

Amendments to the Franchising Code of Conduct

August 2007

Franchise arrangements are strictly regulated in Australia under the Franchising Code of Conduct (Code). The Code, established under the *Trade Practices Act 1974* (Cth), is mandatory. It requires franchisors to follow strict rules and disclose specific information to franchisees/potential franchisees.

Regulations amending the Code were made on 9 August 2007. These regulations are a result of the Franchising Code Review Committee's report on the Review of the Disclosure Provisions of the Franchising Code of Conduct last year.

The regulations commence on 1 March 2008.

Overview of the amendments

The amendments can be divided into a number of broad categories as follows:

- a) Provision to franchisees of additional documents.
- b) Provision to franchisees of information, and timeframes for the provision of information.
- c) Application of the Code to franchisors.
- d) Foreign franchisors.
- e) Other amendments.

Provision of additional documents

The Code currently requires a franchisor to provide a disclosure document including a summary of the franchise agreement and any requirements for the franchisee to enter into other agreements.

The amendments now require:

- a) The **franchise agreement** (in the form intended to be signed) to be provided with the disclosure document.
- b) **Associated documents** (such as leases, hire-purchase agreements, guarantees and confidentiality agreements) to be provided at least 14 days before the franchise agreement is signed (or, if not available at that time, when available).
- c) A **copy of the Code** to be provided (there was previously an inconsistency in the Code leading to some doubt as to whether this was a requirement).

Provision of information

The Code currently requires franchisors to disclose whether they or an associate will receive a **rebate or other financial benefit**. The amendments now require that the names of persons from whom such rebates or other benefits are received must also be disclosed.

The Code currently requires financial information for a franchisor to be provided to franchisees. The amendments now provide that **financial information of a consolidated entity** to which a franchisor belongs must also be disclosed on request.

In relation to the **management and application of marketing and other co-operative funds**, franchisors can currently avoid providing financial information on such funds by seeking approval from 75% of their franchisees. The amendments now provide that such approval will last for three years (after which time it will need to be obtained again). Also franchisors will now be required to provide the financial statement and any auditors report (previously this was only on request).

The amendments require franchisors to disclose in the disclosure document the existence and content of an **order or undertaking under section 87B** of the *Trade Practices Act 1974* (TPA) (previously only the date of such an order was required to be disclosed). Section 87B gives the ACCC power to accept written undertakings by companies and these undertakings can subsequently be enforced by the Federal Court. Such undertakings are usually given when the ACCC is concerned that a company may contravene the TPA. Franchisors will now also be required to disclose the matter (where not in the disclosure document) within 14 days (rather than the previous 60) after the making of an order or the giving of an undertaking.

In relation to a **franchise history**, the amendments require:

- a) Franchisors to disclose not just the numbers but (subject to the ex-franchisee the subject of the disclosure requesting otherwise) also the names, locations and contact details of ex-franchisees whose franchises:
 - i. Were transferred.
 - ii. Ceased to operate.
 - iii. Were terminated by the franchisor or franchisee.
 - iv. Were not renewed on expiry.
 - v. Were bought back by the franchisor.
 - vi. Were terminated and the franchise business being acquired by the franchisor.

Franchisors will not be required to retain this information for more than three years or, as stated in the Explanatory Statement, update it.

- b) The **details and the history of the franchise site or territory** to be supplied *with* the disclosure document (presently the Code allows the details to be made available for inspection at a time and place mentioned in the disclosure document).

- c) Disclosure of **business experience** of each officer of the franchisor (presently the Code only requires such information for each director, secretary, 'executive officer' or partner of the franchisor who is likely to have management responsibilities). 'Officer' is defined by the *Corporations Act 2001* (Cth) which includes directors, secretaries and persons who make decisions affecting the business of the company.
- d) Disclosure by a **director of a franchisor** of proceedings, a judgment or an award relating to breach of a franchise agreement, the TPA, the *Corporations Act 2001*, unconscionable conduct, misconduct or dishonesty, and certain proceedings under employment legislation or by franchisees. Previously this information was limited to the franchisor.
- e) **Provision of information** on request in relation to specific matters such as the business experience of each director, secretary or partner, payments to agents or information relating to existing franchises. A franchisor was previously able to opt out of providing this information if it was 'reasonable to withhold' it.

The **timeframes within which information** must be provided have also changed, so that franchisors:

- a) Will now have an extra month (now four months):
 - i. After the end of each financial year within which to update their disclosure document.
 - ii. To prepare an annual statement for marketing or other co-operative funds, and an extra month (now four months) to have it audited.
- b) Will have to disclose materially relevant information within 14 days rather than the present 60 days.

Application of the Code

The Code currently provides that it does not apply to a franchise agreement where the franchisor is outside Australia and grants only one franchise or master franchise for operation in Australia. This exception will be removed. All other exceptions remain.

Foreign franchisors

There are amendments allowing foreign franchisors to use auditors in and accounting standards of their own jurisdiction for their foreign operations. Previously, franchisors were required to comply with Australian standards and audit requirements.

Other amendments

Other important amendments include:

- a) The current prohibition on franchisors **preventing franchisees associating** with each other being extended to include prospective franchisees.
- b) The introduction of a **prohibition on the use of waivers** of written representations in franchise agreements and other documents.

There were also a number of **clarificatory amendments**, as follows:

- a) The recurring and isolated payments payable by a franchisee to an associate of the franchisor and disclosed by the franchisor will include real property related payments.
- b) The requirement that a current disclosure document is required where a franchisor plans to 'extend a franchise agreement' will be clarified by stating that 'extend' relates to both 'term' and 'scope'.
- c) Whether a short form or long form disclosure document is required will be clarified. Currently, this depends on the expected annual turnover of the franchised business. It is now clear from the amendments that a short form disclosure document can be used when the expected annual turnover of the franchised business **over the term of the franchise business** is less than \$50,000.
- d) It will be clear that prospective franchisees who terminate within the 'cooling off' period may do so without cost if this is done within seven days after signing the agreement (subject to reasonable expenses or their method of calculation being set out in the franchise agreement).

The amendments to the Code are far reaching and are largely intended to promote greater transparency between the franchisor on the one hand, and potential franchisees and existing franchisees on the other. They remove much of the discretion afforded to franchisors to provide certain information and clear up a number of the discrepancies in the Code.

Franchisors should ensure that their:

- a) disclosure document; and
- b) business practices,

comply with the amendments prior to their commencement early next year.

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