
THE FRANCHISE LAW REVIEW

SECOND EDITION

EDITOR
MARK ABELL

LAW BUSINESS RESEARCH

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THE FRANCHISE LAW REVIEW

Second Edition

Editor
MARK ABELL

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EDITOR'S PREFACE

Since the publication of the first edition of *The Franchise Law Review*, there have been some significant economic and geopolitical developments that have had a significant impact on world trade. The apparently inexorable march towards the globalisation of commerce, however, has again continued unabated despite, or perhaps even because of, these changes.

Despite the slow emergence of a few economic bright spots, the economy of what was once called the 'developed' world continues on the most part to struggle, while even Brazil – one of the much-vaunted BRICS nations – has fallen into recession. As a consequence, businesses are often presented with little choice but to look to more vibrant markets in Asia, the Middle East and Africa for their future growth.

At the same time South–South trade is on the increase, perhaps at the expense of its North–South counterpart. All of this, coupled with the unstable wider geopolitical landscape, presents business with only one near certainty: there will be continued deleveraging of businesses in the coming years and, thus, growing barriers to international growth for many of them. All but the most substantial and well-structured of such businesses may find themselves facing not only significant difficulties due to their reduced access to funding to invest in their foreign ventures, but also challenges arising from their lack of managerial experience and bandwidth.

Franchising, in its various forms, continues to present businesses with one way of achieving profitable and successful international growth without the need for either substantial capital investment or a broad managerial infrastructure. In sectors as diverse as food and beverages, retail, hospitality, education, health care and financial services, it continues to be a popular catalyst for international commerce and makes a strong and effective contribution to world trade. We are even seeing governments turning to it as an effective strategy for the future of the welfare state as social franchising gains still more traction as a way of achieving key social objectives.

Given the positive role that franchising can make in the world economy it is important that legal practitioners have an appropriate understanding of how it is

regulated around the globe. This book provides an introduction to the basic elements of international franchising and an overview of the way that it is regulated in 32 jurisdictions.

As will be apparent from the chapters of this book, there continues to be no homogenous approach to the regulation of franchising around the world. Some countries specifically regulate particular aspects of the franchising relationship. Of these, a number try to ensure an appropriate level of pre-contractual hygiene, while others focus instead on imposing mandatory terms upon the franchise relationship. Some do both. In certain countries there is a requirement to register certain documents in a public register. Others restrict the manner in which third parties can be involved in helping franchisors to meet potential franchisees. No two countries regulate franchising in the same way. Even those countries that have a well-developed regulatory environment seem unable to resist the temptation to continually develop and change their approaches to regulation – as is well illustrated by the new changes in the Australian regulations.

Many countries do not have franchise-specific regulation, but nevertheless strictly regulate certain aspects of the franchise relationship through the complex interplay of more general legal concepts such as antitrust law, intellectual property rights and the doctrine of good faith. This heterogeneous approach to the regulation of franchising presents yet another barrier to its use as a catalyst for international growth.

This book certainly does not present readers with a full answer to all the questions they may have about franchising in all the countries covered – that would require far more pages than it is possible to include in this one volume. It does, however, try to provide the reader with a high-level understanding of the challenges involved in international franchising in the first section and then, in the second section, explain how these basic themes are reflected in the regulatory environment within each of the countries covered.

I should extend my thanks to all of those who have helped with the preparation of this book, in particular Graeme Payne, Victoria Hobbs, Caroline Flambard and Melissa Murray, who have invested a great deal of time and effort in making it a work of which all those involved can be proud.

It is hoped that this publication will prove to be a useful and often-consulted guide to all those involved in international franchising, but needless to say it is not a substitute for taking expert advice from practitioners qualified in the relevant jurisdiction.

Mark Abell

Bird & Bird LLP

London

February 2015

Chapter 15

AUSTRALIA

*Philip Colman*¹

I INTRODUCTION

Franchising is a sophisticated and stable sector of the Australian economy. This is supported by the Asia-Pacific Centre for Franchising Excellence at Griffith University, which notes in its report 'Franchising Australia 2014' that, based on its research:

There are approximately 1160 business format franchisors in Australia in 2014; compared with 1180 in 2012.

There are an estimated 79 000 units operating in business format franchises, reflecting an increase of 8.2 per cent increase since 2012.

More than 460,000 people are employed directly in franchising.

Sales turnover of the entire franchising sector was estimated at A\$144 billion.

86 per cent of franchise systems originated in Australia.

Some 30 per cent of franchisors have entered international markets.

Only 1.5 per cent of franchisees were involved in a substantial dispute with a franchisor over the past 12 months.

Fully 45 per cent of franchise systems engage in online sales with customers.

Despite it being reported that 86 per cent of franchise systems in Australia are 'home-grown', many foreign-based systems are well established in Australia. They include KFC, McDonald's, Subway, 7-Eleven, Marriott, InterContinental Hotels, Lift Brands, Europcar, Jani-King and Curves.

Nevertheless, Australia has many home-grown successes, including Bakers Delight, Boost Juice, Hairhouse Warehouse, Jim's Group, Autobarn, Nanotek and Priceline Pharmacy.

¹ Philip Colman is a partner at MST Lawyers.

The Franchise Council of Australia Limited is the peak body for the franchise sector in Australia, representing franchisees, franchisors and service providers to the sector.

II MARKET ENTRY

i Restrictions

Subject to the foreign investment laws referred to below, foreign business entities are not precluded from operating a franchise system in Australia (including granting master franchise or development rights to local entities) provided they comply with Australian law (particularly laws governing franchising outlined below). A foreign business entity may establish an Australian subsidiary in accordance with the Corporations Act 2001 (Cth).

If the Australian subsidiary is an Australian private company, at least one director of the company must reside in Australia. If the company is an Australian publicly listed company, that company must have at least three directors (two of whom must reside in Australia).

Foreign investment is governed by the Foreign Investment Review Board (FIRB). Whether foreign investment approval is required depends upon the type of investment and whether the investment is above a monetary threshold. Most residential real estate acquisitions require prior FIRB approval, as do certain acquisitions of commercial real estate. Acquisitions of shares in or assets of businesses valued at more than the applicable monetary threshold (which as of 1 January 2013 is A\$248 million for non-US investors) require FIRB approval. For US investors, the free trade agreement between Australia and the United States has established different criteria and threshold values depending on whether the investment is within a 'prescribed sensitive sector' of industry. In most instances, these scenarios will not apply to a prospective foreign franchisor, unless it proposes to enter the Australian market via an acquisition. Further information can be obtained from the FIRB website at www.frb.gov.au.

ii Foreign exchange and tax

There are several key tax considerations relating to cross-border franchising in Australia. These can apply to both inbound and outbound transactions and to franchisors and franchisees:

- a* Residency and double taxation: in which country or countries are you liable for income tax?
- b* Foreign exchange; how are dealings in foreign currency treated and when are they subject to tax?
- c* Withholding tax: is withholding tax payable, what rate applies and is double taxation an issue?

- d* Goods and Services Tax (GST): is GST payable and if so who is liable to pay the GST? Is this a cash-flow issue or does this impact your profitability? GST can be a real cost in relation to international transactions.
- e* Transfer pricing: are dealings between parties in different countries at arm's length and is the documentation adequate?

Some of these are discussed in more detail below. Careful planning and experienced tax advice is essential in dealing with these issues.

III INTELLECTUAL PROPERTY

i Brand search

IP Australia (the Australian government agency responsible for the administration of Australia's intellectual property) maintains databases of all registered trademarks, designs, patents and plant breeders' rights. These databases can assist in determining whether the use of a new brand name, logo, design or patent could infringe another party's rights. These searchable databases are available at www.ipaustralia.gov.au.

However, IP Australia's databases are limited in that they only contain information regarding registered rights. As a result it may difficult to ascertain whether a third party has any unregistered intellectual property rights, particularly in the case of prior use of unregistered trademarks or copyright. Searches of the Australian Securities and Investment Commission's databases of registered company and business names, domain name searches and general internet searches can assist in locating third parties that may have unregistered intellectual property rights, particularly in relation to trademarks.

ii Brand protection

Applications to register an interest in intellectual property must be made through IP Australia either online or in paper form. The registration process differs depending on the particular right you are trying to obtain. Generally applications will be subject to an examination by IP Australia to determine whether the registration should be accepted. Third parties will have an option to oppose the applications before they are registered.

More detailed information regarding each particular registration process is available at www.ipaustralia.gov.au.

In Australia there is no system of registration for copyright. If the material satisfies the statute, copyright protection will exist automatically.

iii Enforcement

Australia does not have a regulatory body that enforces a party's intellectual property rights. It is the responsibility of the party with an interest in the intellectual property to enforce its rights, usually by way of court proceedings. A registered intellectual property interest generally gives the registered owner the right to prevent other people from using the intellectual property, or to obtain relief if the intellectual property is infringed. Such relief may consist of monetary compensation or the right to seek an injunction whereby the court orders the party to immediately cease its infringing behaviour.

Additionally, both registered and non-registered intellectual property rights may be indirectly enforced with the application of the tort of passing off and the statutory prohibition on corporations engaging in misleading and deceptive conduct.

iv Data protection, cybercrime, social media and e-commerce

In Australia there is no legislation regarding cybercrime, social media and e-commerce that specifically pertains to franchises. However, there is legislation that applies to most organisations in a more general sense.

New privacy protection reforms came into effect in March 2014.² These laws, known as the Australian Privacy Principles (APPs), significantly affect the way organisations collect, store, use, disclose and dispose of personal information about individuals. For example, organisations may be held accountable for sending personal information offshore if the recipient subsequently breaches the APPs. Additionally, the APPs limit the right to use personal information for direct marketing purposes in certain circumstances.³ There is a higher standard of protection afforded to sensitive information, which includes information about a person's sexual preferences, health and biometric data.

The Privacy Commissioner's powers include additional investigation and audit powers and the power to make enforceable undertakings, develop and register binding privacy codes and commence proceedings in the Federal Court or the Federal Magistrates Court. Penalties of up to A\$1.7 million can be ordered for serious or repeated breaches of the APPs by corporations and up to A\$200,000 for individuals. E-commerce has become a vital component of most businesses in Australia and as a result cybercrime has become a pertinent issue. The APPs require organisations to take reasonable steps to protect data from theft, misuse, interference, loss, unauthorised access, modification or disclosure.⁴

Currently there is very little legislation that deals directly with e-commerce. However, the Electronic Transactions Act 1999 (Cth) does contain provisions that promote business and community confidence in the use of electronic transactions. The Act states that a transaction is not invalid because it takes place wholly or partly by electronic communications.⁵ Additionally, the Act sets out when the requirement of a signature is satisfied in relation to electronic communications.⁶

Coupled with the growth of e-commerce trading is organisations' utilisation of social media communication channels. Australian laws will no doubt continue to evolve to govern the commercial use of social media outlets. The courts have recently ruled that companies may be held responsible for third-party comments posted on their

2 The Privacy Act 1988 (Cth), Schedule 1.

3 For example, organisations must not use personal data for direct marketing purposes unless the individual would reasonably expect the organisation to use the information for that purpose and the organisation provides a simple means by which the individual may easily request not to receive direct marketing.

4 The Privacy Act 1988 (Cth), Schedule 1, Australian Privacy Principle 11.

5 The Electronic Transactions Act 1999 (Cth), Section 8.

6 The Electronic Transactions Act 1999 (Cth), Section 10.

social media pages if such comments contravene Australian consumer laws or advertising standards.⁷ As a result, organisations are required to monitor their social media pages frequently to actively remove any defamatory, misleading or abusive comments posted by third parties.

IV FRANCHISE LAW

i Legislation

On 1 January 2015, the Competition and Consumer (Industry Codes – Franchising) Regulation 2014 entitled ‘Franchising Code of Conduct’ (the Code) replaced the former Trade Practices (Industry Codes – Franchising) Regulation 1998 (the Old Code). This is the primary franchise specific law in Australia.

The Code is a prescribed mandatory industry code under the Competition and Consumer Act 2010 (Cth) and is underpinned by that Act by virtue of that Act providing that a person must not, in trade or commerce, contravene an applicable industry code.⁸

The stated underlying purpose of the Code is to regulate the conduct of participants in franchising towards other participants in franchising.⁹

The Code applies to conduct occurring on or after 1 January 2015 (other than to discharge an outstanding obligation that arose under the Old Code) in relation to a franchise agreement entered into on or after 1 October 1998.¹⁰ The application of the Code is dependent upon the existence of a franchise agreement. The Code acknowledges that a franchise agreement may be wholly or partly in writing, wholly or partly oral, or wholly or partly to be implied.

Hence, in determining Code applicability, one must look at the entire relationship between parties and necessarily ignore the title given to any document. When looking at that entire relationship one must positively answer all of the following questions for the relationship to be considered a franchise agreement:

- a* Does one person (the franchisor) grant to another person (the franchisee) the right to carry on a business of offering, supplying or distributing goods or services in Australia under a system or marketing plan substantially determined, controlled or suggested by the franchisor or an associate¹¹ of the franchisor?
- b* Is the operation of the business substantially or materially associated with a trademark, advertising or commercial symbol owned, used or licensed by the franchisor or an associate of the franchisor or specified by the franchisor or an associate of the franchisor?
- c* Is the franchisee obliged to pay money to the franchisor under its arrangement with the franchisor?

7 *Australian Competition and Consumer Commission v. Allergy Pathway Pty Ltd* (No. 2) [2011] FCA 74.

8 Section 51AD of the Competition and Consumer Act 2010 (Cth).

9 Franchising Code of Conduct, Clause 2.

10 Franchising Code of Conduct, Clause 3.

11 Defined in the Franchising Code of Conduct, Clause 4.

Then, having received positive answers to the above questions, one must consider whether the relationship falls under any of the exceptions. These are:

- a* where the only money payable by the franchisee to the franchisor under its arrangement with the franchisor is either:
 - payment for goods and services on a genuine wholesale basis;
 - repayment of loans from the franchisor to the franchisee;
 - payment for goods taken on consignment on a genuine wholesale basis; or
 - payment of market value for purchase or lease of real property, fixtures, equipment or supplies needed to start the business or to continue the business under the franchise agreement; and
- b* employer–employee relationships, partnership relationships, landlord and tenant relationships, mortgagor and mortgagee relationships, lender and borrower relationships, the relationship between members of a cooperative registered and operating under various state and territorial laws and ‘fractional franchises’.¹²

The Code imposes obligations on franchisors:

- a* to act in good faith towards franchisees¹³ (note that an identical obligation is also imposed on franchisees) – the mutual obligation to act in good faith is dealt with in greater detail below;
- b* to create and update and maintain¹⁴ a prescribed disclosure document¹⁵ (see below as to content);
- c* to provide the disclosure document to franchisees and prospective franchisees;¹⁶
- d* to refrain from entering into a franchise agreement until it has received signed certificates from the franchisee as to the obtaining or non-obtaining of legal, accounting and business advice;¹⁷
- e* to provide a prescribed information statement (containing an explanation of franchising and warnings about business risks) as soon as practicable after a

12 Franchises where the goods and services of the franchise are substantially the same as those sold for the previous two years by the franchisee before the franchise agreement was entered into, and sales of those goods and services are unlikely to provide more than 20 per cent of the franchisee’s gross revenue in the first year of the term.

13 Franchising Code of Conduct, Clause 6.

14 The obligation to create and update so as to be compliant with the Code does not arise until 31 October 2015 if the franchisor has an existing disclosure document created under the Old Code. Otherwise the obligation to update must be met within four months of the end of the franchisor’s financial year; however, the requirement to update does not exist if the franchisor did not enter into more than one franchise agreement in that financial year and the franchisor does not intend to enter into a franchise agreement in the next financial year.

15 This obligation does not exist for master franchisors in relation to sub-franchisees (i.e., where a sub-franchisor or master franchisee is interposed).

16 Franchising Code of Conduct, Clause 9.

17 Franchising Code of Conduct, Clause 10.

- prospective franchisee formally applies or expresses an interest in acquiring a franchised business;¹⁸
- f* to provide premises lease documents or information to franchisees, including details of any incentive or financial benefit that the franchisor or an associate of the franchisor might receive from a landlord;¹⁹
- g* to provide copies of other relevant agreements, such as those relating to intellectual property, security agreements, confidentiality agreements and restraint agreements;²⁰
- h* to prepare annual financial statements of any marketing or other cooperative fund within four months of the end of a financial year and have such statements audited²¹ and to supply to franchisees a copy of the statements and audit report within 30 days of them being completed;²²
- i* to provide a copy of its current disclosure document to existing franchisees upon request;²³
- j* to provide ongoing disclosure to franchisees²⁴ in relation to:
- any more recently issued statement of solvency, financial statement and audit report relating to the franchisor;
 - changes in majority ownership or control of the franchisor;
 - certain proceedings brought by public agencies against the franchisor or a director of the franchisor;
 - judgments against the franchisor under independent contractor laws;
 - civil proceedings against the franchisor by more than 10 franchisees or 10 per cent of franchisees;
 - certain judgments against the franchisor unsatisfied for more than 28 days;
 - the franchisor becoming externally administered (for example, because of insolvency);
 - material changes to intellectual property relevant to the franchise; and
 - undertakings given to the competition regulator (the ACCC) or orders relating to such undertakings;
- k* to advise franchisees within six months²⁵ of the end of the term of a franchise agreement whether or not the franchisor will extend the franchise agreement, or enter into a new franchise agreement;²⁶
- l* to keep proper records;²⁷

18 Franchising Code of Conduct, Clause 11.

19 Franchising Code of Conduct, Clause 13.

20 Franchising Code of Conduct, Clause 14.

21 Unless 75 per cent of franchisees agree that it should not be audited.

22 Franchising Code of Conduct, Clause 15.

23 Franchising Code of Conduct, Clause 16.

24 Franchising Code of Conduct, Clause 17.

25 This period is one month if the term of the franchise agreement is six months or less.

26 Franchising Code of Conduct, Clause 18.

27 Franchising Code of Conduct, Clause 19.

- m* to refrain from including in franchise agreements general releases of the franchisor from liability to the franchisee or waivers of verbal or written representation;²⁸
- n* not to include in franchise agreements litigation, arbitration or mediation venue provisions that require these processes to take place in venues outside the state or territory in which the franchised business is based;²⁹
- o* not to include in post-1 January 2015 franchise agreements clauses that require the franchisee to pay the franchisor's dispute resolution costs;³⁰
- p* not to unreasonably withhold consent to a request from a franchisee to a transfer of a franchise agreement where the request is accompanied by all information that the franchisor would reasonably require and expect to be given to make an informed decision;³¹
- q* to specify any conditions upon which consent to a transfer of a franchise agreement is given;³²
- r* to specify the reasons why consent to a transfer of a franchise agreement has been refused:
- if refused following the initial request;³³ or
 - if revoked under a right of revocation that exists for 14 days after the consent was given;³⁴
- s* to allow a franchisee to terminate the franchise agreement within seven days of signing it and paying non-refundable money;³⁵
- t* subject to limited exceptions,³⁶ not to terminate a franchise agreement because of a breach unless a breach notice has been served on the franchisee, the franchisee

28 Franchising Code of Conduct, Clause 20.

29 Franchising Code of Conduct, Clause 21; also note that this Clause only applies to franchise agreements entered into or varied on or after 1 January 2015

30 Franchising Code of Conduct, Clause 22.

31 See the Franchising Code of Conduct, Clause 25(2). Clause 25(3) sets out certain circumstances where it would be reasonable to withhold such consent.

32 Franchising Code of Conduct, Clause 25 (1)(b).

33 Franchising Code of Conduct, Clause 25(1)(a).

34 Franchising Code of Conduct, Clause 25(5).

35 Franchising Code of Conduct, Clause 26.

36 The exceptions, described in Clause 29, only apply if the franchise agreement gives the franchisor the right to terminate the franchise agreement. They are:

a the franchisee no longer holding a necessary licence to conduct the franchised business;

b franchisee insolvency;

c a corporate franchisee being deregistered under Australian company law;

d voluntary abandonment of franchised business or the franchise relationship by the franchisee;

e the franchisee is convicted of a serious criminal offence;

f the franchisee operating business in a way that endangers public health or safety; and

g the franchisee acting fraudulently in connection with the operation of the franchised business.

- has been given reasonable time to remedy the breach³⁷ and the franchisee does not remedy the breach within the reasonable time specified in the breach notice;³⁸
- u* to give reasonable notice to a franchisee of termination of a franchise agreement and the reasons for termination in circumstances where a franchisor exercises a contractual right to terminate where there is no breach by the franchisee;³⁹
- v* not to require a franchisee to undertake 'significant capital expenditure'⁴⁰ in relation to the franchised business during the term of the franchise agreement;⁴¹
- w* to maintain a separate bank account for marketing fees and advertising fees contributed by franchisees;⁴²
- x* to pay marketing and advertising fees in relation to units operated by the franchisor on the same basis as franchisees are required to contribute;⁴³
- y* to expend marketing and advertising fees only for expenses of the type disclosed in the disclosure document or otherwise legitimate marketing or advertising expenses, expenses agreed to by a majority of franchisees or the costs of administering and auditing the marketing fund;⁴⁴
- z* not to engage in conduct with the intention of influencing a former franchisee to request that his, her or its details be omitted from the disclosure document;⁴⁵

If one of these exceptions exists, a franchisor may immediately terminate the franchise agreement, unless the agreement provides otherwise.

37 This need not exceed 30 days.

38 Franchising Code of Conduct, Clause 27.

39 Franchising Code of Conduct, Clause 28.

40 The Franchising Code of Conduct, Clause 30(2) provides that significant capital expenditure does not include:

a expenditure disclosed in the disclosure document given on entering into, renewing or extending the term of the franchise agreement;

b if the expenditure is to be incurred by all or a majority of franchisees, expenditure approved by a majority of those franchisees;

c expenditure incurred by the franchisee to comply with legislative obligations;

d expenditure agreed by the franchisee;

e expenditure that the franchisor considers is necessary as capital investment in the franchised business, justified by a written statement given to each affected franchisee of:

- the rationale for making the investment;
- the amount of capital expenditure required;
- the anticipated outcomes and benefits; and
- the expected risks associated with making the investment.

41 Franchising Code of Conduct, Clause 30(1).

42 Franchising Code of Conduct, Clause 31(1).

43 Franchising Code of Conduct, Clause 31(2).

44 Franchising Code of Conduct, Clause 31(3).

45 Franchising Code of Conduct, Clause 32.

- aa* not to induce franchisees not to form or participate in a franchise advisory council or like body;⁴⁶ and
- bb* to include in the franchise agreement a complaint handling procedure that complies with the Code;⁴⁷

The Code also requires franchisors (as well as franchisees) to:

- a* act in good faith (see below);
- b* attempt to resolve disputes; and
- c* attend mediation through a duly authorised person.

ii Pre-contractual disclosure

A linchpin of the Code is the requirement for franchisors to:

- a* create (before entering into a franchise agreement) and update (within four months after the end of each financial year) a disclosure document that accords with the Code in terms of content and layout;⁴⁸ and
- b* to give its disclosure document (and a copy of the Code and the franchise agreement in the form in which it is to be executed) to prospective franchisees (including prospective franchisees who are acquiring an existing franchised business), renewing franchisees and existing franchisees where the term or scope of the franchise agreement is being extended, at least 14 days before the relevant documents are executed by the prospective franchisee or 14 days before a prospective franchisee pays to the franchisor any non-refundable money (whichever is the earlier).

The disclosure document requires franchisors to make disclosure under a number of key topics and subtopics. The key topics cover:

- a* background and relevant business experience of the franchisor, its associates and key personnel;
- b* details of relevant past and current litigation, convictions for serious offences or insolvency relating to or involving the franchisor or its directors;
- c* payments to agents for the introduction or recruitment of franchisees;
- d* details of existing franchisees and key events⁴⁹ that have occurred in the past three years;

46 Franchising Code of Conduct, Clause 33.

47 Franchising Code of Conduct, Clause 34. As to the nature of the complaint handling procedure, see clauses 38 and 39.

48 If, as at 1 January 2015, a franchisor has an existing disclosure document created under the Old Code, it will not be required to update its disclosure document so that it complies with the 2015 Code until the earlier of four months from the expiration of the franchisor's financial year or 31 October 2015.

49 Franchise transfers, businesses closing down, terminations, non-renewals and franchisor buy-backs.

- e* certain prescribed information as to the relationship between the franchisor (if the franchisor is a sub-franchisor) and the master franchisor;
- f* relevant information regarding intellectual property, including how and on what basis the franchisor can pass on rights to use such intellectual property to franchisees;
- g* details of exclusivity or otherwise of sites or any territory;
- h* details of franchisor's requirements for supply of goods or services to a franchisee;
- i* details of franchisor's requirements for supply of goods or services by a franchisee;
- j* rights, if any, of the franchisee to sell goods or services online;
- k* rights, if any, of the franchisor to sell goods or services online;
- l* any profit-sharing arrangement between the franchisor and franchisee in respect of online sales of goods or services;
- m* the franchisor's site or territory selection policy;
- n* circumstances surrounding past franchise businesses ceasing to operate in the territory to be franchised;
- o* payments to be made by a franchisee, including prepayments, establishment costs and other recurring or isolated payments;
- p* details relating to contributions to, expenditure from, administration and auditing, a marketing or other cooperative fund;
- q* details of any financing offered by the franchisor;
- r* details of unilateral variations to the franchise agreement in the past three years and circumstances where the franchise agreement may be unilaterally varied in the future;
- s* details of arrangements to apply at the end of the franchise agreement;
- t* details of whether the franchise agreement will be amended on a transfer or novation;
- u* any earnings information that a franchisor wishes to give and the basis for such information;
- v* a statement of solvency signed by a director of the franchisor;
- w* either financial reports of the franchisor for the past two financial years or an audit report supporting the franchisor's director's statement of solvency; and
- x* any other relevant updates pertaining to key changes that may have occurred since the disclosure document was created.

The disclosure document must have attached to it a copy of the Code and the franchise agreement in the form in which it is to be executed by the franchisee. In addition, it must include a form of receipt for signing and return by the franchisee.

If, after the date the disclosure document is given the franchise agreement is amended to give effect to a request by the franchisee or otherwise by filling in required particulars or correcting mistakes or to clarify minor matters, there is no need to re-disclose.

Violations of the Code can give rise to affected parties seeking a wide range of civil remedies, such as damages, injunctions and orders setting aside or varying the franchise agreement or the regulator (the ACCC) issuing an infringement notice (A\$8,500) or issuing legal proceedings seeking a civil pecuniary penalty of up to A\$51,000 per offence.

iii Registration

There are no mandatory requirements for the registration of disclosure documents or franchise agreements in Australia.

iv Mandatory clauses

The only mandatory clauses prescribed by the Code are those relating to complaint handling and dispute resolution. These are more fully described below.

However, in practice, franchisors mirror many of the provisions of the Code in their franchise agreements, particularly those relating to the cooling-off rights of a franchisee, termination and the procedure for considering requests for a transfer or novation of a franchise agreement.

v Guarantees and protection

As a general rule, guarantees given by persons to support the obligations of franchisees to franchisors are enforceable against the guarantors. The guarantee must be properly executed and it must not be procured by the fraud, undue influence or unconscionable conduct of the franchisor. Where guarantees are sought from persons who do not have equity in or a financial interest in the franchisee, prudent franchisors should insist that the guarantors obtain independent legal advice before accepting the guarantee.

V TAX

i Franchisor tax liabilities

Franchisors domiciled in Australia are subject to the following Australian taxes:

- a* income tax: Australian franchisors will be subject to Australian income tax on their worldwide income, including income from foreign sources. The current company tax rate is 30 per cent; and
- b* GST: GST (currently 10 per cent) must be collected on Australian sales and remitted to the tax office. This is only a timing issue and should have no impact on profits. Exports of goods and services may qualify for a GST exemption if strict conditions are met.

If the franchisor has foreign branch franchisees, they may end up paying double tax even if a taxation treaty exists. Further, payments received from foreign franchisees may be subject to withholding tax in a foreign country.

Foreign franchisors are subject to the following Australian taxes:

- a* income tax: if business is conducted through an Australian subsidiary, the subsidiary is liable for Australian income tax at the 30 per cent tax rate. A foreign-owned Australian subsidiary often results in double taxation because the profits are generally also taxable in the head entity's jurisdiction but without credit for any Australian tax paid by the subsidiary, particularly in the absence of a double taxation treaty. If a foreign entity has a branch in Australia, it is subject to Australian income tax on its Australian business profits. Franchisors will not ordinarily have a branch simply because they have Australian franchisees.

Branches can also result in double taxation even if a tax treaty exists. Careful structuring is the key;

- b* withholding tax: a foreign franchisor receiving fees from Australia may lose some of those fees in withholding tax. Contracts and costing need to account for this. Presently, franchise royalties are subject to a 30 per cent withholding tax; and
- c* GST: importers of goods into Australia are generally liable for GST on importation. If not properly structured, importation of goods can result in denial of GST credits leaving the franchisor or their agent out of pocket. ATO public ruling GSTR 2003/15 covers importation and GST.

ii Franchisee tax liabilities

Franchisees are subject to the following taxes:

- a* income tax: Australian-owned franchisees are subject to Australian income tax on their worldwide income. Fees paid to a franchisor will generally reduce the Australian taxable income of the franchisee. This may not be the case for payments such as upfront franchise fees and initial training, which may be seen as a capital and hence non-deductible expense;
- b* withholding tax: if withholding tax applies to payments made to foreign residents, the obligation to withhold tax rests with the franchisee. A denial of franchisees deductions will often occur until the withholding tax is paid;
- c* GST: as with foreign franchisors, the franchisee may be the importer of goods and should be aware of structuring issues, which may lead to the loss of GST credits on imported goods; and
- d* foreign exchange; foreign-denominated transactions must be translated into Australian dollars and gains or losses on currency movements are subject to Australian tax. Foreign exchange gains can sometimes be taxed on an accrued basis and not when received.

iii Tax-efficient structures

The key to cross-border franchising is being able to understand the interaction between the two jurisdictions' tax systems to avoid double taxation. This applies for all inbound and outbound transactions, and for both franchisees and franchisors.

There is no single optimal structure and each situation must be evaluated on its facts. Sometimes the use of trusts, partnerships, limited partnerships or hybrid entities can provide a better result by allowing foreign tax credits to pass through, and by avoiding double tax.

VI IMPACT OF GENERAL LAW

Australia is a federation of six states and two territories and has a common law-based legal system. Franchising primarily involves contractual considerations and, hence, the common law and equitable principles of contract developed or adopted by Australian courts play a significant part in franchising. It is not possible in this chapter to even summarise those principles other than to say that they are in many respects similar to those in the United Kingdom and, to a slightly lesser extent, the United States.

i Good faith

The Code mandates that each party or proposed party to a franchise agreement must act towards each other with good faith in accordance with the common law.⁵⁰ A court, in deciding whether there has been a breach of this obligation, may have regard to whether the party acted honestly and not arbitrarily and whether the party cooperated to achieve the purposes of the franchise agreement. Any clause in a franchise agreement that attempts to limit or exclude this obligation will be void.

Parties who act in their legitimate commercial interests are unlikely to offend this provision. Likewise the Code expressly provides that a franchisor who does not offer an option to renew or right to extend a franchise agreement will not be deemed to have acted contrary to the good-faith obligation.

The existing common law position in Australia is that:

- a* there is to be implied in every franchise agreement a term of good faith and fair dealing that obliges each party to exercise the powers conferred on it by the agreement in good faith and reasonably and not capriciously or for some extraneous purpose; and
- b* the scope of the duty is fettered in that it cannot operate to deny to a party the right to exercise a power conferred by the contract for the promotion or protection of its legitimate commercial interests.⁵¹

The former chief justice of the High Court of Australia (Australia's highest appellate court) Sir Anthony Mason has stated⁵² that good faith comprises three notions:

- a* an obligation on the parties to cooperate in achieving the contractual objects;
- b* compliance with honest standards of conduct; and
- c* compliance with standards of conduct that are reasonable, having regard to the interests of the parties.⁵³

The consequences of a failure to comply with the good-faith obligation include potential exposure to the affected parties seeking contractual remedies, such as damages, restitutionary orders, injunctions and the like as well orders varying the terms of a franchise agreement.

50 Franchising Code of Conduct, Clause 6.

51 *Far Horizons Pty Ltd v. McDonald's Australia Ltd* [2002] VSC 310; *JF Keir Pty Ltd v. Priority Management Systems Pty Ltd* (administrators appointed) 2007 NSWSC 789.

52 In his article 'Contract, Good Faith and Equitable Standards in Fair Dealing' (2000), 116 *Law Quarterly Review* 66.

53 This approach has been cited with approval in a number of cases including *Burger King Corp v. Hungry Jack's Pty Ltd* [2001] NSWCA 187 and *Hughes Aircraft Systems International v. Airservices Australia* (1997) 76 FCR 151. See also *Garry Rogers Motors (Aust) Pty Ltd v. Subaru (Aust) Pty Ltd* (1999) ATPR.

ii Misleading and deceptive conduct

The Australian Consumer Law, which is part of the Competition and Consumer Act 2010 (Cth), prohibits conduct that is misleading or deceptive or that is likely to mislead or deceive.⁵⁴ Allegations of breach of this law are very common in lawsuits and pre-litigation demands. They are also the most common type of allegation made by a franchisee against a franchisor. It is often alleged that a franchisee has been induced by pre-contractual conduct or representations to enter into a franchise agreement and that the conduct or representations were misleading or deceptive. The Australian Consumer Law deems representations as to future matters (for example, earnings projections) to be misleading and deceptive, unless the maker of the representation can prove that it had reasonable grounds for the representation.⁵⁵

The consequences of a finding of misleading and deceptive conduct in a civil suit include awards of damages, injunctions, orders for refund of money or, orders varying or rescinding a contract. If the regulator, the ACCC, brings proceedings, it can, in addition, seek pecuniary penalties, enforceable undertakings, publications orders and orders requiring the offending party to implement a trade practices compliance programme.

These laws are of wide application and also apply to marketing and credence claims in relation to goods and services that are offered for sale. The regulator, the ACCC, has and remains very vigilant in monitoring such activities and, in appropriate cases, seeking pecuniary penalties often in excess of A\$1 million for breaches of these laws.

iii Unconscionable conduct

The Australian Consumer Law also prohibits unconscionable conduct.⁵⁶ The courts have been reluctant to restrict the definition of unconscionable conduct but seem to have settled that it entails conduct that involves:

- a* notions of serious misconduct or something that is clearly unfair or unreasonable where the alleged contravener shows no regard for conscience and has acted in a manner that is irreconcilable with what is right or reasonable;
- b* normally, some moral fault or moral responsibility;
- c* some deliberate (in the sense of intentional) act or at least a reckless act; and
- d* a high level of moral obloquy.⁵⁷

The potential consequences of a finding of unconscionable conduct are the same as those for a finding of misleading and deceptive conduct outlined above.

iv Agency distributor model

In theory, in a given case a franchisee could be subject to the laws of agency, whereby it is said that the franchisee is the agent of the franchisor.

54 Section 18 of the Australian Consumer Law.

55 Section 4 of the Australian Consumer Law.

56 Sections 20 to 22 of the Australian Consumer Law.

57 A useful summary is found in *Body Bronze International Pty Ltd & Ors v. Fehcorp Pty Ltd* [2011] VSCA 196 at paragraphs 86 to 94.

If a franchisee was considered to be an agent of the franchisor, the franchisor would be seen as the party contracting with the customer thereby allowing the customer to exercise contractual rights against the franchisor (for example, if goods are defective or not merchantable). It is also conceivable that the franchisor (as principal) might be liable for some debts incurred by the franchisee (as agent).

It is the prospect of these dire consequences that has resulted in nearly all franchise agreements used in Australia making provision that no agency relationship exists. Courts generally will uphold these provisions.

v Employment law

At federal and state level workplace relations laws exist that regulate the employment of staff by franchisors and franchisees throughout Australia. The Fair Work Act 2009 (Cth) contains a set of employment standards that apply to all workers in Australia.

Franchisees will not be treated as employees of the franchisor unless the relationship is, in reality, an employer–employee relationship but clothed with a sham description such as a franchise agreement or independent contractor arrangement.

vi Consumer protection

Although the Australian Consumer Law has some application to franchising, the traditional protections offered to consumers, such as laws relating to unfair contract terms,⁵⁸ are not available to franchisees, primarily because a franchise agreement is not considered to be a consumer contract.⁵⁹

The concept of ‘consumer’ underpins many of the provisions in the Australian Consumer Law. A person can only be considered to have acquired goods or services as a consumer if:

- a* the goods or services were not acquired for resupply or the purpose of transformation in the course of production or manufacture and;
- b* the amount paid for the goods or services does not exceed \$40,000; and
- c* the goods or services were of a kind ordinarily acquired for personal, domestic or household use or consumption.⁶⁰

Goods or services (including franchise rights) acquired under a franchise agreement will generally not meet these tests.

58 Part 2.3.

59 A consumer contract is defined in Section 23 as a contract for the supply of goods or services or the sale or grant of an interest in land to an individual whose acquisition is wholly or predominantly for personal, domestic or household use or consumption.

60 Section 3 of Competition and Consumer Act 2010 (Cth).

vii Competition law

Australian competition laws⁶¹ are extensive and complex. Penalties for breaches of the 'restrictive trade practices' provisions can result in fines of up to A\$10 million, or fines calculated at three times the benefit obtained by the infringer from its illegal activities.

The most common areas under the restrictive trade practices laws that affect franchising are:

- a* the prohibition of cartels and cartel provisions (i.e., contracts, arrangements or understandings between competitors that relate to price-fixing, restricting outputs in the production and supply chain, allocating customers, suppliers or territories or bid-rigging);
- b* the prohibition of third line forcing (i.e., where, for example, a franchisor compels a franchisee to purchase goods or services from a third-party supplier); and
- c* the prohibition of resale price maintenance (i.e., where, for example, a franchisor sells goods to a franchisee on the condition that the franchisee will not resell those goods below a certain price).

This list is by no means exhaustive and best-practice franchisors in Australia undertake extensive trade practices training and create and implement compliance programmes.

All of the above examples are capable of being effectively sanctioned by the competition regulator (the ACCC) through processes known as 'authorisations' and 'notifications'. A person seeking an authorisation or notification clearly needs to put forward a legitimate case as to why it should be allowed to engage in conduct that is otherwise illegal. At a minimum it must be shown that the proposed conduct creates a public benefit that outweighs the detriment associated with such uncompetitive conduct.

viii Restrictive covenants

Non-compete or restrictive covenants contained in a franchise agreement must be carefully drafted. If they are vague, they may not be enforced or, at the very least, be read down to the least restrictive interpretation.

If the non-compete or restrictive covenant goes beyond what is necessary to protect the legitimate business interests of the franchisor (as they were at the time the franchise agreement was executed), it will not be enforceable.

They may also be unenforceable by virtue of Clause 23 of the Code (which only applies to franchise agreements entered into or varied on or after 1 January 2015), which provides that a restraint of trade clause in a franchise agreement or some other associated document will have no effect after the franchise agreement expires if all of the following five circumstances exist:

- a* the franchisee has sought in writing to extend the franchise agreement on substantially the same terms as those contained in the franchisor's current franchise agreement and that apply to other franchisees or would apply to prospective franchisees;

61 The Competition and Consumer Act 2010 (Cth).

- b* the franchisee was not in breach of the franchise agreement or any related agreement;
- c* the franchisee has not infringed the intellectual property of, or a confidentiality agreement with, the franchisor during the term of the franchise agreement;
- d* the franchisor does not extend the franchise agreement; and
- e* either
 - the franchisee claimed compensation for goodwill because the agreement was not extended, but the compensation given was merely a nominal amount and did not provide genuine compensation for goodwill; or
 - the agreement did not allow the franchisee to claim compensation for goodwill in the event that it was not extended.

If a franchisee is in breach of a legitimate and enforceable non-compete or restrictive covenant and refuses to cease such conduct, a franchisor may apply to a court for an injunction restraining the franchisee from continuing with such conduct. An injunction can be obtained fairly quickly (at an interlocutory stage in the proceeding) if the court is satisfied there is a serious question to be tried, the balance of convenience favours the granting of the injunction (which often involves consideration of whether damages can provide an adequate alternative remedy) and the applicant (franchisor) undertakes to the court to compensate the franchisee for any loss it suffers if, at the final hearing, the court holds in favour of the franchisee.

ix Termination

Termination of a franchise agreement must be effected according to the franchise agreement, the Code or the common law.

A franchisor who has validly terminated a franchise agreement will be able to enforce provisions in the franchise agreement intended to survive termination, such as non-compete or restrictive covenants (provided they are not too wide – see above), confidentiality obligations, prohibitions on ongoing use of intellectual property, return of confidential information and manuals and de-branding obligations.

The ability of a franchisor to effectively take over the terminated franchisee's business will depend on a number of factors such as:

- a* whether the franchisor has rights to occupy leased premises to the exclusion of the franchisee;
- b* whether the franchisor has the right to use or to acquire the hard assets used by the franchisee in operating the business (well-drafted franchise agreements will contain these rights); and
- c* whether the franchisor has the resources to take over operation of the business.

x Anti-corruption and anti-terrorism regulation

The laws of Australian States and Territories outlaw what is commonly known as bribery.

The Criminal Code 1995 (Cth), while not applying to bribes in the private sector, creates offences relating to the bribery of local and foreign public officials. A company can be held criminally responsible for the actions of its employees, officers or agents acting within the actual or apparent scope of their employment or authority.

The Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (Cth) contains extensive provisions designed to combat money laundering and the financing of terrorism. This legislation imposes various obligations relating to customer identification, transaction monitoring and suspicious transaction reporting. The money laundering offences are quite wide and extend to receiving, possessing or disposing of money or property that is reasonably suspected of being the proceeds of crime.

xi Dispute resolution

Very few franchising disputes reach adjudication in Australian courts. In the 12 months to 30 September 2014, there were fewer than 10 reported cases following the trial of substantive issues.

The major reasons for this are:

- a alternative dispute resolution, such as mediation, is extensively used;
- b litigation is extremely expensive, slow and uncertain; and
- c it is very difficult to succeed on summary judgment applications.

Although franchise agreements must contain complaint handling provisions prescribed by the Code,⁶² the right of a party to commence legal proceedings is not affected by those provisions, unless the franchise agreement says so.⁶³

It is extremely rare for local franchising disputes to be referred to arbitration in Australia. It is extremely rare for local franchise agreements to provide for arbitration as a means of adjudicating disputes. Nearly all civil cases in Australia (and all franchising cases) are decided by a judge; juries are not permitted and, hence, the fear of the runaway jury does not exist.

Properly drafted exclusive forum provisions in franchise agreements entered into prior to 1 January 2015 will generally be upheld by Australian courts. It is wise to highlight in a disclosure document, or some other document provided to the franchisee before it signs the franchise agreement, the disadvantages the franchisee might face if it is required to litigate or arbitrate overseas.⁶⁴

In respect of franchise agreements entered into on or after 1 January 2015, the Code makes it unlawful to include a clause requiring a party to bring an action or proceeding or conduct mediation in relation to a dispute under the agreement in any state or territory of Australia or any other country other than the state or territory of Australia where the relevant franchised business is located.⁶⁵ Further, any clause in a franchise agreement entered into on or after 1 January 2015 to this effect will not be enforceable.⁶⁶

62 Franchising Code of Conduct, Clauses 34, 38 and 39.

63 Franchising Code of Conduct, Clause 37.

64 See *Timic v. Hammock* [2001] FCA 74 where the *Subway* forum provision was upheld primarily because of the clear warnings it gave the franchisee before entering into the franchise agreement.

65 Franchising Code of Conduct, Clause 21(2).

66 Franchising Code of Conduct, Clause 21(3).

The procedure for instigating mediation involves:

- a* a party serving on another party a notice of dispute;⁶⁷
- b* attempts then being made to try to resolve the dispute; and
- c* if the dispute is not resolved in 21 days either party may refer the dispute to mediation; this is done by notifying the Office of the Franchise Mediation Adviser, which will then liaise with the parties and appoint a mediator from its panel of mediators.

Once a mediator is appointed, a mediation agreement will need to be signed by all parties (including any non-parties who may attend mediation). This agreement will set the ground rules, which will include confirmation of the without-prejudice nature of the discussions, the critical confidentiality obligations and the mediator's fees and the sharing of fees.

The Code also imposes some rules. It requires:⁶⁸

- a* the parties to attend mediation and try to resolve the dispute;
- b* the person attending on behalf of a party having full authority to settle the dispute;
- c* the parties to make clear what they want to achieve from the mediation process; and
- d* the parties not to do things that might damage the reputation of the franchise system.

As stated above, in the absence of a provision in a franchise agreement to the contrary, a party may head straight down the litigation path. This is common if an urgent injunction is required, for example in circumstances where a terminated franchisee might be continuing to use the franchisor's intellectual property or breaching a valid non-compete provision. Usually, an interlocutory injunction will be sought, which is one that stays in place until the final hearing and determination of the proceeding and at this point, no costs orders are made in favour of a successful applicant – rather they are reserved for later determination.

Subject to this reservation, in most courts in Australia, costs follow the event (the loser is ordered to pay the winner's costs), with the quantum of costs being determined not by what the lawyer charged his client, but by reference to costing scales or concepts of reasonableness.

Enforcement of judgments and arbitral awards in Australia involve court processes, including asset seizure and sale, attachment of debts or earnings and insolvency proceedings.

As a signatory to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitration Awards (the New York Convention), a foreign award

67 Setting out the nature of the dispute, what outcome the complainant wants and what action the complainant thinks will settle the dispute.

68 See the Franchising Code of Conduct, Clause 29.

(not an award made in Australia in an international arbitration) may be enforced in the federal, state and territory courts⁶⁹ as if the award were a judgment or order of that court.⁷⁰

VII CURRENT DEVELOPMENTS

The Australian government is currently considering and is likely to enact laws extending unfair contract laws to business to business transactions.

The current law, which only applies to consumer transactions involving ‘standard form contracts’:

- a* deems unfair terms to be void;
- b* requires three tests to be satisfied to establish that a term is unfair:
 - it would cause a significant imbalance in the parties’ rights and obligations arising under the contract;
 - it is not reasonably necessary to protect the legitimate interests of the party who would be advantaged by the term; and
 - it would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on;
- c* presumes that a contract is a standard form contract unless the other person proves otherwise (a reverse onus); and
- d* provides that a court may take account of the following in determining whether a contract is a standard form contract:
 - whether one of the parties has all or most of the bargaining power relating to the transaction;
 - whether the contract was prepared by one party before any discussion relating to the transaction occurred between the parties;
 - whether another party was, in effect, required to either accept or reject the terms of the contract in the form they were presented;
 - whether another party was given an effective opportunity to negotiate the terms of the contract; and
 - whether the terms of the contract take into account the specific characteristics of another party or a particular transaction.

If the Australian government proceeds with this proposal, the real issue will be whether franchise agreements will be regarded as standard form contracts or, more importantly, whether a franchisor can establish they were not standard form contracts.

69 Under Section 8(2) and (3) of the International Arbitration Act 1974 (Cth).

70 See article by Justice Rares of the Federal Court of Australia at www.fedcourt.gov.au/publications/judges-speeches/justice-ares/Rares-J-20110914.rtf.

Appendix 1

ABOUT THE AUTHORS

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Philip Colman is a partner at MST Lawyers in Melbourne, Australia, a firm with one of Australia's most extensive and experienced franchising practices. MST Lawyers acts for a large number of successful Australian franchisors and master franchisees and has advised and acted for many inbound foreign franchisors. While currently heading his firm's litigation and dispute resolution practice, Mr Colman headed the franchising practice from 1996 to 2007. Mr Colman has practised substantially in franchising since 1985 and since 2007 his practice has focused on litigation and dispute resolution in the franchising sector. Mr Colman is a member of the Legal Committee of the Franchise Council of Australia and has on a number of occasions spoken at, and been on the organising committee for, legal symposia conducted by the Franchise Council of Australia. Mr Colman is also a member of the four-member Expert Legal Committee that assisted the Franchise Council of Australia with its submissions to the Australian government in respect of the Franchising Code of Conduct. Mr Colman was a panellist at the IFA-IBA Joint Conference in May 2013. Philip is the author of many papers and articles touching on franchising and has participated in writing the Australian chapter in other publications dealing with franchising throughout the world.

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