framework that is provided so that the regulator can look at that. Secondly, it actually improves competition. If you can go to a web page and see what is on the market you can compare franchise system A with B, C and D and you can make a better decision. Often people who enter a franchise end up buying the first one who has come to them—what is available at the moment. The idea is to make that industry more transparent and much more efficient and to improve competition in the industry so that you actually have better decision making by potential franchisees, which means you have a better industry. When you put the disclosure document on the web page, for example, you are not putting up any intellectual property. The intellectual property is in the operating manual. That will still become a confidential document between the franchisee and the franchisor. What you are putting up is the document which says, 'This is what our system is about', et cetera, but not necessarily the operating manual details.

CHAIR—Does the operating manual then circumvent whatever might be in the contract in the view that the manual can ask you to do all sorts of things, take on all sorts of activities and make expenses, and that can change pretty much at will?

Mr Piccolo—The manual is a bit like regulations; it is subject to the act above it. You have policy, you have regulations and you have the acts. That is the order of how things happen. The manual has to operate within the context of the contract and also the disclosure document.

Senator MASON—This is then part of the contract?

Mr Piccolo—The operating manual?

Senator MASON—Yes.

CHAIR—It is actually deeper than that. Just for clarification—

Senator MASON—That is why I raised the issue before. I thought it was. You have the contract and below that as a subsidiary part of it you have—

Mr Piccolo—Yes.

CHAIR—But if I am right there is also attached to the contract newsletters, verbal communication, communiqués, memos, letters and any other form that forms part of directions—

Mr Piccolo—That is right.

CHAIR—It can be absolutely anything at all.

Senator MASON—Isn't it part of the contract?

CHAIR—But it is not contained in the contract. It is not contained within the contract.

Senator MASON—Yes, but it is part of the contract.

Mr Piccolo—The answer is, yes. I agree with you, yes. That is why it is important to get the disclosure documents correct. As I said, in terms of analogy, the disclosure document is a bit like the situation with an act. If the act is right then the regulation is all right, et cetera. You need to get the disclosure document right and that is why you need to actually register that to make sure the framework is correct. You have the operating manual and, as you said, other documents that are part of that contract, but they have to be consistent with the disclosure document. If you get the disclosure document correct, the documents below it have to be consistent with it. That is why the disclosure document is so important, to get it right.

CHAIR—The difference being, and I suppose the point of contention, that the contract is not going to change let us say on a weekly basis but the operating manual could or the letter, memo or other direction could change daily. There are no rules as to how that applies. The contract does say 'subject to' and therefore it can change at any time?

Mr Piccolo—That is correct, but it also means that it still has to be consistent with documents above it that control it. Another thing in terms of pre-contract is that we would argue that there is a place for better training and information in industry. The FCA does extremely well for the

franchisors. I am not sure what they said today but from what they have put to our committee my view is that the FCA does not represent industry. It does represent the franchisor and does that very well. In terms of representing the interest of franchisees I will contend they do not do that part of it so well. That is fine. There is no problem with that. It is very hard to find an association that looks at both ends of the contract. But in terms of the franchisees, what is available to franchisees is not as good as what is available to franchisors. I think that needs to be addressed. Again, it will not resolve every problem in the industry, but it will certainly assist in making people think twice about signing up. In this country I am not aware of any accredited program for franchisees. There is only one in New Mexico in America, which is an accredited program where you go along and you do a program. It walks you right through the steps of managing your own franchise. We may need something similar here to make sure people do it right.

In terms of the contract itself, we would argue that continuous disclosure is important so the franchisee knows where their business is, because they are both a business in their own right but are part of the franchise. I will give you an example of the Kleins liquidation. When Kleins were going through the hoop as the franchisor there were franchisees still buying new stock as that was happening. They just did not know about it. They actually had new stock and then they all closed down. These people were hurt even further than they were required to be hurt. It is important—

CHAIR—In terms of continuous disclosure, it is an onerous task to disclose in the first place, but what about the continuous disclose on a 12-month basis or as a new event occurs? What is your view on that?

Mr Piccolo—The FCA put the view about compliance costs and I think they exaggerated those compliance costs. For example, as to the disclosure documents, everything is electronic these days. It does not take much to actually send a document to the ACCC or whoever to be put on the register. You can effectively send your compliance costs in an email. What they are really arguing about is they do not want accountability, and quite frankly they should be accountable. A franchisor should be accountable for the behaviour of impacts from other businesses. Businesses are audited regularly. But also businesses directly have a requirement to report to make sure they are not operating if they are not liquid. That is a company law. They need to report that to regulators. Why can they not extend that to include reporting to the franchisees? The compliance cost is minimal because they have to do that by law to company regulators already. You just extend that provision to your own people in your own group. Again, compliance costs are very minimal. I think they are more concerned about the image of the business, et cetera, which is valid, but it is not about the compliance costs. That is misleading.

As I said, contracts should address exit issues and payments. We do not argue and we cannot support a view that says there should be automatic renewal of contracts, because that is a fundamental change to the law of contract. If you go into a business for five or 10 years you know what you are going in for. We would argue that is reasonable. What we are saying, though, is that when you sign a contract for that five, 10 or 20 years you should know what you actually walk out with. You should know that when you sign up, not have to fight it out at the end. That is not provided for at the moment. The parties should adhere to that. We are not saying the code should say what it is. We are saying that when you sign a contract you will discuss these issues and make sure it is catered for in your contract. That should be mandatory, because you try to minimise disputes at the end of a contract, and you know what you walk out with. It would be

wrong for us to say, 'Issue this form or that form.' That is inappropriate. But it is appropriate for the code to say, 'Your contract shall address this issue in some way.'

Senator MASON—One of the other witnesses mentioned set-up costs, ongoing costs and exit costs should all be disclosed.

Mr Piccolo—When you exit, for example, the parties might say, 'We will agree up front that the formula will be that when we cease as an exit payment you will get 10 per cent of six months returns' or whatever formula they agree to. That is still theirs. That is up to the parties to freely contract to, but it has to be addressed. Most of the ones which go bad do not address that. That is why you spend a lot of time in courts in disputes, et cetera, because it is silent.

In relation to good faith and fair dealing, we would support the provision in the code for explicit good faith and fair dealing. The reason we say it should be 'explicit' is that it is implied in law already. Given that it is implied in law, the difference between it being an implied provision and an explicit provision is that an implied provision can actually be written out. It is still there but it has to be fought for in the courts. An explicit provision states up front the standard of behaviour we require. I think it was put today that good faith is in the act applying today. No, that is not correct. The law does actually recognise good faith dealings already and it is made quite clear by the court cases, but it is an implied good faith and fair dealing. We say it should move from being implied to explicit under the statutory requirements. Up front that promotes good behaviour rather than trying to remedy bad behaviour.

Senator MASON—Does it change the law?

Mr Piccolo—No. It makes it easier to enforce, because the courts already recognise good faith dealing. They actually say there are a number of cases at the Federal Court level and Supreme Court level that say, 'This is what we understand good faith dealing is.' It is implied in contracts. We are saying it should be statutory, which makes it easier to enforce and to see. An example of that would be Ketchell's recent case. The importance of Ketchell's case is that it provides the grounds for a section 87 remedy under the Trade Practices Act to be available. By introducing good faith it actually says it provides a cause—as you mentioned earlier—for action. Then the existing law provides the remedies. It moves it from the implied to the explicit. This is the behaviour you do and these are the remedies. So, you do not have to this in a convoluted way. It is much more direct.

CHAIR—It does not retrospectively change contacts or anything else?

Mr Piccolo—No.

CHAIR—It is already there. It is already implied. It is just about making it more clear and up front?

Mr Piccolo—That is correct. Also, good faith promotes business integrity and ethics, which I think we should all aspire to.

CHAIR—You have stated that franchisor rebates or benefits ought to be disclosed. There are other views that that is commercial-in-confidence or that it would provide an unfair advantage to

competitors to know what their rebates are and so on. Do you have a view on that—rebates, discounts and so forth?

Mr Piccolo—Our view would be given that the franchise relationship is a mutual relationship, in other words, we actually rely on each other to succeed, and we rely on each other to behave well and to be honest with each other to succeed because either one can actually upset the other. We would liken commissions such as that to secret commissions. In a lot of business these days secret commissions are already outlawed. In a lot of areas of business today, if you obtained a secret commission, in partnerships and other areas, it is outlawed. It is an offence. Why shouldn't it be disclosed? It will happen. Why shouldn't it be disclosed in this case? If my business is going to be set up in this particular shopping centre, if I know that one of the motivating factors for my franchisor is that he gets a kickback, I might say, 'Hold on. Is this good for your business or is it better for my business?' That information allows me to make a better decision about which shopping centre I will go to.

CHAIR—You are saying that there should be disclosure that it happens rather than disclosure of the amount?

Mr Piccolo—Yes, disclosure that it happens.

CHAIR—You also state that we should require disclosure of leases as well.

Mr Piccolo—Yes. I got a phone call about this today. Apparently there is some law in Ontario. One of the issues raised was where the franchisor is the head lease in a shopping centre and then the franchisee operates their business in this shopping centre, often the franchisee in the green site actually fits out the site. The franchisee takes all the risk in terms of the capital. All the franchisor does is actually take a head lease. They may also get some kickbacks on that. If the franchisor goes into liquidation, goes through the hoop, the contract is between the franchisor and the shopping centre, and the franchisee gets pushed out. They have no remedy. They lose all of their investment. Although I have not been able to verify it, I got a phone call today telling me they have apparently done this in Ontario, and apparently very easily. Our committee would argue the franchisee should also be a party in some way or be recognised in some way in that lease. If the franchisor goes through the hoop the franchisee should be in a place to have the first right of refusal to maintain that site and to perhaps rebadge themselves but still protect their investment. They would lose everything. People can spend up to $400,000 to $600,000 to fit out a small suburban outlet. They could lose all of that within a five year period—the whole lot—not through any cause of their own but because the franchisor goes through the hoop. At the moment the law does not protect them at all. There is no protection for that investment. Recognising them through some lease arrangement gives them a chance to survive should the franchisor go through the hoop. It will not guarantee it, but it will give them a better chance to survive.

CHAIR—In terms of the dispute resolution mechanism, can I ask you your view and what would make it work better?

Mr Piccolo—In terms of dispute resolution, there should be a process of mandatory participation. We believe that the existing—

Senator MASON—Mediation?

Mr Piccolo—There should be compulsory mediation. That is only a first step. The evidence given to my committee and the evidence I heard back from research is that that is inadequate. The current code requires you to attend mediation. It does not require you to attend mediation in good conscience or in good faith. Unfortunately, in reality that is how it is treated in practice. It requires you to participate in a process. If you drag the process out as a franchisor your position to bargain with the franchisee is strengthened. You weaken their position even further than it is already. There has to be some discussion about good faith dealing, time frames, and there should be some process of arbitration. It might be an ombudsman, but there should be some specialist arbitration. It is going to be meaningful, the key to dispute resolution is making it quick and efficient and cost effective. For a lot of franchisees going to the Federal Court to get a remedy is out of their reach. They do not have the resources to fight in the courts. A lot of franchisors know that and that is why it is dragged out. A lot of franchisees are actually sent to the wall before the mediation is completed. Any system of dispute resolution has to initially try to mediate and get the parties to resolve their own problems, which I accept. Failing that, there should be some sort of third-party involvement that can resolve that process in a speedy way.

Senator MASON—Backed by law?

Mr Piccolo—Backed by law, of course. In the absence of law it will not happen. Voluntary codes are wonderful, but they do not often work, particularly for the group of people we are trying to deal with. What we are proposing is not trying to deal with people who do the right thing. We are trying to deal with the people who do the wrong thing. That has to happen, in our view. Finally, I know Senator Mason has an interest in unconscionable behaviour.

Senator MASON—I am a politician; of course I do.

Mr Piccolo—My view is that the law in terms of unconscionable behaviour is inadequate at the moment. It is the law that needs to be changed. It is also true that the process of getting there is inadequate at the moment, but if you changed the law it would improve. The law at the moment focuses on procedural unconscionable behaviour. The courts deal with that in a very narrow, strict way, getting back to the common law history where people doing business freely should be able to resolve their own disputes. That is where it starts from. We argue that the actual unconscionable behaviour should be defined in the act itself. At the moment you deal with procedural issues. You should actually deal with the substantive issue itself. The act does not do that at the moment. It does not define what unconscionable behaviour is. We would argue that the definition provided by Professor Zumbo is one we can support and would allow for the appropriate direction.

CHAIR—Thank you very much for your time and your submission.

Proceedings suspended from 1.02 pm to 1.31 pm

HACKETT, Mr Rodney, Private capacity

CHAIR—Welcome. I invite you to make a short opening address.

Mr Hackett—I am looking for some badly needed and overdue reform by parliament and would ask that not only this inquiry but parliament itself adopts a far more proactive attitude to these things than it has shown in the past. There have been many inquiries in the past and there have been only minor changes made. Perhaps I can ask those who are new to this inquiry process to have a look at all the other *Hansard* reports and submissions by witnesses at past inquiries and compare them to the ones we made in this inquiry and see if any change has taken place.

CHAIR—Do you want to make any remarks in terms of your submission?

Mr Hackett—No. I said it all in the submission. I am here for you to examine me. One thing I might ask about is I am just a bit confused about the process. I am not sure if I am entitled to get straight answers on this, but I will ask. Please forgive me, I am a little bit deaf and I am all clogged up with the flu at the moment.

CHAIR—Sure. You are concerned about the committee process?

Mr Hackett—What I was going to ask about was that I noticed what you call 'expungements' and what I call censorship has taken place in a lot of the submissions. To my knowledge that has not taken place in past inquiries. I am just wondering why that has taken place?

CHAIR—This is a Commonwealth inquiry. None of the other inquiries have been the same as this one. The decision was made that where an adverse comment is made about a party that party has an opportunity to respond. Where we can avoid that, we do, particularly where it makes no material difference to the inquiry process itself.

Mr Hackett—Of course, a lot of the gravitas is knocked straight out of a submission when names are knocked out.

CHAIR—Thank you. Can we deal with—

Mr Hackett—Can I ask one more question? I am just wondering how free the inquiry is. Can I have a copy of the audio transcript as well at the end of the inquiry? I have noticed some very poor quality—

CHAIR—It is a completely open and free process. Hansard is available to the public as will be the report—

Mr Hackett—I would like a copy of the audio inquiry please?

CHAIR—I do not see any reason why that is not the case. We will make some inquiries as to whether you can get a copy in audio.

Mr Hackett—Tones of voice I have heard this morning that came out of the hectoring and badgering of some of the people concerned me.

CHAIR—It would be helpful if we could just deal with the submission.

Mr Hackett—Have I upset you? You sound like you are cutting me short. I am happy to leave now. I am just here because you asked me to come along.

CHAIR—I am not cutting you short at all. I am just trying to deal with the substantive issues of the inquiry rather than—

Mr Hackett—As I was.

CHAIR—It is a completely free and open process—

Mr Hackett—It does not sound it like it so far, but please proceed.

CHAIR—This is a public hearing. Members of the public are here and present as are the media. It is completely free and open. I am just trying to deal with the issue of time. The biggest issue we have is not the public nature of this. This is a very public process, an open process; it is how much time we actually have to give. As you may have noticed in this morning's deliberations, we are actually running out of time. We are just trying to deal with that. I am trying to give you as much opportunity so you can actually talk about the substantive issues rather than deal with the committee process, which is available—

Mr Hackett—I understand. You gave a lot of time to the Franchising Council of Australia, but please proceed.

CHAIR—I am happy to talk all day about all of that, but we will run out of time very soon for you—

Mr Hackett—Of course you will.

CHAIR—which will mean you will not get an opportunity to speak.

Mr Hackett—That is okay. I am happy to leave now if you want. It might give you some more opportunity.

CHAIR—You are under no obligation or pressure. I am just here to happily say—

Mr Hackett—You were pressuring me, but please proceed.

CHAIR—Can I assure you we are not pressuring you in any particular way.

Mr Hackett—You were, but please proceed.

CHAIR—You are free to go any time if you feel that somehow we have put you under pressure. We are just trying to deal with the substantive issues—

Mr Hackett—Please proceed.

CHAIR—of the inquiry and the terms of reference. I am not too sure, but okay. Perhaps you can give us some indication. You talk about fair franchising standards and the need to establish a proper basis for determining fair and reasonable conduct within a franchising arrangement. Maybe you could just elaborate on that. I know it is in your submission.

Mr Hackett—It is.

CHAIR—You are free to speak.

Mr Hackett—I actually put it all in there. I am not sure whether all the members of the inquiry have read the submissions. I understand you and Mr Mason—

CHAIR—Maybe if I explain to you the process, we will actually get through this in a more efficient manner.

Mr Hackett—Yes.

CHAIR—We have your submission and we have read your submission and it will form part of the committee's deliberations. The opportunity to have a public hearing for you to come and talk to us is that in the free exchange of conversation things that are not written in your submission may come out or we might be able to explore certain factors. We have your submission. We thank you very much. There was a lot of effort in it. It was quite comprehensive and we very much appreciate that. The opportunity you now have is to add weight to areas that you feel are those that concern you the most and an opportunity for you to discuss with us directly in a public forum which is open to—

Mr Hackett—Thank you. I do appreciate that. If you want me to perhaps give you a bit of an overview of what I have already said, I can certainly do that.

CHAIR—That was the invitation at the beginning to make some opening remarks. Please go ahead, thank you.

Mr Hackett—From my viewpoint there is a problem immediately with the whole issue of franchising being dealt with under the Trade Practices Act. It is an inappropriate act. The Trade Practices Act is all about independent contracts, not dependent contracts. It is all about business-to-business relationships, consumer-to-vendor relationships and trying to free up the market to ensure that no-one monopolises it or otherwise thwarts the marketplace. Franchising on the other hand is all about a relationship that smacks more of the old legal notion of master and servant relationship. It borders on a fiduciary relationship, that between an insurer and the insured; that between the teacher and the student. I could go on and on but I will not go on too far with that at the moment, given the short time we have.

The Trade Practices Act is not designed to deal with any of that. The ACCC, as the monitor of the Trade Practices Act, is not coached in how to deal with that situation. It is up to parliament, I say, to get onto the ball game, wake up to the issues and start becoming proactive. All I am saying now has been said for the last 20 years—for the last 10 years—and no changes of any note have taken place. Little polishing bits around the code—wow! There are no teeth to the code but, hey, everyone feels good after a little polishing takes place and a whole lot more people commit suicide or go broke in the process. The parliament that represents we the constituents of Australia is not being proactive, or has not been very proactive so far.

The people who have the power in this country are the people who are highly resourced, well organised, big secretariats, PR companies and they have the ear of the politicians. It is generally the publicly listed companies, the big companies that provide large donations to political parties. I do not. I, as a small businessman, cannot afford it. McDonalds—expunge—does to both political parties, Liberal and Labor. I can say that it was John Howard who invited Charlie Bell to become the chairperson of the task force he promised to form several elections ago to reduce red tape for small business people. Charlie Bell then gloated quite a lot after that to the franchisees saying he had been around having lunch with Johnnie Howard. I do not get that same advantage. I am not saying there is anything wrong with that process by itself, but it is not balanced. There are more things that need to happen.

You are now giving the opportunity for small business folk to be heard. But I am not talking to Kevin Rudd. Other folk will be that are far more powerful than I am. Big organisations know how to utilise that. It is called lobbying. We little folk do not. The problem is we get done over—rolled all the time. We cannot get ourselves organised because by our very nature we are independently minded. I get a bit upset when I might be given an opportunity to make submissions and find there is censorship all the way through it. With the comments I might make now, if I use names you will delete them. I notice McDonalds in its submissions actually quoted my case in full, the citation Rodney Hackett and Far Horizons Pty Ltd v McDonalds Australia Limited—not censored. When I used it in my submission all I see is it says, 'Rodney Hackett and Far Horizons Pty Ltd v', and then there is a black mark. I wrote a letter to Brendan Bailey. I put that in on my own letterhead in my submission. It was actually quite a nice letter, I thought. There was no contest about Brendan Bailey. I wrote to him having regard to his office at the time. By the way, I see he also put in a submission. But, hey, Brendan Bailey's name is texted out of my submission. My letterhead is texted out of my submission, so I am just a little bit concerned about how a lot of distortion seems to be taking place by way of this process, even at the very bottom end where some lip service is seen to be getting done for small folk to be heard by parliament, those people who are meant to be representing 'we', the Australian constituents, not necessarily big business or big organised groups. Do you have any other questions? Do you want me to go?

Ms OWENS—Assuming the master/servant relationship that you described is right, if consenting adults enter into that relationship and the relationship works to the benefit of both, then that is not necessarily a bad thing, is it?

Mr Hackett—No, of course not.

Ms OWENS—A lot of them work—

Mr Hackett—My point is you do not understand.

Ms OWENS—I actually do understand. I am just trying to get you to expand on it a little bit further. A lot of these relationships work; is that right?

Mr Hackett—Are you talking about franchising or master/servant relationships?

Ms OWENS—Whether they are master/servant relationships or whatever they are, a lot of the franchising relationships them seem to work.

Mr Hackett—You are looking at master/servant relationships—

Ms OWENS—I am talking about franchise relationships. A lot of them do work to the benefit of both.

Mr Hackett—Of course they do. I might say McDonalds is a very good operation.

Ms OWENS—Yes. I was going to say I eat there occasionally, but it is so occasionally it is probably not worth mentioning. The fact that it is a master/servant relationship itself is not the problem for you, is it?

Mr Hackett—No, not at all. But again, I am sorry, I am just trying to pick you up on it because it not recognised at law that it is a master/servant relationship.

Ms OWENS—Are any master/servant relationships recognised in law that are good models?

Mr Hackett—A master/servant relationship is a notion actually I think on this one that really covers things like employer/employee, a whole class of relationships. The franchisor/franchisee does not fit within that class because there has been no-one brave enough, like parliament or some judicially activist judge, to make the law. There is no law. It is ambiguous. There is a vacuum. There have been no declarations made by any of the powers that be that make the laws of the land upon which the framework of business operates and we small people who get done over occasionally get protection. It is not there.

Ms OWENS—Are any of the changes that you want to make, some of which you have described, something which is closer to employment law?

Mr Hackett—I think more dependent contractors.

Senator MASON—Fiduciary relationships; is that what you are after?

Mr Hackett—Yes, I am saying there is basically a fiduciary relationship that exists. It may not go quite that far.

Senator MASON—It is the law of equity; it takes in a whole new—

Mr Hackett—Absolutely, but that is where the concept of unconscionable conduct comes in. All of a sudden lawyers understand what you are talking about, but right at the moment there is very little law that really covers this very ambiguous relationship between franchisor and franchisee. I have said this many times before and nothing happens, no changes take place. What else was I going say? I get frustrated, I am sorry. The whole concept of a master/servant relationship, a well-known concept at law, is an old concept. It does not pertain to franchising as such because no-one said it does. There is no-one saying that it is not an arm's length relationship between business to business because there is no law that countenances the fact that franchisees are in a very dependent state with franchisors. It is that of a master/servant relationship in fact but not in law.

It is even worse than just an unprotected master/servant relationship. What we have actually got is in practice a master/servant relationship where the servants are also expected to pay over lots of money to the master to be a servant in that sense but they cannot control the money. There are no controls. The law is not there to help them. If you have got a few million dollars you can go into court, sure. What happens in court? It is quite capricious. The judges will say that on the record and any lawyer will know this: judges determine things by personal value systems, so you get the plaintiff's judge or the defendant's judge, whatever it might be. That means a biased judgement will basically come out. Good barristers know this and will play the judge accordingly. What happens is that small businessmen go in before a court, spend millions of dollars and it is just like going to a casino. Big business, on the other hand, can afford to throw the roulette wheel again. Small businessmen cannot. We need proper law. We need certainty.

In order to be protected, franchisees require a regime that provides certainty in terms of what their relationship is with the franchisor where they know up front that if good things are happening, tremendous; win-win, everyone shares the gains. When the times are bad, it should be: okay, we will all share the pain as well. Often it is not that way. On the point you were making a little earlier, I would say there are lots of great franchise systems around. There are lots of great master/servant relationships around. All I am trying to say is that there are a lot of franchisees that are in pain and are being dudded and they cannot go anywhere to get help. This is a chance but it is a chance, one of many. I have basically now turned into the sceptic. I expect a little bit of silver coating to come out of this, but parliament is where the real lobbying starts. After this inquiry, even if it is a really good report to parliament that is able to see that reform is overdue, I cannot get to have lunch with Kevin Rudd.

Ms OWENS—Nor can I.

Mr Hackett—Yes, because you are not a big business person. You are not a person of influence.

Ms OWENS—Actually, I probably could. You talk a bit about the discounting. I have read your submission actually but I must have been watching the news or something while I read that bit because I cannot—

Mr Hackett—I would ask you to re-read it because basically all I am saying—and I was very careful not to say too much; that really came out of my own mouth—was about well-known, eminent Professor Neville Norman's statement or commentary on what big discounting is all about. It is not my commentary. I just support and endorse what he said. A lot of other

commentary has come from well-known, established journalists from reputable newspapers in this land. I endorse what they say but I notice that a lot of that was censored by this inquiry and therefore the commentary loses its gravitas.

All I can ask you to do—although I have upset the chair and I apologise for that—is to please listen to some of the pain. If you believe that there is reform needed, make reform. Try to get it through parliament. The FCA is not the peak body representing franchisors and franchisees. For goodness' sake, they can still say that and get away with it with a smile on their face. They are a franchisor lobby group. They do not represent franchisees or their interests. They try to diminish the interests of franchisees at every turn. They sponsor Lorelle Frazer at Griffith University. She is a very lovely lady. But if you do not just read the overviews of their submissions which say there are no problems in franchising but you get into the meat—because as academics they usually have a bit of meat supporting the overview—the meat will say, 'We only sampled franchisors because our sponsor only wanted us to sample franchisors.' Or, 'We only did very little sampling of franchisees.' The meat in those reports by Griffith University clearly indicates that the methodology, the quality of the outcome of that survey, is a load of nonsense. It is not a genuine inquiry into what has been going on.

But people will endlessly quote just the executive summary in those Griffith University surveys which go on to regurgitate endlessly that there is no problem in franchising. Sorry guys, there is. If you like, I might be able to compile a list of suicides for you so you can understand how serious it really is. I probably did not get that across to you. No-one cares. I think it is called 'people falling through the cracks'. There are always going to be people falling through the cracks; who worries about them? The people who should be worrying about people falling through the cracks are the representatives of those people who have fallen through the cracks: our parliamentarians, our politicians. That is where the buck ends. It is not with the judges. It is not with the lobby groups. It is with the politicians. I understand you have to make inquiries and I think that is very worthy, but what goes on then is this whole lobbying process where all sorts of things can be derailed. It is not fair.

CHAIR—You talk about the regulation and the Trade Practices Act not being satisfactory or not directly applying. What do you see would be a better application? How do you deal with what bits of law or where could that be better applied?

Mr Hackett—What I would say to that is that it is a stopgap exercise in the Trade Practices Act. It was stunning law of 30, 40 years ago or whatever it was. It had just come in. It was designed to really try to regulate relationships between the sale of goods and what have you between a buyer and a seller basically. We are now talking about franchising, which is nothing like the same. It is all about this dependency. It is a relationship of dependency where one person is very vulnerable and the other person is a dominant player. That is fine by itself, the master/servant relationship, as long as there is proper leadership exercised by the master and it is not an exploited form. I do not mean exploited in perhaps the bigger commercial sense, but exploitative in a nasty sense.

Taking one step further, the only other laws in this country that start to head in the right direction to which franchising would perhaps be far better suited would be something like independent contractors legislation. That still does not even get there because really it is even more than that. Here it is like you are indentured when you go into a franchise. You are bonded

to the master and you have to pay a lot of money to do this and you expect proper treatment; good treatment; worthy treatment; supportive treatment; leadership. In a lot of cases you do get that, by the way. I will say on the record, although please expunge it, McDonalds right now is fantastic. They always were a great business, by the way, it is just that certain officers make some bad calls from time to time. No-one is big enough. I am a very proud McDonalds ex-franchisee. I loved the people. I think they were fantastic. I was taught a lot. Brilliant. But the whole McDonalds texta colour system could teach Australians a great deal about business. Fantastic. It is just that we have to stop the rot when it occurs. They will all try to stop it themselves from time to time. It does not always work but there has to be an avenue available in a structured civilisation where we are not living in independent caves happy to do our thing and where the people who make the rules under which we all exist, that is, the politicians make the rules which will actually ensure there is proper harmony that goes on between the various dwellers in the caves, the masters and servants and what have you, and that there is fair play. I like to think of myself as a very fair-minded Australian who believes very much in the concept of fair play. I have seen a lot of unfair play going on.

CHAIR—Does the ACCC as the regulator have enough power or does it exercise its power in your view? Does the ACCC do what it is intended to do?

Mr Hackett—I believe that under the limitations of the Trade Practices Act, which is highly inappropriate to really control the issues I am talking about, it probably does almost as much as it can be expected to do. We have a nonsense code without any teeth, some investigatory abilities which are as limited as investigations that—I am trying to think of something perhaps a bit more worthy. There was an *Insight* program—do not know if you watch *Insight*—about two months ago or even less where the ACCC was investigating what was going on with fuel prices in Australia. The ACCC actually said after a six-month investigation that they had no idea what was going on. That is there if you want to get the SBS tapes. Ron Bowden of the Service Stations Association summed it up in three minutes when he was given a chance to talk on the same *Insight* program. What I am saying is that the ACCC really I think are hoist on their own petard. They do not seem to do proper investigations and they have very limited powers anyhow, I suppose. They are also operating on ground rules that are just not valid to produce fair outcomes.

CHAIR—Obviously having experience of being a franchisee yourself you would understand the process from beginning to end. Where do you see the biggest weaknesses? Is it the pre-education, pre-contractual stage or is it really everything that happens after that because you cannot account for everything in a contract. A contract is really just an agreement to go and then do a whole heap of things which are not necessarily all written down—

Mr Hackett—I agree.

CHAIR—but it is by agreement. Therefore where do you see the biggest conflict or disputation?

Mr Hackett—You summed it up well. Both areas, because there are certainly a lot of people who get into franchising who perhaps should not be in there. It is not necessarily their fault. They have not perhaps been given the right heads-up advice in the first instance and maybe in a society like ours who is going to? We are meant to look after ourselves, largely. But there would

be a lot of franchisees who are not ever going to become proper businesspeople. Maybe the selection process is wrong for them in terms of working out franchising was probably going to be a great way to buy themselves a job, or whatever it might be. They may have all sorts of terribly wrong expectations about, 'This is a licence to print money', when it is going to be a lot of hard work. I can remember working 85 hours a week for at least the first couple of years in my business. Not everyone is going to put that much in.

Other times you could educate the franchisee as to what expectations are. I think that is very worthy. I think there are programs around, although you have got to be a bit cautious. There are a few outfits around that do not necessarily teach it the right way, without being an expert on the whole subject. But then once the relationship is formed—so there are hurdles before the relationship is formed and that can be dealt with through education to a degree—the problem is that there is very little real law around that is pertinent to that actual relationship that then exists. It is laws that are designed for all sorts of other things.

Franchising has been something that has only come into say a really big deal in the last 30 years. When it started off no-one had every heard of franchising 30 years ago. It used to be called licensing. You used to license something. That is a very limited sort of concept but as the years have rolled by it has really become a very vibrant and dynamic part of our economy and I believe has got a lot further to go providing the relationship is sorted properly. I am not big on over-regulation. I think it is great if everyone just by socialisation thinks, 'Let's make laws happen together and we go for the win-win.' The point is we know that is not always going to work so sometimes you need the overseer so that actual fair play is done in that win-win relationship.

CHAIR—In terms of disputes and the disputes process, what is your experience and your view and how might it work better?

Mr Hackett—My experience is that it is absolutely shocking. It is all there in my submission. Whenever mediation was attempted it was always just a case of people going through the process because you had to go through it. There would be no proper relationship deals done. I remember that at a court-required mediation that took place in my case the mediator actually said to McDonalds in a private consultation room that happened to have Robert Zarco, a US attorney I had brought over, in that room with them, the mediator, a former judge, actually said, 'Hackett is not going to win this case. He should just'—he did not say 'capitulate'—'compromise right now.' This is before the thing had gone to court. That is the sort of mediation process. As soon as I heard from Robert Zarco that that had been said I lost total faith in the mediator. Mediations can be nonsense, but mediation can be a great first step. I am a big believer in communication despite the fact that I might have otherwise started up another way. Put that down to a bit of a cold—

CHAIR—Absolutely. Move on.

Mr Hackett—and a few other things going on. If we can actually get people talking, it is even that much better again. But where you cannot—and that is what dispute resolution is all about; that is where it really gets hard—what do you then do? At the moment it is going to the Supreme Court. Do you know how many millions of dollars that can cost you for a four-week trial? Then it just so happens under the laws of our land because of the wonderful medieval doctrine which

protects incompetent barristers, you cannot sue the bastards. I have lots of material in my submission about that.

Ms OWENS—I know.

CHAIR—I am very reticent to pull you up at all but, given that we have gone slightly over time with your acceptance, I will say thank you very much for your presentation. I appreciate your time.

Mr Hackett—My apologies chair for the little outburst at the start earlier—

CHAIR—There is no apology required. That is okay.

Mr Hackett—It is required.

CHAIR—Thank you very much for your detailed submission, too.

[2.04 pm]

BELLIN, Mr Howard, Chairman, IF International Pty Ltd; Private capacity

CHAIR—Welcome. I invite you to make some opening remarks.

Mr Bellin—I am appearing on behalf of my company and on my own behalf on the basis that there are some problems with franchising that can fairly readily be solved.

CHAIR—You are more than welcome to give us an overview or some opening remarks and maybe just speak to your submission.

Mr Bellin—I was involved in introducing franchising to Australia in 1969 as the southern hemisphere's first franchise adviser. My longevity in the field paints me either as a dinosaur or alternatively as someone whose experience can be the basis of a useful contribution to this important inquiry. I respectfully leave the dinosaur call to the committee.

In 1999 the Franchise Council of Australia said that franchising's growth would be slowed by out-of-touch government regulations. Franchising has boomed since that time and since that regulation. However, uneven and lax government enforcement often allows unscrupulous franchisors to operate as if there were no franchise code. The FCA says no further review or regulation is required. Why? This then brings me to my view of the FCA. It purports to represent franchisors and franchisees. I have heard of no companies in the world that have successfully had union members on their boards of directors. There is a total conflict. Different needs arise all the time. Basically my view of the FCA is that it is a lobby group for Deacons lawyers, franchise consultants and independent lawyers and accountants and then franchisors.

Theoretically the franchise code protects franchisees against exploitative and poorly managed franchisors, yet there are many cases where prospective franchisees are pressured into joining franchise systems as a result of being provided with misleading information. Some franchisees buy franchises from franchisors that have less capital than they do individually. Franchisors have to be adequately regulated and severely penalised when they breach the franchise code. How effective do you think drink driving regulation would be if it were not enforced?

Effective enforcement of the franchise code will ensure that credible franchisors continue to grow and will slow the growth of the undercapitalised fly-by-night operator whose main business is selling franchises as opposed to managing franchise chains. Unsophisticated people regularly invest in the stock market. They are protected by product disclosure documents, prospectuses, half-yearly and annual reports and information on significant corporate changes. ASIC and the police do their best to ensure that investors are not misled even if their investment is for example less than $10,000. Where necessary, action is taken.

Contrast the stock market protections with those of franchisees who usually invest their life's savings and put their houses on the line to buy their franchises. They are not nearly as well informed and have far less protection than stock market investors.

Finally, I am an Australian citizen by choice. I have learned about and respect the Aussie concept of a fair go. Do the members of this committee really believe that the Australian concept of a fair go exists in the franchising world?

CHAIR—You mentioned the code and we have heard evidence from other people as well. Do you think the code which deals mostly with disclosure is satisfactory in its current form? Can it be made more efficient?

Mr Bellin—Yes.

CHAIR—We are open to your suggestions.

Mr Bellin—It is grossly ineffective because of this and I said this in my submission. We have to understand who it is that buys franchises. They are not multimillionaires usually, unless they are buying a hotel franchise. They are just average people. They are people like us. Most people really do not know a lot about business because that is not what they do. When I went from my employment to start my business I did not know anything. I did not know about tax stamps. I knew nothing. I learned on the go. Okay, franchising teaches you how to run a franchise. It does not teach you how to be a businessperson. Now we have got someone who sadly at the age of 40 loses his job and says, 'I am not going to get fired again.' He decides he is going to be a franchisee. They say, 'Well, this document is a requirement from the ACCC. Here it is.' The minute the average person hears that he says, 'I am protected by the federal government. I have no problems.' He is not protected by anybody. They can say anything they want in a disclosure document and not get done for it. Are the committee members familiar with the Quiznos case? That was an ACCC case.

CHAIR—Yes.

Mr Bellin—The Quiznos franchise went broke in America. A man in South Australia who sold his franchise business for $30 million was the master franchisor for Australia. I was told by a journalist that after wages and rent the gross profits did not cover any other expenses. The ACCC said that Quiznos had to give the failed franchisees $25,000 each for a $400,000 investment. Is that a fair go; right; reasonable? It is just wrong. My submission talked of the Federal Trade Commission. I guess committee members are aware that our Trade Practices Act is largely based on the Robinson-Patman Act and the Sherman Antitrust Act. In fact the first quarter if not first third of our Trade Practices is the FTC legislation. People went over to the FTC. I was involved in this very early. I have letters here from when I requested franchise legislation in this country in 1971. I went to see then Senator Murphy about it. I have letters here that I found going back to 1977 talking about franchise associations.

I never envisaged a franchise association that purported to act for all and sundry. I do not know how any association can act for all and sundry. Number one, somebody has to take responsibility. When a disclosure document is misleading the people who provide the misleading information should suffer civil and perhaps criminal penalties. What is the difference in practical terms between producing a false prospectus—which many of our fine citizens have gone on to make big rocks into little ones for—and producing a false disclosure document? You collect more money when you have a prospectus document because you have got more people with less money. I think that is something that is not happening, because I have met these people. Think

about the 50-year-old who loses his house. He has lost his job or she has lost her job. They went into a franchise because it is the greatest thing. Everybody knows it is. You cannot make a go of it because it is a con. How many of those 150 Kleins franchisees that went broke lost their houses?

Mr Hackett is right. I know of cases in America, not here, where people kill themselves. There was a story in the *New York Times*. A guy who was a Quiznos franchisee fought and fought and fought, finally went into the restroom in the restaurant and shot himself in the head. This is real. We are not talking about a theoretical system where you say, 'Let's make this better because it will look good'; we are hurting innocent and relatively gullible people. All we have to do is say, 'So and so issued a false disclosure document.' Take them to court. You saw my submission. In America the directors are personally liable where there is misleading information. I have my submission here. Do you remember those parts of it?

CHAIR—Yes.

Mr Bellin—What we are saying is, 'I've got your back; I am here to protect you.' But we are not protecting them. We are just saying it. It is just words.

CHAIR—Just to follow through on that even better disclosure, more efficient disclosure—

Mr Bellin—Full and proper.

CHAIR—Full, proper, the whole lot—

Mr Bellin—Those are the words.

CHAIR—Full disclosure would not prevent certain behavioural outcomes. Disclosure is more about information, but behaviour is a bit harder to manage.

Mr Bellin—That is precisely correct. We reach a point, don't we, where we have to take responsibility but let us get to the point at least where when we take responsibility we have been provided with everything that is full and proper. Sure, people fail in business. Franchisees do fail. There are crooked franchisors and there are stupid franchisees, and there are recalcitrant franchisees, franchisees that steal, franchisees that do not report their income and there are franchisees that the minute they make a buck they go out and buy a Mercedes and they go out and get a girlfriend. I have seen every one of these things. Every one of these things I have personally seen—

CHAIR—Perhaps a Mercedes and a girlfriend.

Mr Bellin—But we—

CHAIR—I appreciate what you are saying. I am actually trying to draw something out of that. Let us say even with full disclosure—

Mr Bellin—There are two words though, sorry, full and proper. There really is. That is not semantics, because it has got to be proper.

CHAIR—Even with full and proper disclosure there is still the opportunity for people to behave in an unscrupulous or unfair manner, or to do certain things—

Mr Bellin—Absolutely.

CHAIR—Just trying to deal with those who would do the wrong thing rather than everyone who is doing the right thing, what sort of system would be effective in trying to deal with the behavioural component? Is it sanctions? Is it good faith? Is it by making it clearer in law or in the code? How do we deal with the real practical end? I accept what you are saying. What I am saying now is what information do you give to us to say, 'Now that we recognise these issues, how do we then move on ameliorating these problems?'

Mr Bellin—I would say this: full and proper disclosure puts things in the light of day. Governing human behaviour will result in a situation where whomever is judging it will come down to the story: he said; I said; he said; I said. You cannot govern human behaviour. Otherwise you would not have any prisons.

CHAIR—Sure; I accept that. In other words what you are saying is that it is not so much about trying to govern the behaviour, it is more about detailed full and proper disclosure which considers every possible scenario or gives direction to every scenario. Is that more of where you are going?

Mr Bellin—For example, if a director of a franchise company has been up on criminal charges that ought to be disclosed—I know people who have gone broke in franchise chains and that is not shown in the disclosure documents.

CHAIR—When you say they have gone broke is that—

Mr Bellin—As franchisors. Jason Gehrke who made a submission as well—I saw it online—said that 34 per cent of franchisors failed over the last 10 years. We did a survey in the 1990s where two-thirds failed. That is what I am really talking about. I am not talking about an individual franchisee failing. Going into business on your own means you have the right to make more money than you thought you could make. It also means you have the right to fail. Franchises fail. Businesses fail. Everybody fails if they do not do what they are supposed to do or if they are unlucky. I am not even talking about that. It is hard to make a buck out there on your own. It has always been hard, but why should he or she go broke if they were provided with false information? Why is that fair and why is that right and why doesn't the government come down on these people? It is not the government; it is really the ACCC. I do not think you need to change legislation. I do not think you need to do anything. I think you just need to give the ACCC some more teeth.

I have another complaint about the ACCC. They have a franchise consultative council. My view is that it is not really consultative; it is hand-picked people who know John Martin well. I can tell you I have a bias because they kicked me off it because they would say things like, 'We should have the government pay for franchisee education.' I said, 'Why? That is not a government role. People own their own business. If people want to get franchisee education they go and pay for it.' It is a free enterprise society. I said a lot of things that were not toeing the line.

CHAIR—What is the role of the ACCC and the Franchise Consultative Council? You have been a member of it, so maybe you can enlighten us on what they actually do?

Mr Bellin—They meet. John Martin is the commissioner. They talk about various issues in franchising. Richard Evans who used to run the FCA was there. There was me. I am not really—

CHAIR—What is the role and purpose, though. It is there, but what does it set out to do?

Mr Bellin—It is the equivalent of an advisory board in a company where they are not legal. You give them advice and they will go back to the ACCC, Graeme Samuel, and then Graeme I guess will go to parliament and say, 'We would like the law changed so we can do this, that and the other thing.'

CHAIR—In your view does that take place effectively or not at all?

Mr Bellin—I have not seen too many changes. The last inquiry was far too narrow as to disclosure. The thing I come back to is if any of us buy shares with a prospectus and the shares fall to half and we have been given proper information, that is the luck of the draw, isn't it? If a franchisee buys a franchise with full and proper disclosure, that is the luck of the draw. That is fair. In terms of regulating the relationship it is not a master/servant relationship, by the way. There is a clause in all franchise agreements that says very specifically he is not an employee. He is not a partner.

If we can come back to the very basics—I am not trying to educate you—franchises are basically a licence agreement. It is a licence to do something, just like a drivers licence. If you do the wrong thing you have your licence taken away. The reason the franchisor has to be able to do that is that it protects the integrity of the system. I have used this example previously. If an Angus and Robertson franchisee stocks pornography, that is over the line. If Angus and Robertson does not terminate that franchisee immediately, the chain is finished; absolutely done. The franchisor has to have the right to terminate. I am not here saying franchisors should not be able to terminate. I am not saying they should not be able to—

CHAIR—They have got that right. They have all got that right.

Mr Bellin—In my experience the biggest complaint that franchisees have is that you, Mr Franchisor, are letting these cowboys ruin my business.

CHAIR—I am sorry, who are the cowboys?

Mr Bellin—A bad franchisee is a cowboy in their eyes and he destroys their business. If you go into a McDonalds and the service is horrible our view is McDonalds service is horrible everywhere. It is not that cut and dried. What I am really pushing is: let's fine these guys. If they are criminal, let us put them in jail. Let us give this thing some meat so people will be afraid. The drink driving legislation has been magnificent. It said, 'If you are over .05 you can lose your licence.' They support it. What has happened with—

CHAIR—If you are going to use that analogy of drink driving it obviously does not prevent drink drivers but it does set a clear framework with clear penalties and clear actions. You know that you will not only be policed you will be checked and you will pay the price.

Mr Bellin—And what has happened to drink driving over the years? It is for real. You cannot say, 'If you do the wrong thing we are going to get you', because you are not. Everybody will just go ahead with impunity.

CHAIR—Can you also maybe give us a description through your experience as to what is the area where people are doing the wrong thing? Where are the areas in which there is, let us say, an abuse of power rather than a breach of law?

Mr Bellin—First I will just name names of two things. On the same day that a Clark Rubber franchisee was voted the fastest growing franchisee of the year, he was put into receivership. That kind of means that people were not in touch. Kleins went broke with 150 stores and nobody knew that they were in financial trouble because they did not have to update their disclosure document. That cannot be right. As I said, we have franchisors who are out there selling franchising. We have heard the issue about churning. It goes on forever.

CHAIR—With Kleins, were they still selling franchise systems right up until that time? We could make an assumption that they did not disclose. They probably were?

Mr Bellin—I do not know, but I would not be surprised. I am glad you raised that because I want to show you something very interesting. Everyone knows that mortgage brokers are really not very solid businesses now. Here is an ad from the *Age* dated 25 October 2008:

Mortgage gallery. Now is the time. Over 45 per cent of all new home loans are written by mortgage brokers.

That is advertising for franchisees. NAB has its eye on the Wizard network, which has gone broke; GE Money pulled out of mortgage broking; house sales are down, yet here is a company advertising, 'Come on and be a mortgage broker because you will make a lot of money.' I can give you a prediction; I can guarantee it. Coffee lounge franchises, mortgage broker franchises, juice franchises, financial planner franchises over the next three years are going to go broke. Not all of them, but a hell of a lot of them because there are not enough customers to service all those businesses. There is a wonderful case in America where a man started a chicken chain called Minnie Pearl's Chicken. She was a southern music icon. He said there were more chicken eaters out there than there were chicken places and he sold about 150 or 200 franchises and went public at $80. But none of the franchises opened and the shares fell to 80c. These are the kinds of things that happen. They cannot do that any more. They cannot take credit for the franchise fees.

But the point is the punter really thinks the government is protecting him. I honestly believe that. When I think the government is protecting me I will take the chance, but the government is not protecting me. One thing that could be raised is: why doesn't government vet every disclosure document. You cannot. It just will not work. But do something when people are cheated. Another thing I said in my submission which is totally out of the purview of this committee but is nevertheless right, in America if I am a wronged franchisee I get a lawyer who works on contingency. If he wins the case he gets a third of what I get. I can easily bring a class action and if I win or my class wins there will be treble punitive damages. Now you are talking.

Furthermore, if he goes over the state lines he has got the Federal Bureau of Investigation after him because it is mail fraud.

Senator MASON—Are you citing the United States legal system as a model for Australia? I do not know.

Mr Bellin—No, I would never do that. What I am saying is—

Senator MASON—You are talking about having teeth in terms of enforcement.

Mr Bellin—It works like this. You have got the Westminster system with its flaws. You have got the American political system with its flaws. The Americans will say the contingency system is good because it gives the little guy a go. The Australians will say it creates a litigious society. I live here by choice. I am just saying that is something that could happen. I have spoken to these guys. I got ripped off in my franchise—

Senator MASON—I will ask a couple of questions, if I can?

Mr Bellin—Go ahead.

Senator MASON—You commence your submission with this line:

A major problem with Australian franchising is the quality of disclosure …

The chair has addressed those issues in questioning and that is terrific. Your submission continues:

and also the lax enforcement of the disclosure provisions of that code.

When you say 'lax enforcement', is that because of a failure of the ACCC to use their discretion to prosecute or investigate or a lack of administrative resources? Or is it because there is not the legal power to do so? Which is it?

Mr Bellin—It is a lack of administrative resources. An example—

Senator MASON—Just so that everyone is clear, in other words, it is their failure to pursue a matter rather than them not having the legal capacity to do so?

Mr Bellin—I do not really—

Senator MASON—Because they are very different issues.

Mr Bellin—Okay. I do not think there are sufficient penalties under the code but I do not know because—

Senator MASON—We will get to the administrative issues in a second, but do you think the ACCC has sufficient power to pursue these issues if they need it?

Mr Bellin—I do not know. I genuinely do not know. I have read the act.

Senator MASON—That is something I will ask Mr Samuel when he comes in. That is fine.

Ms OWENS—You have talked a lot about catching and punishing intentional bad behaviour. Assuming the disclosure is full and proper and ongoing, it essentially seems to me that you are then saying buyer beware.

Mr Bellin—Of course. There is stupidity and there is cupidity. I am worried about the cupidity.

Ms OWENS—But there has been a lot of talk about the need for there to be accredited training and all sorts of other things that would help people. But for you it is a question of fixing up the information so that people can make decisions?

Mr Bellin—So they can make informed decisions like you do when you buy shares issued by a company that is about to float and when you invest in a company you need to be told that something happened. Really, if we think about franchising, it is a risk and reward equation. If I go into my own business I will put up less money than I will in a franchise because I do not have to pay a franchise fee and ongoing fees. My risk is less but my reward is probably less—I do not know about the risk and reward. I probably cannot be terminated but I might go broke. If I go into a franchise and if I think I am going to make a lot of money, I have got a risk. We cannot protect people against themselves, and nor should we.

Ms OWENS—If things start to go bad through incompetence or whatever, do you think the relative bargaining positions are a problem?

Mr Bellin—The franchisor always has power. The reason he has power is, first of all, because franchise agreements are tough. Some of them are 60 to 100 pages. I started my career selling franchises. I used to say to the people, 'Listen, if the franchisor wants to screw you, you are screwed, okay? So before you sign the agreement you check out the franchisor. You go talk to other people. If you have got any doubt about his integrity, its integrity, do not touch it.' Any franchisor can burn any franchisee just by sending notices, by withholding support. It is sad but it is true. The franchise agreement is virtually omnipotent.

CHAIR—You obviously have a lot of experience. Can you tell us what they can do? You have mentioned withholding certain things, but can you give us a list? What are the things they can do?

Mr Bellin—For example, I have a car dealership; I do not get the parts. Or I have got a hot new model and the hot new model is distributed based on volume from last year. If a franchisee is a problem, one of the things you do is you cite them. You say, 'If there are three breaches of an agreement within a year, we can terminate you.' So you find little things to breach them on. But the most common thing that the big boys do—not a lot of them—is they call a guy up and they say, 'Look, it is not working for you. It is not working for us. And they would probably give him a fair price. If he says no, they let him know the way the world works. 'We've got this much money. You've got this much money. Do you really want to take us on?'

CHAIR—You said they would probably offer them a fair price. What if they do not offer them a fair price?

Mr Bellin—That is an issue. There are some conundrums that arise. For example, in the car industry the numbers of outlets in retail of all types are contracting. There used to be 12,000 petrol stations in Australia. Now there are about 5,000 or 6,000. A motor company might run into a situation where it has a small dealership in a suburb and it wants to consolidate. They approach the man who runs it and they say, 'We would like to buy you out', and they offer him what they think is a fair price, but he cannot sell because that is his life and his livelihood. Now you have got a real conundrum and it usually becomes a legal issue. The question is: who is wrong and who is right? The motor company cannot make any money because he is not moving enough units. He is making enough money because he probably owns the premises. You get those kinds of situations, but that is not unscrupulous. It is just very hard. Who could adjudicate something like that? What is fair? If you pay him double what it is worth, the shareholders will crawl all over you. If you pay him less you are seen as a tyrant and a thief.

CHAIR—I accept the example that you have given. Just at a more simplistic level, let us take a small food retail outlet. There is a similar situation.

Mr Bellin—They will find things to breach them on. They will say, 'Your place is dirty. Here's a report' or whatever. In the old days in America they used to look at their contracts to find ways to breach them so they could resell the franchise all the time; that is, putting pressure on and making it untenable. It is not much different from how a corporation decides to get rid of an employee without firing them. The agreement usually says, 'If any of the following were to occur the agreement is immediately terminated.' That is receivership and so on. 'If this breach occurs we will give seven or 30 days notice to repair it. If it is not repaired we can terminate you.' Then they might say, 'If two breaches of the same clause are committed within the year we can terminate you.' The point is that there is an economic imbalance. Sure, they can go to mediation, as I said in the submission, but that does not seem to work. Again, my point is: if there were full and proper disclosure, and if we were really able to ensure that the franchisors that sold franchises were ethical and straight, it would be a lot easier. This is probably not consistent with what most people think. The bigger the company the more ethical they are with franchisees.

Ms OWENS—Because they do not get to be big.

Mr Bellin—Do you know why? I talk to a lot of these people. When a company employee tries to cheat a franchisee he is putting his career on the line. That is the kind of stuff that gets him fired and it gets him so he does not get hired again. It is the little people that are the worst. As stated in the submissions, I think a third of the franchisors are less than $5 million turnover. The abuses occur with the little people and not with the big companies. In America—and I would suggest that it should be here—the car companies are not under the franchise code.

Ms OWENS—Do you think they should be here?

Mr Bellin—No. In America they have the Dealers Day in Court Act, which is for the car industry. We have got the oil code here for the oil industry. I do not know why the oil code would have to be under the franchising code. I would rather see a Dealers Day in Court Act

equivalent here, and make the code for the franchisors under a certain amount. I honestly can tell you that the big companies will rarely try to do the wrong thing, because people do not want to lose their careers.

Ms OWENS—It could also be that the size of the franchisor is correlated to their competence and skill as well. Perhaps this is not intentional bad behaviour necessarily.

Mr Bellin—There is a situation now where Yum is trying to take Jack Cowin's franchises away. In my view, that is unethical, but again that comes right from the top. There could be an argument both ways on that about whether it is right or not. Companies get big because they play the game straight.

Ms OWENS—No matter what laws you put in place that regulated the break-up of the marriage, some people would still manage to work within them and do the same thing.

Mr Bellin—We cannot regulate decency.

Ms OWENS—No.

Mr Bellin—I really like this place. This concept of a fair go is honest to God. I am just saying: can we give these people a fair go? Sure, they will go broke. We know that. Everybody takes risks. We cannot stop people going broke. We cannot stop people losing their jobs. We cannot stop people losing money on the stock market. We just want to give them a fair go. That is something that the committee can do.

CHAIR—Thank you very much for your submission and for appearing before us today.

[2.38 pm]

CASSIDY, Mr Brian, Chief Executive Officer, Australian Competition and Consumer Commission

RIDGWAY, Mr Nigel, General Manager, Compliance Strategies, Australian Competition and Consumer Commission

SAMUEL, Mr Graeme Julian, Chairman, Australian Competition and Consumer Commission

SCHAPER, Dr Michael, Deputy Chairman, Australian Competition and Consumer Commission

CHAIR—Good afternoon. Would you like to make an opening remark?

Mr Samuel—Yes. I will keep it brief, because you have our submission, which is quite detailed. I do not want to go into a lot of the background. To get the heart of the matter, if I were to look at the categories of complaints that the ACCC receives in relation to broadly franchising issues, they could be categorised into three separate groups. The first would be those where a complaint is lodged with us, normally through our Infocentre line, which is the first port of call for a complaint being lodged, but the complainant does not really want to take it any further. They would expect the ACCC to follow up the complaint, but do not want to spend any more time of the issue. That can be for a range of reasons. It could be fear of intimidation. It could be concern about having to become involved in legal action, even only as a witness. It could be a concern about the whole court process. In other words, there is a reluctance to take it any further than to simply lodge a complaint with the ACCC and hope that the ACCC will then take on the task without ever having to involve the complainant any further.

The second category of complaints are those that are lodged and the complainant assists us with our investigations, but the evidence presented after thorough investigation does not necessarily match the fundamental basis of the complaint itself. The complaint might be that the franchisor has done certain things, but when we get down to a detailed investigation using our investigators and trying to get the sort of information and evidence that would be necessary to take the matter through to, for example, litigation in the court, it appears that the evidence does not substantiate the complaint for a range of reasons. It may well be that what the complainant is alleging is a series of misrepresentations that were made at the time the franchise was entered into but it turns out those misrepresentations were oral rather than written, and then there is a debate or a dispute between the franchisor and the franchisee as to what the oral representation was.

In some cases it appears that there has been an inadequate analysis of the business model, either by the franchisee or by the franchisee's advisers, if they have chosen to appoint advisers. There may well have been a lack of analysis of what is required in terms of investment of time, expertise, as well as money on the part of the franchisee in terms of entering into the business or an inadequate analysis of the viability of the business model. Sometimes we find that in relation

to complaints where the franchise has failed the main contributing factor will be inadequate management practices on the part of the franchisee. That is the second level of complaints.

The third category of complaints is where a complaint is lodged, the franchisee is willing to assist and is able to give proper evidence that will assist us to take the matter through to litigation and to follow up on the complaint, and the nature of the complaint is substantiated by the evidence that is provided to us.

Those are the three separate categories. One thing is genuinely common amongst all three categories, and that is that the franchisee suffers hardship, and at times great hardship, but the difficulty that we have so often is that, while there may be hardship, if the complaint falls into the first two categories, that is, the complainant does not want to take the matter any further or the evidence does not substantiate a breach of the law and sometimes may not even substantiate a breach of ethical conduct or of proper commercial conduct on the part of the franchisor, then it is very difficult for us to take it any further. That would not be to deny that hardship has occurred as a result of the various circumstances that have arisen.

Where we can take the investigation further is in that third category of complaint that I talked about. The investigation and resultant action can take essentially three forms. The first would be to demonstrate that there has been misleading and deceptive conduct under part V of the Trade Practices Act, and more often than not, providing the evidence is there, that can be a black or white case. If there has been written evidence or there has been a written representation made and it is shown to be misleading and deceptive then that is almost, as I say, a black and white case.

The second category will be that of a breach of the Franchising Code of Conduct, and given the prescriptive nature of the Franchising Code of Conduct, again, demonstration that the Franchising Code has not been complied with can be a relatively easy thing to be able to take further processes—that is, litigation, as the case may be.

The third category, though, is that of unconscionable conduct. I have to say that that is a lot more difficult. I have said in many speeches given to small business seminars and the like that unconscionable conduct involves a lot more analysis and a lot more detailed investigation. It involves judgements being exercised as to whether or not the conduct on the part of the franchisor was harsh and oppressive or without conscience or failing the test and going well beyond the appropriate ethical standards that are appropriate in business transactions. We need to remember that the threshold of unconscionable is as the term contemplates, that is, without conscience or being harsh and oppressive as distinct from being simply tough bargaining.

More often than not we will pursue matters involving franchises under the misleading and deceptive conduct provisions or breaches of the franchising code, because that will give us a timely outcome. The moment that our investigations will show a breach of the misleading and deceptive conduct provisions or of the franchising code, given that the consequences of taking action under part V or under part IVB in respect of breaches of the franchising code are exactly the same as the consequences of taking action for unconscionable conduct, we will go that route to get a timely outcome rather than further pursuing the investigation of unconscionable conduct.

However—and this needs to be understood—as the law currently stands, whether it is a breach of part IVA, which is unconscionable conduct, or part IVB, a breach of the Franchising Code, or part V, a breach of the misleading and deceptive conduct provisions, except in a case where we proceed with a criminal prosecution under part VC—which is quite unusual—it is not possible for us to get any pecuniary penalties. The most that we can obtain by proceeding under any of those three headings that I have described is an injunction to stop conduct continuing. We might be able to get some corrective advertising or a declaration by the court that there has been a breach of part V, misleading and deceptive conduct, or part VB, franchising code, but we cannot go much further than that. We can sometimes take representative actions for damages, but they are quite complex under the Trade Practices Act, particularly where there is a large number of franchisees involved and there are some other complexities associated with that, but there are no pecuniary penalties available.

When we achieve a successful outcome in the courts, the most often asked question by the media is, 'Why did you go so soft on the franchisor? After all, this appeared to be fairly egregious conduct and yet you did not seek any penalties.' I have to point out that there is no capacity under the law to seek any pecuniary penalties. As we put in our material to government and in this submission, it seems to us—I was nearly going to use the word 'unconscionable'—somewhat unusual that we can, for example, get many millions of dollars of penalties for people who engage in anti-competitive conduct, but for those who engage in dishonest conduct, misleading and deceptive, or breaches of the franchising code, which are after all prescriptive rules, or breaches of unconscionable conduct, which is so harsh and oppressive as to be without conscience, there is no financial penalty that could either act as a deterrent or be extracted from the party concerned.

There is no evidence, in our view, of systemic failure of franchising as a business model. Given that the numbers of franchises in existence are in the tens of thousands, and the number of complaints/inquiries we receive each year is of the order of 400 to 500, we do not believe there is a systemic failure of franchising as a business model, but in short what we have said is that the information that is given to franchisees should be accurate, timely and, let me emphasise, meaningful. The quantity of information given does not necessarily operate in direct correlation to the quality of the information given, and often the quantity of information given can be in inverse proportion to its quality and to its meaningful nature as far as franchising is concerned.

Secondly, we exhort and encourage franchisees to seek expert independent advice. That means expert legal advice, expert accounting advice and sometimes expert business management advice. So often what can happen is that a franchisee will enter into a franchise arrangement and will do so by investing a substantial sum of money with the thrill of getting a very substantial return, but without having proper business management advice as to the economic viability of the franchise, or indeed of the business expertise of the franchisee, and therefore the ability of the franchisee in business management terms to make the franchise work successfully.

Thirdly, we would want to stress to franchisees that their strongest bargaining position exists up until they sign the franchise contract. Although a lot is said about the disparate bargaining positions of a franchisor and a franchisee, up until the franchising contract is signed they have a very strong bargaining position. They have the money in their pocket. They have the pen in their pocket, and they do not have to sign up to the franchising contract. The moment the contract is signed by the franchisee, the bargaining position shifts dramatically. That takes me back to the

comments I made before, that is, the information given prior to the contract being signed needs to be timely, accurate and meaningful. If they seek independent expert advice prior to signing the contract when they have the greatest leverage, their strongest negotiating position is to simply say, 'No. I won't proceed on the basis that has been set out before me in the contract because my legal adviser, my business management adviser and my accounting adviser are all telling me that the following safeguards are missing', or alternatively, 'This is not a franchise I ought to enter into for a whole range of reasons they have so described.'

Finally, in terms of franchising, as I have indicated, the strength of bargaining is up until signing of the contract. After the signing of the contract the strength of bargaining switches dramatically in favour of the franchisor. It is at that point that disputes occur, and we believe there can be some improvements made to the mediation process to strengthen that. Mediation, in many respects, will overcome a lot of the difficulties that we can face in endeavouring to get the necessary evidence to be able to litigate. It can also avoid one of the real problems that we often find in making our risk assessment on litigation, which is to say, 'If we litigate against this particular franchisor, there is potential brand damage that will be done and that brand damage can have its own backwash effect on other franchisees, which in the global context of a particular franchise could do more damage than may have occurred as a result of the particular misconduct that has affected the franchisee concerned.' I will stop at that. I am not sure whether my colleagues want to add anything more.

CHAIR—Thank you for your submission and for appearing before us today. I will start with the issue of regulation. We have had many submitters who have said to us that they believe the franchising sector is overregulated or highly regulated or world's best practice, but generally the core principle is that there is plenty of regulation in place. Aside from the code, which specifically deals with disclosure more than anything else, there does not seem to be too much regulation at all in effect, certainly practically at a ground level where you could point to. There is the Trade Practices Act, which is a very high bar to attain, and to pay for in terms of costs. Where is all of this supposed regulation? Where does it exist?

Mr Samuel—I am not sure. As you have indicated, there is the Trade Practices Act. I would just dispute one issue there. I think the bar in the Trades Practices Act, in terms of breach of the franchising code or misleading and deceptive conduct, is not high. If you are dishonest and you mislead and deceive, you are in breach of Part V of the Trade Practices Act. If you do not comply with the prescriptive requirements of the franchising code, again, that is not a high bar to jump. Unconscionable conduct is a high bar, as we spoke about before. It may be that some of those that are reflecting on the franchising code are asking whether the volume of prescriptive regulations contained in the code is not acting in inverse proportion to the quality of its impact. We have commented upon some of those aspects in our submission.

CHAIR—We hear a lot about there being overregulation. I am struggling to find where it all is. According to you, it is not really there, either. In terms of this high bar, a question that is before us is: is there enough legislative power somewhere, be it TPA or the code, versus enough enforcement of those rules. How does that interplay? Is it more a case that there needs to be more enforcement or just a case that there needs to be more legislative power, perhaps to lower the bar slightly in terms of making it more clear and more direct; rather than having implied power through the Trade Practices Act, having it more explicitly expressed through the code, which might just be the first port of call for anyone in the sector?

Mr Samuel—I am not sure it is an either or. I would suggest to you that, subject to the issues that we have raised in our paper, the code and the act do provide adequate enforcement tools.

Senator MASON—It is the lack of penalties.

Mr Samuel—Yes. That is a very important issue and it has been a big missing gap for certainly the five years that I have been involved with the ACCC. Can there be more enforcement? I have indicated this in public speeches, but it is not a hollow promise. For some three to four years now the issue of franchising and of small business has been a matter of high priority for the ACCC. There are many out there who claim that we ignore small business and we do not assist them. I have to say to you that results as much from an expectation gap as to what the ACCC is empowered to do under the Trade Practices Act versus what some in small business expect that we might be able to do. That does not apply in the case of franchising. We have adequate regulation there, but we need to keep in mind the two categories that are most populated in terms of the complaints, and they are the first two I described, that is, where franchisees do not want to take the matter any further, except to say to the ACCC, 'You do it, but don't ask us to get involved any more because we have not got the time or the desire and we are concerned about intimidation and pursuit of our core process', or alternatively, 'Look, what I told you I thought was right, but actually when you really asked me further and you made further inquiries, I know it is not exactly the way I described it to you ...' That sort of disparity between the evidence given and the complaint that is initially lodged with us does again raise an expectation gap. 'I complained to the ACCC. I have suffered great hardship, but the ACCC has not taken any action. Therefore, they are not enforcing enough.' No, we are enforcing. In fact, the extent of that expectation gap was so sensitive as far as we are concerned that we did something very unusual and quite unprecedented recently, and that is in relation to Baker's Delight. Normally when we conduct investigations we do not talk about them publicly. We will not even confirm or deny that we are undertaking an investigation if it is raised in the media or elsewhere. We have been very concerned about the expectation gap, and the fact that there are suggestions that the ACCC is not investigating thoroughly, or is not proceeding to an enforcement. Indeed, I note in one of the submissions it is suggested that we have been dishonest in our enforcement process, which I have to take objection to obviously and expressly deny that is the case.

We put significant details of our investigation processes and of the findings of those investigations on to our website, so that those who had complained, those who had been observing and others could observe the nature of the investigations that we undertook. It included what we found, what we did not find, why it was that enforcement action was not taken. It was all designed to try to bring a reality check to what is occurring in relation to these investigations.

Mr Cassidy—I would like to put this in context. We do not receive all that many franchising complaints. In the last financial year we had 517. About half of those were single complaints about a single franchise system.

CHAIR—As to the point of saying that, does that diminish the 517 cases?

Mr Cassidy—No.

CHAIR—That is the way it comes forward to us.

Mr Cassidy—We are looking at every one.

CHAIR—Just the virtue of saying, 'We don't get many complaints', immediately leads to the thought that there is no issue.

Mr Cassidy—No.

CHAIR—There are 517 individual cases. They are no less important than if there were just one good case that says there is a problem.

Mr Cassidy—That is true. I was not meaning to say that. The point I was trying to get across is in terms of the absolute number—and this is contrary to the impression that is sometimes created, particularly in relation to what I might call some of the more public franchisor arrangements where there have been problems—we are not receiving a great volume of complaints. But that is not to say they are not important.

CHAIR—I would say to you that the reason you are not getting them is that people do not believe you can do anything about them. You would get a lot more, but they have no faith in what you can do or will do.

Mr Cassidy—That is always hard to judge.

CHAIR—That may be, but that is certainly a view that is out there. You have confirmed it by saying to me that you do not get many complaints. That has just confirmed to me what I have been hearing, and what has been put to me. They say, 'We would go to the ACCC but, firstly, they are not going to do anything and, secondly, they don't really have the power or, thirdly, they are just not interested.'

Dr Schaper—Can I put that into some context?

CHAIR—Please. I want you to. That is why I am saying it. I am hoping you can.

Dr Schaper—The point that has been made about the number not being large relative to the number of firms participating in franchising as franchisees or indeed for that matter as franchisors; that it is a very small number relative to the overall business population that we have. This probably tips back to your previous question about the quality of regulation and—correct me if I am wrong—whether the number of complaints is indicative of some sort of systemic failure or systemic weaknesses in the Franchising Code of Conduct. We do not evaluate franchising across the planet on a global level, but there are a number of indicators that look at the quality of regulation that takes place right across the developed world. You may be familiar with the World Bank's annual review *Doing Business*. If you have seen that, you will know that Australia rates quite highly on that each and every year. For them—and this comes back to your earlier question—it is not necessarily the quantum of regulation that is the most important measure, it is the quality of the regulation.

It is impossible for us to prove a negative. It is impossible for us to prove that because there are only 500 there are an unknown number out there beforehand. But there are a number of other external indicators. There is that, but you have also probably looked at the New Zealand inquiry going on at the moment as well, which begs the matter that perhaps there are other countries that have identified a need to adopt franchising systems similar to ours. It is still a very small proportion, and just like a number of other indicators it indicates a fairly low performance.

Senator MASON—Just in terms of the numbers, there are 517 complaints. Breaking that down into your three criteria or outcomes, the first being the complaint with the information, the second being where evidence does not warrant litigation, and so on, how do those 517 break down?

Mr Samuel—I do not know that I can give you the exact numbers.

Senator MASON—That would be helpful. I can understand the chairman's point.

Mr Samuel—I will try to give you a bit of an estimate, because I can take 517, and I know what comes out at the end of the pipeline in terms of investigations that are proven up into matters that can be litigated.

Mr Ridgway—There would be 20.

Senator MASON—Are there 20 in category 3?

Mr Samuel—Yes, in category 3. It may be a bit more, possibly 25.

Senator MASON—Twenty-five?

Mr Samuel—Yes. I have to remember that there may be several franchisees associated with a single franchise. Don't tie me to the number, but it may be 25.

Senator MASON—No.

Mr Samuel—You have to remember that that 517 will be the number of complaints and/or inquiries lodged with the Infocentre, and very often they will be dealt with in the initial phone call. The phone call will say, 'I have run into a problem with a particular issue. How do I resolve it?' The advice is given, 'What you ought to do is contact the following people.' It will be categorised as a franchising complaint but may not actually be a matter that would be a breach of either misleading and deceptive conduct or the franchising code even at the first port of call. There is one thing I do want to emphasise, as I was endeavouring to say before. We can always play with statistics. I stated publicly at the National Small Business Summit run by COSBOA three or four years ago that as far as we were concerned these issues were a top priority for the ACCC. The staff of our enforcement division have been given a clear direction by the commission going back now over three years that these are fundamental issues that are top priority for the ACCC. Having been given that quite direct message does not alter the fact that so many of these complaints just fall into those first two categories where we cannot do anything.

CHAIR—I would like to ask you a question, because it is going to help, rather than you just talking at me. I need to seek some information that I am not getting. I think you have missed the point. It is not about the ACCC receiving complaints. The number is irrelevant. There is a whole range of people out there who deal with their initial complaint internally within the system. You will never hear about it, so it will not even register. There are a number of people who go through a mediation process outside of the ACCC process. There is a whole variety of methods out there where complaints and problems exist. You say there are low numbers, but that is just your view, in terms of what you do and not what takes place in the sector.

People that do not go to the ACCC are going to other places. The issue is not that there are not a lot or that it is not systemic. Neither of those are the issue. Not being systemic does not mean that a problem does not exist. What I am trying to deal with is where the actual problems exist. Even if you only ever got one complaint and a problem did exist within that complaint there is an expectation that you would actually follow it through. I hear you; that you are following that through. I am not questioning that.

What I am trying to establish is: where are the failings in the system that give you the power to act, to make some decisions, to following through deficiencies in either the Trade Practices Act or something specifically relating to franchising that perhaps hampers your ability? I can see in your submission you have made a number of suggestions and recommendations. I appreciate those, because there are some very good ones there. I might even take you to the second one, in terms of reviewing the mediation model. Could you explain what is wrong with mediation today? We have heard plenty about what does not work about it. Maybe you could tell us where you see it does not work and how we can improve mediation? That is your second dot point; reviewing the mediation model under the Code.

Mr Ridgway—Perhaps I could make one initial observation. Picking up a little on the issue of expectations identified before, there are also different expectations that parties have when they seek a mediated outcome. In our experience and in our discussions with those who are closer to the mediation process, the more successful mediations occur where there is some preliminary work done with the parties as to what they should reasonably expect from the mediation process itself and what they should reasonably expect in the circumstances in which they find themselves in that dispute.

Alternatively, we have seen on some occasions almost ambit sort of claim processes by some advocates for some complainants suggesting that extremely high outcomes are sought, and those individuals are sometimes encouraged not to reconcile their processes unless they achieve those very high outcomes. That, in itself, does not lend to a mediated outcome that is successful.

Dr Schaper—There are also other points that a number of commentators have made about possibilities for improvements. For example, an open-ended scale of fees for mediation services can work to the disadvantage of some franchisees, because for them it is not a legal process, but it can still be expensive. In their mind it feels almost as expensive as going to get legal advice.

CHAIR—We are only talking about the rogue segment. I am not talking about the ones that work out where there were different expectations and so on. There are plenty of good people. Putting a high figure on it, let us say it is 90 per cent or whatever. I am talking about the bad ones, the ones who want to do the wrong thing quite deliberately for their own purposes.

Mr Samuel—It is unlikely to be a case that would be suitable for mediation, though. If you are talking about a rogue, that is a case for litigation.

CHAIR—Perhaps there are those simple cases where it is just miscommunication, but for those who do not want to participate, you have a mediation process in place but really in the end it is meaningless because nothing needs to happen out of it. You basically turn up if you really want to and you can draw it out for as long as you like. You do not really have to comply with anything. I am trying to get to the nuts and bolts here. The ACCC needs to give us the nuts and bolts of what takes place on the ground. I need to sense that you understand that so we can take on your submission. For those who do not want to participate mediation is completely meaningless. We have an Office of the Mediation Adviser. They have data. The department has advised that basically that data is meaningless because in the end the outcomes of those are, in a lot of cases, not choice outcomes. You turn up. The franchisor says, 'You can do whatever you like. You either swallow this or not, but this is how it is going to be, and in the end we will terminate you.' It has been the case where people have been terminated while in mediation. They say, 'Accept our outcome or it's all over.' Where do we move on to next? Where is the ACCC movement in that area? How do we make the system better and fairer?

Mr Samuel—You have just used the word that can cause the greatest degree of complexity. You said, 'How do you make the system fairer?' I have to go back to my opening comments. The greatest point of leverage for the franchisee is the day before the contract is signed. He or she has got the money or the contract is not signed.

CHAIR—I will take you up on that one, because it is an interesting concept. It is a take it or leave it contract. They are standard form contracts. There is no negotiation. We have established that well and truly and there is agreement about that. With all the pre-education and all the good advice in the world that might keep some out, but somebody will sign. We know that as a matter of fact, so how do we protect those? Let us get beyond the fact that they should not get into it; they have. They are not all bad. Within a franchise system you might have a whole heap of players that do the right thing, but there might be one player in one particular region or state of Australia that decides to play outside the general rules of what would be acting in good faith, misleading conduct and all the stuff that is in the act.

Mr Samuel—Let us just distinguish this. If they are acting outside the bounds of misleading and deceptive conduct, then we take them on. If they are acting outside the bounds of what is required by the franchising code in terms of disclosure and the other prescriptive regulations, we will take them on and they will go to court.

CHAIR—You say that you would take them on, but would you take them all on?

Mr Samuel—Yes, where we can prove that there has been a breach of the franchising code or a breach of misleading and deceptive conduct or the more complex one, a breach of unconscionable conduct, then we will take them on and we do.

CHAIR—What about the high bar that I was talking about earlier? Let us get down to the nuts and bolts and the reality of what happens on the ground. If somebody decides through phone calls and verbal communication—we have plenty of evidence this is often what happens—then you cannot really establish that. You say the power lies in the contract up until

the moment you sign, but obviously people do sign. Once they sign, the contract does not really protect them in any way. That is why we have a code. But the code really just deals with disclosure, which is taken care of as pre-contractual. Post-contractual behaviour becomes the issue. Breaches can be really for anything. How do you equate that into it? It just seems from the ACCC's view and from your submission, apart from a number of suggestions about pecuniary penalties and so forth, that there really is not much of a problem and we should not tinker with it too much.

Mr Samuel—It does go to the heart of the rights and responsibilities of those that enter into contracts. To what extent does government and parliament wish to regulate the rights and responsibilities of those who enter into contracts? You say it is a take it or leave it, but of course the great strength of the negotiating party, the franchisee, is to leave it. If the contract does not suit—remembering that there is often a significant sum of money to be invested—you leave it.

CHAIR—Isn't that contrary to all other principles that we deal with? It is buyer beware and you are out on your own, but do we not have a heap of consumer laws to protect people just for that? It is not just a case of take it or leave it. It is much more than that.

Mr Samuel—When you go to buy a house, which often involves a significantly greater sum of money, and you go to an auction, the deal is take it or leave it, that is, you stand there, the terms and conditions of the contract are read out to you by the auctioneer, you either put up your hand or you do not.

CHAIR—With respect, that is a bit simplistic. It is not like buying a house that you own and can sell on. When you enter into a very special dependent relationship in terms of a franchise, you can have that house—if you want to use that example—taken away from you within seven days and have no legal comeback at all, because you have been breached for something you may or may not have done. I find it difficult to accept what you are saying to me in putting forward your views, that it is just like buying a house or it is like a contract. It is not. A contract between two people in the normal business world has a separate set of rules. This is a dependent relationship where one person does put on the value of a house, often much more than that—in fact sometimes their life savings and superannuation—and they are then dependent on the behaviour of that franchisor to ensure that, for example, six months down the track they are just not terminated for whatever reason.

Mr Cassidy—It might help if you direct us with a few more questions. We simply do not agree with some of what you are saying, your sweeping statement that they can be breached for something they have not done.

CHAIR—No, I did not say they could be breached for something they have not done.

Mr Cassidy—You said they could be breached for something they may or may not have done.

CHAIR—That is right.

Mr Cassidy—If they are breached for something they have not done then we go after them.

CHAIR—That is why there are disputes, because they may or may not have. Are you telling me that the franchisee is always in the wrong?

Mr Cassidy—No, not at all.

CHAIR—That is what I am saying; they may or may not have.

Mr Ridgway—If there is an indication of a breach that is not genuine, that is something we take seriously. As well as the disclosure regime, the code does provide a termination regime, which requires some reasonableness in the way that franchises are terminated. We have dealt with a number of issues since the code has been introduced that go to those provisions to ensure that franchisors observe those reasonableness requirements when they terminate.

CHAIR—How do you ensure that? How do you do that?

Mr Ridgway—In the event that someone receives an abrupt notice of termination that is not consistent with the code's requirements, the logic is they come to us to identify that, and they have from time to time. On those occasions we intervene and we put very promptly and very clearly to the franchisor involved the obligations they have under the code and ask them to justify why they are going about this process. In a number of those occasions, which do not generally make it to the press necessarily, they have adjusted their conduct and the issue has moved on. The dispute then is resolved according to the dispute processes under the code.

Ms OWENS—You have made a couple of suggestions about disclosure documents and end of franchise agreements. I would like to go through them. I am also wondering whether these suggestions have come about because of the analysis of complaints that did not necessarily fall outside the law but required a change in order to be fair. The first one is on the disclosure documentation. You have already said that you think perhaps the law is more onerous than the results, and I know it has been growing in height even over the last six months. I have heard that. There is also the limiting of disclosure of relevant information to prospective franchisees, the privacy laws, et cetera. Would you like to expand on that and tell us why you have come to those conclusions?

Mr Ridgway—In relation to the disclosure, other submissions might also have made it clear that there are some disclosure documents and so forth that, while they meet the requirements of the code, are quite legalistic, fairly obscure and hard to digest. In our view, given the information needs of a prospective franchisee at the time they are looking to make a decision, it would be more useful to have perhaps a shorter form of disclosure that goes more clearly to the primary risks that they are facing when they are considering their purchase. We have not thought through the detail, but some work could usefully be done in that direction.

CHAIR—How do you know whether they do or do not meet the code?

Mr Ridgway—A number of the concerns that come to us, say, two or three years down the track after a party has entered into a franchise agreement. They point back to their point of entry and suggest that there may have been some misleading conduct or some inadequate disclosure when they entered that agreement. As a norm, we will seek a copy of the disclosure document,

and often secure one, and then look and compare the information in that document against the requirements of the code.

Ms OWENS—What you are saying is that, even though they meet the requirements of the code, the code is not necessarily serving the interests of the relationships now?

Mr Samuel—Let me try to draw a parallel. It might be sufficient to substitute all the disclosure requirements of the code with a simple one-liner that says that the franchisor shall disclose to the franchisee, in a timely and meaningful manner, all information that would be material to the decision by the franchisee whether or not to enter into the franchising contract. The consequence of that, which sounds very simple and very adequate, is that the disclosure document will probably be five times its current volume, because the lawyers will say, 'This might be material and that might be material', so it will all be there. The prospects of it being useful to the franchisee will diminish almost in inverse proportion to its volume. But more importantly, that happens to be one of the fundamental tests of prospectuses today. Do investors read prospectuses? Some do, but too many do not, and then they complain afterwards when they lose their money when the share market falls 60 per cent, 70 per cent or 80 per cent or companies go broke. They will say, 'Yes, but we never realised.' That is the judgement that is required, sometimes assisted by competent legal and/or accounting or business management advice, and it is the judgement that also requires a bit of knowledge about who the franchisor is and whether the franchisor is a person of good repute. That does not always work, either, because we can point to certain prospectuses where you look at the board of directors or you look at the lawyers or accountants involved and make a decision to invest purely on that alone, because you are not going to read the several hundred pages of information that is provided in the prospectus, and guess what, it goes belly up.

Ms OWENS—You are also suggesting prohibiting franchisors from limiting the disclosure of relevant information through the use of confidentiality clauses. Have you seen that as a problem in what you have been looking at?

Mr Cassidy—There is already a provision in the code that prevents a franchisor from inducing franchisees not to associate with one another. To be quite frank, we have seen confidentiality clauses that do not seem to have any real commercial purpose, if I can put it that way, other than preventing franchisees from being able to discuss some fairly important details of their franchise arrangement with other franchisees.

CHAIR—Privileged information.

Mr Cassidy—We think the confidentiality clauses are being used to defeat that existing requirement within the code.

Ms OWENS—The end of the franchise agreement seems to be an area that is missing in a lot of agreements. Again, is this recommendation coming because you are seeing that in the complaints?

Mr Samuel—I noted as we walked in here the previous witness was making some comments about the particular Hungry Jack's franchise and the issues that have arisen there. There are two fundamental issues here. The first is that, if there is no statement made at all about what happens

at the conclusion of the franchise, you either have to draw certain implications or it may well be that by omission it becomes misleading or deceptive. So often what happens is that the franchising agreement does state—albeit in fairly complex legal language—exactly what the position is, but the franchisee, again, has not taken the appropriate advice at the time of entering into the franchise, gets to the end of the franchising arrangement and says, 'But what has happened to my goodwill? I expected this to be renewed. You told me in the beginning that it was going to be renewed. You didn't actually tell me, but I certainly had the expectation it would be renewed if it was successful. Now you are telling me it is lost, it is all over and my goodwill is lost. I put a lot of money into this. How has this happened?' Again, that is a question of getting some competent advice in the beginning. Chairman, you have said it is a take it or leave it, but I would have to say to you that if I were going to invest my life savings in a franchise that said to me that at the end of five years my life savings are lost, any goodwill I have built up by successfully operating the business is lost and I have got nothing to show for it, I would have to say that I would leave it.

CHAIR—I would say it is worse than that, because they can take it at any time. Every franchise agreement is not that at all. It is at the bare minimum just seven days. Your contract is actually for seven days or 30 days notice. Again, it is nuts and bolts and practical on the ground. For the rogue that is quickly manufactured and done. I am not saying that is the case all the time, but we are trying to deal with the ones that fall through the crack, the bad behaviours that are not accountable.

Mr Samuel—You do have to ask why any person would enter into it.

CHAIR—That is the whole franchising sector, though. You would have to ask the whole sector, because they all have that. We asked the MTAA: why would you spend $10 million to $15 million on an upgrade of a BMW franchise on the basis of a 12-month rolling contract? They said, 'We don't have any choice.' You only ever have a choice the first time you sign up. After that your sunk costs and your life investment mean you cannot just decide to walk away.

CHAIR—I will just draw you to the Kleins issue. In terms of disclosure, it would appear that right up until the last day, the point at which Kleins fell over, that no-one knew. I am making the assumption here that right up until the last day they were still out there selling and flogging the franchise. How is that possible under our existing laws in terms of trading insolvent?

Mr Ridgway—In terms of the requirements of the code and the Trade Practices Act, on the face of it the issue would go to the point in time at which the franchising firm understands it is no longer able to meet its payments as and when they fall due, which is the terminology of the insolvency regime.

CHAIR—This is historically fact. It is not about if, what if and maybe. This actually took place. That is my question: how is it possible under our existing laws? If you cannot give an answer, that is all right. I am just asking the question.

Ms OWENS—It is disclosure. Disclosure is prior to entering into the contract. There are no current requirements for updating?

Mr Ridgway—There are requirements for updating. It used to be something significant like going into administration. They would have 60 days to notify the franchisee. I think there is a common view, which was accepted by government in the last round of changes to the code that came into place this year, that that was an inadequate period of time and that was reduced to within 14 days of that event happening. The question is: how effective is that? That regime has only been in place since 31 March this year.

Ms OWENS—Other than that is there not a requirement at the moment for disclosure of other significant events that might affect the continuation?

Mr Ridgway—There are. There is a range of material information required to be disclosed within the period of time.

Ms OWENS—Are post-contract disclosure requirements sufficient?

Dr Schaper—There is always a trade-off between what is sufficient and what is practical. It is a bit like the issue about how you regulate the rogues as well.

Ms OWENS—Not with laws.

CHAIR—There are heaps of ways. That is why we have our regulations and consumer protection laws.

Ms OWENS—The ACCC does not become involved where the disputes are about the franchising agreement. I assume a lot of disputes are that, which would explain one of the reasons why so many of them are not with the ACCC. You have said that you feel the need to make mediation more accessible. What ideas do you have there? Clearly this is outside of the role of the ACCC.

Mr Cassidy—This goes again to some of the comments the chairman was making earlier. A number of what you might call those contractual issues do come to us. We refer a lot of them on to the mediation process, where a lot of them are satisfactorily resolved. In a sense that is why we have a bit of an interest in the mediation process. We do refer a lot on and we do get involved a bit. We like quasi mediation ourselves in terms of getting franchisor and franchisee talking to one another about what is basically a contractual dispute. I missed the second part of your question.

Ms OWENS—You have made some remarks about the need to try to make it more accessible in terms of cost, and changing the name of the OMA.

Dr Schaper—I do not think there is any doubt that the more access we can give small businesses to mediation as an option—not necessarily as the only route but as an option—it improves their faith in the system. In our case we have a mediation process for a particular code, but also because many small businesses generally find that access to the legal system is difficult due to cost, because of the evidentiary requirement and so forth. In that sense, mediation would be desirable in order to give them another option to settle disputes and to help deal with that power imbalance especially between a large firm and a small firm.

Mr Samuel—Is there a magic bullet for dealing with mediation? Not in these sets of circumstances, because mediation so often occurs as a result of litigation that has been commenced, and the judge in the court will say, 'I order the parties to mediation.' The mediation process then takes place under an aura of a court order. I guess the aura is that, if the parties do not undertake mediation in good faith, the court may take a dim view of the party that has not engaged in an appropriate mediation process.

Where we are dealing with contractual disputes in franchising matters that are not before courts, as the Chairman noted before, if one party says, 'I am just not going to participate in this mediation' or, 'Yes, I will attend the mediation, but I have no intention whatsoever of mediating or permitting the matter to be resolved, other than you take it on this basis or else', there is not a lot that you can do. You cannot regulate for—

Ms OWENS—People who break laws.

Mr Samuel—No, you can.

Ms OWENS—I know that, but you cannot stop lawbreaking with laws.

Mr Samuel—You cannot regulate to force people to engage in a reasonable mediation process.

CHAIR—You raised the issue of good faith. I thought I would wait until you raised it before I did.

Mr Samuel—I did not raise it in the context of—

CHAIR—No, but I thought this would lead me into it, anyway.

Ms OWENS—I do not believe you can stop lawbreakers by introducing more laws. They just break them. You can just have better penalties for when they do.

Mr Samuel—If you have laws that have teeth, and the teeth in this case involve penalties of hundreds of thousands or, as we have under part VC, over $1 million, that imposes something a little more concerning on those who break the laws. There is something more involved.

CHAIR—The issue of good faith has come up in all of the public hearings and in every single submission. What is your view, in its most basic pared down concept, on the same principle of good faith that applies as we all understand it to be the case, whether it is industrial, et cetera? Would including that in the code in its most simplest form give it a bit more teeth? Would it add some weight? On the other hand, would it be a negative? Would it somehow diminish people's capacity?

Mr Samuel—I think it would significantly increase the expectation gap. I am not sure whether that is a wise thing to do. The expectation gap is significant at the moment.

CHAIR—Why?

Mr Samuel—I will just explain that. You have indicated that there are parties out there that say, 'We don't bring our complaints to the ACCC because they will not do anything about it.' I would like to point out a public challenge now: show us a complaint that the complainant is prepared to back up with the appropriate evidence that it is a breach of the Franchising Code of Conduct or a breach of the misleading and deceptive conduct provisions. I will make it easy; I will not go as far as the unconscionable conduct provisions. Show us circumstances where the ACCC has said, 'We're not going to pursue that matter because we just are not interested', and I will come out and publicly apologise. There is the challenge. I just do not believe it is happening. I hope that is safe.

CHAIR—Too late now if it is not.

Mr Samuel—I am happy to apologise if that can be demonstrated. There is that expectation gap. On top of the prescriptive requirements of the Franchising Code of Conduct and of the relatively low threshold of misleading and deceptive conduct, that is, have you been honest or have you been dishonest, layer on top of that this somewhat hazy, woolly concept of good faith, and all I can say to you is that we will end up having is an increased expectation gap where people will say, 'But I believe that the franchisor did not act in good faith, and the ACCC wouldn't deal with it.'

CHAIR—How can you say it is hazy, woolly good faith when it is already there?

Mr Samuel—No. It is there as a guidance issue in relation to conscionable conduct. It is there as an indication, as a criteria.

CHAIR—It is not hazy.

Mr Samuel—I beg to differ with you. The courts would regard it as quite hazy, and it is one of the reasons why I indicated before that we will go down the route of pursuing a misleading and deceptive conduct or a breach of the franchising code as the route that will lead to a timely resolution of a matter through the courts. If you have to go down the unconscionable conduct route the evidentiary burden is so much more significant. The time involved not on the part of our investigators but on the part of those who are providing evidence, which are often small business people, is significantly greater, as is the process they have to go to in the court, because they have to show harsh and oppressive conduct. One of the elements involved in doing that is to demonstrate a lack of good faith. It is a complex process.

Ms OWENS—I have two questions. There is obviously a large gap in perceptions and expectations. What can we do to decrease that?

Mr Samuel—I was hoping you could provide the answer because it would solve one of the banes of our existence. These are issues that are created. I did say in the beginning that of the three categories of complaints that we receive almost all of them involve significant hardship as far as franchisees are concerned. I will not mention a name, but I had a particular franchisee ring me—and I took the call personally—to describe the hardship that the franchisee was going through in terms of the bank, et cetera. I listened and lent a sympathetic ear and then referred on to one of our investigators. They listened, but they said that as much as they understood the hardship there was nothing they could do. Interestingly, I received a responsive email from the

franchisee concerned to say, 'I really appreciate the fact that you listened, that you heard what I had to say, but I also appreciated the fact that nothing could be done.' That is an unusual case.

CHAIR—Who builds up the expectation?

Mr Samuel—Do you want me to get into trouble by naming people?

CHAIR—No.

Senator MASON—Is it parliamentarians?

Mr Samuel—No, it is not parliamentarians.

Senator MASON—It is a serious question.

Mr Cassidy—There is a serious answer. I will not name them, but there are certain people operating in the franchise sector as supposed advisers who I must say are more in the nature of carpetbaggers than genuine advisers. They show up, tell a franchisee who is out of pocket for whatever reason, 'Yes. This is a clear breach of the law. You have a right of action.' There is probably some fee involved for that sort of advice.'

Senator MASON—No, sorry—

Ms OWENS—I was just not talking about that.

Mr Samuel—This is going to the expectation.

Mr Cassidy—That is part of what is occurring, the expectation. There are people who are out there who are quite deliberately, we think, not giving full advice on what the state of the law is.

Mr Samuel—There are those who have a fairly high profile in this area and do exactly the same thing. It is not parliamentarians. This is outside the parliamentary scene. There are people with various titles after their name representing various associations as the case may be. The association consists of one person, that is, the person who is the spokesperson. They are out there and enjoy the profile. They are out there making extravagant and exaggerated comments. In my view, very often those comments are frankly dishonest. They are dishonest to the extent that they are misleading franchisees into believing that there are solutions to their problems, which are problems of extraordinary hardship, whereas in fact no law—and I would suggest—no judgement on the part of this committee would assess that what they have been subjected to is either unconscionable conduct or dishonest conduct, but what has happened is that there has been misfortune in the conduct of the franchise.

Ms OWENS—Is there a way to lessen that?

Mr Samuel—Yes, there is. In one or two cases we have had to, shall we say, strongly suggest to the proponents of this misinformation that they may themselves be engaging in misleading and deceptive conduct, which has been very interesting in terms of the consequences. That is not to quieten people down or to silence them or to silence criticism. It is to say to people, 'If you

engage in the practice of providing advice to franchisees that is clearly misleading and deceptive, then you are as guilty of a breach of part V of the act as the franchisors you are alleging have engaged in similar conduct. That does create an expectation gap. The expectation gap has been there consistently. It is sometimes created at the political level, but I have to say to you that is not often.

Dr Schaper—The expectation gap that you suffer is not dissimilar to the expectation gap that elected members suffer. There is a presumption that because you work in an organisation that has a wide reach it has a universal reach.

Ms OWENS—I was referring to the expectation gap between a franchisor and a franchisee, which I think Mr Cassidy was talking about as well. You are doing some training work and provision of materials, so obviously education is a part of it. Is there a need for a much greater focus on that?

Dr Schaper—We work with a variety of organisations. They range from educational institutions, universities and even some TAFE-level courses. In the past we have worked with bodies such as the Institute of Company Directors, from very small micro firms, business enterprise centres and other business advisers. It is a never-ending task, because you have a large number of new firms always entering into the market, and you have also got a turnover of business owners and managers as well. The level of knowledge out there is very hard to maintain because it is not a fixed constant and you cannot improve it simply by adding more to the level. In terms of the range, it is fairly extensive—print media, educational, sometimes collaborative with other government agencies, small business advisory centres and professional advisers, as well as the general media. It is a fairly multipronged strategy.

Mr Samuel—I am sorry to have to go back to my analogy from before. How do you require a home buyer to check for termites or rotting stumps before buying the home of their dreams?

CHAIR—That is easy.

Mr Samuel—How do you require a prospective franchisee to check all of the issues and to get the right advice before entering into the business of their dreams? That is so often the hard part.

CHAIR—We explored that a little bit earlier. Let us say they do all of that. Let us say they are the most educated, they have the best possible information and they have done all the due diligence, but they run into problems. Let us say there are problems with a franchisor who is not the best quality. It is not necessarily about breaches of law but abuse of power. Again, I am trying to get to the practical bits as to where problems do arise. I am trying to find a remedy that works for both sides. Let us not create more regulation and more burden. The majority work quite well. Let us look at the ones who are not operating well, who believe the environment is weak and therefore they can basically do whatever they like. You have made some suggestions that are very good. Civil pecuniary penalties are a good start, having a bigger penalty up front. That is not going to affect the good actors within the sector, because they are not going to be breaching anything, anyway. Franchising is different. Again, acknowledging that it is not like any other relationship or contract. It is not like buying a house or a car. This is a dependent

relationship where you sink a lot of yourself, including your time and investment. How do we protect in those areas?

Mr Cassidy—I suspect the answer is that there is not a single answer.

CHAIR—That is okay; I was not looking for just one. I am happy to have a range of views.

Mr Cassidy—As you say, we have talked about the incentives and penalties. We have talked about being able to undertake risk based audits, where we do get some indication that perhaps a franchisor is operating close to the wind, and not a hard allegation that gives us a basis for using our existing formal investigative powers. You do get a bit of a sniff that maybe a particular franchisor is pushing the envelope, if you like. This goes to the ability to undertake what we call a risk based audit. In other words, look at the disclosure documents that are being used, see what other material is being put out by a particular franchisor, perhaps speak to other franchisees of that franchisor to see whether we can get a pattern of conduct occurring. You can do things like that which go to address that sort of issue. I could not say to you that it is going to solve it completely, but equally I do not think there is a single answer that will solve it completely.

CHAIR—Is the ACCC the best body to do that? Do you need an extra adviser or role? Let us just say that the ACCC is the best place for this to take place. Is there a go-to place, a one-stop shop as it were that everyone out there in the sector understands this is where you go. It appears to me from all the evidence we have received that there is not. Certainly, some people come to the ACCC. Others use other formats. Others just go and see their lawyer or accountant. Is there room for that?

Mr Samuel—That will be for different reasons. They will come to the ACCC if they believe that there is a rogue involved who has breached the code or the honesty provisions of the Trade Practices Act. That is the appropriate time to come to the ACCC.

If there is a breach of the contract, that is, the disclosure has been absolutely accurate, but clause 21 of the contract has been breached by the franchisor and the franchisor is not supplying goods of the right quality, or is not supplying them at the right time, or whatever might be the case under the contract, then that is a contractual breach. It would be a very unusual step to say that the ACCC should be enforcing contractual breaches. That is when the lawyers have to get involved, when it becomes a private contractual matter. Of course, the OMA, the Office of the Mediation Adviser, also becomes involved to try to resolve those issues.

CHAIR—Does that lead itself into maybe a tribunal or an ombudsman? We have certainly had suggestions of some sort of circuit-breaker. We do not want to escalate things. We do not want to all end up in litigation. We are trying to mediate as quickly as possible and get it out of the road.

Dr Schaper—To some extent there already is an answer to that in the sense that the Commonwealth already funds a network of small business advisory centres right across the country. That serves as your primary contact point, principally the business enterprise centres.

CHAIR—I am talking about somebody with some power, like a Banking Ombudsman.

Dr Schaper—Before you get to that, your first point of contact is often about sorting out what is the nature of the matter. Is it a contractual matter? Is it something that is not purely in the domain of the written contract, but simply some managerial misunderstanding? There is a variety of areas. I do not think it is necessarily possible to pull it all into one source and then say everything can be resolved here.

CHAIR—Let me give you a practical example that might help to give an answer. You sign up in good faith, having done your due diligence. It is an excellent franchise system. It is all good, there is nothing wrong with it and you are going to make money. You open up in place X and a week later the same franchise decides to open up a store across the road in competition to you.

Mr Samuel—I would have to say that you have not had decent legal advice. No-one in their right mind would enter into a contract that allowed that to occur.

CHAIR—It has happened. But it is silent in the contract.

Mr Samuel—You are not allowed to be silent.

CHAIR—It is a take it or leave it. It is a standard form contract. There is no negotiation.

Mr Samuel—As long as I have my cheque in my hands and have not signed it, and as long as I have my pen in my hands and have not signed the franchising contract, in those circumstances—I am not saying I am smarter than anyone else—

CHAIR—That misses the point. What can we do to protect every single person who does sign? It is not about the ones who do not sign. They are protected by not being involved. I am talking about those who do sign and it is silent. If you are an expert and you have had 20 years experience in the franchising sector maybe you know that up front, but you might not know that.

Mr Samuel—In putting the question to us before, you started with a presumption, which is that this is a good contract and you have had full legal advice.

CHAIR—Let us just deal with the contract. No-one knew; it was just decided at the time—

Mr Samuel—With respect, a contract that allows the franchisor to open up another franchise—

CHAIR—They all do.

Mr Samuel—I would be surprised that that was the case.

CHAIR—If you are telling me they do not, then you are also telling me that you have looked at all the different contracts.

Mr Samuel—No, I have not looked at them. I could not possibly look at all the contracts.

CHAIR—I would say the ACCC has not looked at many, only the few that have been brought to you.

Ms OWENS—I could ask that another way. In most of your talk about taking action you tend to leave unconscionable conduct aside because it is obviously very difficult. Is that bar too high, given the uneven nature of the relationship?

Mr Samuel—That is a question that is often asked. It is being tested at the moment in relation to some matters that are before the courts, and may well be tested in the not-too-distant future with some other matters that could well go before the courts. It is not a question of it being too difficult. I wanted to be correct on that. In relative terms it is difficult compared to misleading and deceptive conduct. What do you do? In terms of getting a timely outcome that is satisfactory and does not involve the franchisee in significant time, cost and in some cases—I do not want to put it at too high a level—a trauma in having to go to court and give extensive evidence, it is so much easier to go down the route of misleading and deceptive conduct, breach of the franchising code.

Is unconscionable conduct too high? Back in 2003 we attended a Senate committee concerned with the application of the Trade Practices Act for small business. We offered some suggestions as to how unconscionable conduct provisions might be made clearer and easier for us to pursue. Those suggestions have now been adopted. I am not sure that the bar is so high that we would be saying to you that it ought to be lowered or significantly changed. We need to be careful that we do not start imposing—by setting a lower bar—a regulatory imposition on normal contractual dealings between parties that starts to step across the bounds of allowing parties to engage in their own contractual arrangements and their own contractual negotiations. But this does bring me back to the comment I made before. I am sorry, but it is like the termites and the rotting stumps. People will look at a house, 'It's my dream.' They will sign a cheque to buy the house and then afterwards, 'Why didn't I look for the termites? Why didn't I look for the rotting stumps?' In terms of a franchise arrangement the amount to be invested is often a lot less than the investment in a house.

CHAIR—It is often a lot more as well.

Mr Samuel—Yes, though with current housing prices who knows. All I would say to you is that there is a due diligence to be entered into, and the due diligence in respect of a franchising arrangement is often a lot more difficult but requires a lot more expertise, because you are dealing not with just the rotting stumps, termites or the contractual terms and conditions of the purchase. You are dealing with a longer term relationship and all of that needs to be governed by the legal relationship between the parties.

CHAIR—Thank you for that. I will draw you back to my example, just as a way of drawing all of the possible circumstances into just one example. I would suggest to you that if you are buying a house one of the first things people do all the time—as far as I know—is a range of checks, such as termite checks, engineering checks. There are heaps of regulations to protect people in terms of that purchase. It is a highly regulated area, exactly for that reason; it is a major purchase. With all due diligence done somebody will buy a franchise. There are not too many just going begging. Somebody will get in there. There is some level of protection. In those areas—and I can pretty much assure you of this from my understanding of evidence that we have received—your territorial area and the ability of the franchisor to open a competitive store across the road from you exists. They can do that. There is nothing you can do in pre-contractual due diligence or anything else that would prevent that happening. With those types of examples, then

we look to some sort of protection or some sort of mechanism that gives people recourse. Where is that recourse? There is no breach of law, but it will drive you out of business. It is not about how good you are as an operator. The company deciding to set one up across the road and ride you out is an example of just one of the many things that could take place.

Dr Schaper—Your previous comment was about the need for the ombudsman or a related role. The first point to note about that is that some jurisdictions have experimented with a similar role. For example, Victoria has a Small Business Commissioner. We work with the Office of the Small Business Commissioner quite closely. Indeed, I have held a similar position myself.

Other jurisdictions, for example, some states in the United States, have experimented with similar roles, but at the end of the day none of them has been given the ultimate power to oversee or moderate every aspect of the business relationship, because it simply is not practical. There are sufficient safeguards in the way the ACCC is structured. It has a deputy chair with a small business background. It has a franchising consultative panel. It has a variety of other tools. I just do not think that you can manage every aspect of the relationship through a central government agency. There are inevitably some aspects that really do come down to what the franchisee and the franchisor do.

CHAIR—This is why we have a code and this is why we have the Trade Practices Act.

Dr Schaper—There is a part about culture change and trying to encourage that we have a culture where franchisors endeavour to do their best and where franchisees are fully aware of that. As we said before in answer to your earlier questions, that is something we work on constantly.

Mr Samuel—I might refer you to paragraphs 8.1 and 8.2 of the Franchising Code of Conduct, which require disclosure as to whether or not competing businesses can be opened by the franchisor or by other franchisees within the franchise territory. You said that franchising agreements contain this. I am going back too many decades to when I was a lawyer, but even as a young articled clerk, whenever I was dealing with a purchase of business or sale of business a fundamental clause included in every purchase of business or sale of business said that the vendor cannot compete with the purchaser in that business or in a similar kind of business for a given number of years. That is why I am surprised to hear that a competent lawyer—

CHAIR—Yet it does happen in franchising. That is the problem.

Mr Samuel—I do not claim I was a competent lawyer as an articled clerk.

CHAIR—No, I am not questioning your ability.

Mr Samuel—I am surprised that a competent lawyer would allow that to occur today.

CHAIR—Even with that it still happens. People understand it is there in writing in the code, yet major franchises—and not many do this; this is just about the rogues—still do it. Where is the failure there in terms of those types—

Mr Samuel—With respect, the failure is on the part of the legal adviser, if a legal adviser is sought, to allow his or her client to enter into a franchising arrangement that allows a franchisor to effectively strip away the value of the franchising business by allowing the sorts of circumstances that you have described. As I said, as an articled clerk I used to put that into every sale of business agreement.

Senator MASON—Mr Samuel, you are a very generous man, I can tell. I thought that every parliamentarian in Australia thought that you and the ACCC could solve the ill of every national and international marketplace very easily. I assumed that. I can tell you are not going to say anything about that.

Mr Samuel—Is that a statement or a question?

Senator MASON—It is just a reflection. The chair and Ms Owens have touched on this. Do you believe you have sufficient quivers in your legal armoury to sufficiently protect franchisees except, as the chair has pointed out, with respect to monetary penalties? Is that right?

Mr Samuel—Yes. I would say that is so. We have commented upon the disclosure requirements of the franchising code in terms of volume versus quality. We do think that is something worth reflecting upon. I would have to say to you that we think the combination of the three arrows that we have is adequate.

Senator MASON—You said before that you would apologise if you had not pursued or prosecuted matters that you should have.

Mr Samuel—That is correct.

Senator MASON—In other words, you are using your ACCC powers appropriately. Obviously you are arguing that?

Mr Samuel—Correct, yes.

Senator MASON—They are the two issues that we have heard today. Firstly, you may not have sufficient legal powers and, secondly, you are not using those powers appropriately. That is the general claim, but obviously you are denying that?

Mr Samuel—Clearly. As I said, I would publicly apologise if it could be demonstrated that that were not the case.

Senator MASON—Thank you.

CHAIR—I thank the ACCC, everybody in the gallery, Hansard, the secretariat and other committee members.

Committee adjourned at 3.56 pm