FRANCHISING IN CANADA:
A Guide for Franchisors

Davis LLP, Canadian Lawyers
Franchise & Distribution Group

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INTRODUCTION

This paper is general in nature. It provides a broad overview of legal considerations relating to Canadian franchising and the expansion of franchise systems within or into Canada as of May, 2013.

No part of this paper is to be taken as legal advice by Davis LLP. Legal advice will only be given by Davis LLP once a client has signed a retainer letter with our firm.

I. ACKNOWLEDGEMENTS

This paper has been written by 13 different lawyers of the Canadian national law firm of Davis LLP. Their names are shown in the Table of Contents, as are the topics on which each of them has written. Part VII contains their professional biographies.

As editor, I wish to thank each and every contributor for giving their time to ensure the successful publication of the second edition of this paper. Each contributor has significant expertise in the topic(s) on which he/she has written. Special thanks are due to Sandra Appel, who kindly acted as assistant editor of this paper.

II. CANADA - POLITICALLY, DEMOGRAPHICALLY AND LEGALLY

Canada is a confederation made up of 10 provinces, and 3 territories. While each province and territory has its own government, Canada is governed primarily by a federal parliament located in Canada’s capital city, Ottawa.

Canada's Constitution divides powers between the federal government and the provincial/territorial governments. The Constitution gives provincial and territorial governments powers to legislate regarding property, civil rights and other matters of a local or private nature, while the federal government has powers over defence, criminal law, currency, banking, most forms of intellectual property, competition law and any other matters over which the provincial governments are not given primary jurisdiction.

The Constitution appears to give the federal government the right to regulate franchising on a national level, however it has not yet attempted to do so. Accordingly, Canada has no equivalent to the American FTC Rule. Nonetheless, there are many federal statutes in Canada which have an important impact on franchising. They are discussed in Part III of this paper.

As well, there are various provincial laws throughout Canada which have an impact on franchising, including laws governing franchise regulation, trade practices, consumer protection and taxation.

Canada has 34 million residents, 80% of whom live in urban areas. The majority live near the US border. The 4 most populous cities are, in order, Toronto, Montreal, Vancouver and Calgary. Canada has 2 official languages, English and French, with French speakers concentrated in the province of Québec. Canada, the US and Mexico are members of the North American Free Trade Agreement (“NAFTA”). Eighty (80%) per cent of Canada’s exports are made to the US, while 55% of its imports come from the US. Canada ranks 17th out of 185 countries in the World Bank’s “Ease of Doing Business Ranking”.

The business of franchising is alive and well in Canada. About 45% of all retail businesses are franchised and many major franchisors have established a strong presence nation-wide. The franchisors are both domestic
and foreign, with foreign-based franchise systems enjoying major popularity. Over 50% of existing franchised units are American-based.

The vast majority of franchising activity takes place in Canada’s four most populous provinces - Ontario, Québec, British Columbia and Alberta. Two of these provinces (Alberta and Ontario) have franchise legislation. As will be discussed later, franchise legislation has recently been proposed in British Columbia, although no draft legislation has been prepared yet. Smaller provinces with franchise legislation are Manitoba, New Brunswick and Prince Edward Island.

Unlike the other 9 provinces, Québec has a Civil Code of Quebec (the “Code”) (see Part IV. G on page 18). Although the Code is not specifically directed to franchising, it does have a real impact on franchisors. It is noteworthy that the majority of Québec residents are French-speaking and that Québec has enacted laws aimed at protecting French language and culture.

Relevant legislation in Alberta, Ontario and Québec is discussed in Part IV.

III. CANADIAN FEDERAL LAWS

Many federal laws apply to franchising. Some of the most important relate to:

A. Trade-marks and Domain Names (David Spratley, Vancouver)

Canada has a federal trade-mark system only under a statute called the Trade-marks Act.

A trade-mark (or “Mark”) forms the core of the goodwill of a franchise system. It is therefore important to ensure that each trade-mark of a foreign-based franchise system is properly registered for use in Canada.

A foreign trade-mark registration is not effective in Canada, although the Canadian law of “passing off” does provide limited protection for foreign trade-marks that have already acquired a reputation in Canada.

Nevertheless, enforcing trade-marks that are not registered in Canada can be both uncertain and expensive. Accordingly, it is highly desirable to register trade-marks in Canada before doing business here.

Registration in the Canadian Intellectual Property Office (“CIPO”) protects a trade-mark all across Canada, even in areas where the Mark is not being used. An unregistered Mark, on the other hand, is only enforceable in the area where it has acquired a reputation based on use. Canadian provinces and territories have no jurisdiction to grant trade-mark registration; all registrations are granted by CIPO pursuant to the federal Trade-marks Act. The provinces and territories do have procedures for giving public notice of business names, however such notices do not confer any meaningful proprietary rights.

1. Registration

It is highly advisable to start the Canadian registration process before a trade-mark is used in Canada.

The first step is to conduct a registrability search with CIPO to determine whether the trade-mark may be available. The search should include all words and designs (logos) that may be used to distinguish the franchisor’s goods and services.

The next step is to file an application to register the trade-mark even if it has not yet been used in Canada. Applications may be made on an “intent to use” basis; actual registration will not be given until the Mark is in use and the applicant files a Declaration of Use with CIPO. Since final registration is usually delayed for 18 months or more, the applicant has a lengthy intervening period to start use in Canada. It is sometimes possible to secure Canadian registration based on use and registration in a foreign country (although such registrations are vulnerable if the Mark is not actually used in Canada).
The scope of the trade-mark application is an important consideration. In Canada, applications must describe the goods and services that are (or will be) sold under the proposed trade-mark. In many countries, goods and services are classified into one of several international classes, and the amount of the applicable filing fee depends on the number of classes claimed in the trade-mark application. Accordingly, foreign applicants often narrow the scope of their trade-mark applications in their home countries in order to keep costs down. However, Canada does not use the international classification system and therefore Canadian applications may claim any number of goods and services in any number of international classes for a single, inexpensive filing fee. Accordingly, foreign franchisors should consider whether their international applications adequately cover all of the goods and services that may be sold under their trade-marks in Canada. A Canadian trade-mark lawyer can help broaden the application to make it as comprehensive as possible, with little additional cost.

The cost of a typical uncontested trade-mark registration in Canada is currently around CDN$2,500 including all government fees. The cost would increase if CIPO or a third-party objected to registration of the proposed Mark. Registration of an uncontested Mark currently takes up to 18 months.

2. Licensing

The Trade-marks Act imposes strict rules on commercial use of registered trade-marks. Anyone who uses a Canadian trade-mark, other than its owner, must be formally licensed to do so. Improper or undocumented licensing may render a trade-mark unregistrable or, if already registered, unenforceable. This applies even within corporate families, and therefore use by related entities without a written licence may jeopardize the Mark.

By the Trade-marks Act, the licensor must have direct or indirect control over the character and quality of the goods and services offered by its licensee under its registered trade-mark. The licensor must exercise this control on an ongoing basis to protect its registration. In Canadian franchising, the franchisor (or its affiliate) is the licensor and the franchise agreement contains the terms of licensing of the Mark(s).

3. Canadian Domain Names

Domain names are often important to the success of a franchise. Ideally, the franchisor will have already registered all of its trade-marks and business names as “.com” domain names. As added protection, many franchisors may also have registered several variations, mis-spellings and abbreviations.

In Canada, it is advisable to register domain names in the “.ca” domain for trade-marks, business names and variations thereof. The “.ca” domain is attractive to Canadian consumers who anticipate that products and services on websites in the “.ca” domain are normally advertised in Canadian dollars and are usually available for purchase in Canada.

There is no limit to the number of “.ca” domain names that may be registered, however, a franchisor cannot register a “.ca” domain name unless it is a Canadian entity or has a valid Canadian trade-mark registration for the proposed domain name. Many foreign franchisors deal with this restriction by registering Canadian domain names through a new Canadian subsidiary; this is permissible so long as the subsidiary is first formally licensed to register and use the franchisor’s domain names on the Internet.

The cost to register a “.ca” domain name is nominal and registration may be obtained quickly.

B. Copyrights (David Spratley, Vancouver)

In Canada, copyright protection automatically applies to every original literary, dramatic, musical and artistic work as soon as soon as it is created by a Canadian citizen, or a resident of another country that is a member of the Berne Convention, the Universal Copyright Convention or the World Trade Organization.

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Copyright protection includes the sole right to reproduce, perform, publish and translate the work or a substantial portion of it.

Under the federal Copyright Act, it is possible to register copyright in Canada, although it is usually not necessary to do so since copyright arises automatically by operation of law when a work is created. However, registration does have some benefits. For example, if a franchisor registers a copyright, Canadian law presumes that copyright does exist in the work and that the franchisor owns the copyright. This could save the franchisor significant expense if it needed to sue someone for copyright infringement. Registration of copyright also makes it easier for the franchisor to obtain certain remedies in Court, including damages. Often, copyright registration is not applied for until a related lawsuit has been commenced.

Most franchisors have many works that could benefit from copyright registration. The most important of these are often logos and jingles. Registering the copyright in logos and jingles, in addition to registering them as trade-marks, provides extra protection at a minimal cost.

Copyright registration normally takes 2 to 4 months, and the Canadian government fees are nominal.

A problem that arises in connection with copyright is the failure to obtain ownership of a copyright in a work created under contract by a third party (for example, by a graphic designer). Ownership of Canadian copyright must be obtained according to Canadian rules governing vesting and transfer. Most works created by an employee in the course of performing his/her duties automatically belong to the employer, by operation of law. However, if the work is created by an independent contractor and there is no agreement addressing ownership, the contractor will own the copyright subject to an implied license (only) in favour of the franchisor (or other party) who retained the contractor.

Before a work is authored by a third party contractor, therefore, it is advisable to require the contractor to sign a contract providing that ownership will belong to the franchisor and that the contractor will sign all documents and take all other steps required to vest ownership in the franchisor. Under Canadian law, that promise only establishes an obligation to transfer. In and of itself, such a promise does not convey full legal title to a Canadian copyright that comes into being after the promise was given. To perfect full legal title, the contractor must sign an “assignment” after the work has come into being. Therefore, a two-step process is required (contract for the requested work and assignment of the created work) where a work is created by an independent contractor.

Canadian copyright law also confers separate special rights on authors called “moral rights” that are distinct from copyright. The primary moral rights of authors are “paternity” (the right to have one's name associated with a work) and “integrity” (the right to prevent one’s work from being modified, distorted or associated with a product, business or cause in the absence of permission). Moral rights may be waived in writing by a third party creator of a work.

C. Patents (David Spratley, Vancouver)

A Canadian patent confers on the patent holder (“patentee”) the exclusive right to make, use or sell an “invention” within Canada. A foreign patent has no force or effect within Canada, just as a Canadian patent is not effective outside of Canada. A patentee’s rights arise only by a federal statute called the Patent Act and so “common law” patent law rights do not exist. The CIPO administers patents in addition to trade-marks. Whether the requirements for patentability are satisfied may raise complex legal issues requiring qualified professional advice. Minor differences in terminology and content may have significant effects on the scope, validity and value of any patent to be issued. Those who are not resident in Canada or who do not carry on business in Canada may apply for a patent, however they must appoint a resident patent agent to act on their behalf.

Canada is a “first to file” patent jurisdiction. Subject to allowable priority rights, a patent is issued to the first person(s) to file a patent application claiming the invention. However, only the true inventor or a party deriving rights from the true inventor is entitled to apply for a patent. To be patentable, an invention must,
among other things, be new, non-obvious, and have utility. It must relate to a new and useful art, process, machine, manufacture or composition of matter, or any new and useful improvement in any of the foregoing. If an application describes more than one general inventive concept, then CIPO will require that the applicant’s claims be limited to only one of these, although a divisional application(s) may then be filed to pursue protection for the other concept(s).

The scope of exclusivity conferred by a Canadian patent is determined by the claims made in the patent application. The language of the claim is construed purposively, in light of the disclosure made. Canadian jurisprudence recognizes a “doctrine of equivalence” which may sometimes be applied to extend the scope of the patent beyond the literal wording of the claims made.

Canada follows a qualified absolute novelty rule. Once an invention has been made available to the public anywhere in the world, then unless that disclosure arose with the inventor, it is too late to pursue a Canadian patent. If, however, the invention was first made available to the public by the inventor, then a Canadian patent may still be legitimately sought if an application is filed within one year of the date of first disclosure to the public. Canada is a member of the Patent Cooperation Treaty and the Paris Convention. As a result, a Canadian patent application may claim priority from the date of the first application filed in any other Paris Convention country if the Canadian application is filed within one year of the first filing. On payment of late fees, an international (PCT) patent application may enter the Canadian national phase up to 42 months from the first priority date.

Eighteen months after the filing date, a Canadian patent application is laid open to the public and may be publicly accessed on the website of CIPO. However, the exclusive right to practice the invention does not arise or become enforceable until the patent is granted. Once filed, a Canadian patent application will not proceed further until examination is requested. This must be done within 5 years of filing and the examination process commonly takes 3 to 4 years once the request for examination has been made. The term of a new Canadian patent is 20 years from the filing date. In order to keep a patent alive throughout the 20 years, a maintenance fee must be paid annually starting with the second anniversary of the filing date. Once a patent expires, its content enters the public domain and no renewal is available. Once a patent is registered, the owner may be able to obtain remedies for infringing activities that occurred in the period between the application being laid open to the public and final registration. Once a patent is registered, the owner has the exclusive right in Canada to make, use or sell the invention disclosed in the patent.

D. Competition (Antitrust) (Bill Hearn, Toronto)

The Act contains both criminal and civil provisions prohibiting various types of anti-competitive conduct. It also establishes a pre-merger notification and merger review regime.

Criminal Offences

The main criminal offences that may be pertinent to franchises are: (a) conspiracies among competitors relating to price fixing, market allocation, or fixing production or supply of a product; (b) bid-rigging; (c) intentional and serious deceptive advertising; (d) deceptive telemarketing; (e) deceptive notice of winning a prize; (f) double ticketing; and (g) pyramid selling. These criminal offences are punishable by hefty fines, lengthy jail terms, or both - e.g., in the case of a conviction for conspiracy, a fine up to $25 million, imprisonment of the individuals involved for a term up to 14 years, or both. In addition, third parties (such as consumers and suppliers) harmed by such criminal anti-competitive conduct have a private right of action to sue the perpetrators for damages.

Civil Matters

The main reviewable matters pertinent to franchises include the following deceptive marketing practices: (a) misrepresentations to the public - e.g., about the price, performance, efficacy, length of life, etc. of a product or service; (b) ‘bait and switch’ selling; (c) sale above advertised price; and (d) promotional contests. The
civil sanctions for these reviewable matters are not to be scoffed at and include significant administrative monetary penalties ("AMPs") - i.e., up to $10 million for first time corporate offenders (up to $15 million for each subsequent violation) and full customer restitution.

The main restrictive trade practices reviewable by the governing Competition Tribunal ("Tribunal") which may be pertinent to some franchises include: (a) refusal to deal; (b) resale price maintenance ("RPM"); (c) exclusive dealing, tied selling and market restriction; (d) abuse of dominant position; and (e) agreements between competitors that substantially lessen or prevent competition. The civil sanction for such restrictive trade practices is limited to a remedial cease-and-desist order (including costs) by the Tribunal. However, when an abuse of dominant position is proven, the Tribunal may also impose substantial AMPs - i.e., up to $10 million for a first time corporate offender and up to $15 million for each subsequent violation. The Tribunal cannot order fines or imprisonment. Moreover, with respect to such civil matters, private enforcement and damages awards are not possible.

Resale Price Maintenance

RPM is one area of compliance that often arises in a franchise setting and for which, due to recent amendments to the Act, Canada’s competition laws are less restrictive than their antitrust counterparts in the United States (especially the various RPM laws at the U.S. state level).

In 2009, the Act was amended to replace a broad criminal offence (i.e., there was no need to show an anti-competitive effect) punishable by unlimited fines per se and up to 5 years imprisonment with a civil regime that permitted RPM except where it has an adverse effect on competition with contraventions addressed only through remedial cease-and-desist orders. The amendment effectively allows franchisors to set resale prices in Canada unless and until prohibited by an order of the Tribunal.

Exclusive Dealing, Tied Selling and Market Restriction

Exclusive dealing, tied selling and market restriction are also common in franchises. The Tribunal may make an order prohibiting the franchisor from engaging in these practices only if the Tribunal finds that all of the following conditions have been met:

1. the practices have been engaged in by a major supplier or have been widespread in a market;
2. the practices have impeded entry into or expansion of a firm, product or sale or have had another exclusionary effect; and
3. the practices have resulted, or are likely to result, in a substantial lessening of competition in the relevant market.

The Act also creates exemptions from the exclusive dealing and tied selling restrictions, some of which are relevant to franchises. In particular, the Tribunal may not make an order prohibiting (i) exclusive dealing, if the practice is engaged in only for a reasonable period of time to facilitate entry into a market or (ii) tied selling, if the practice is engaged in on a reasonable basis, having regard to the technological relationship between or among the products to which it applies. The Tribunal is also unable to make an order prohibiting either exclusive dealing or tied selling in circumstances where one party (a franchisor) grants to the other party (its franchisee) the right to use a trade-mark or trade-name to identify the business of the grantee (the franchisee), if the business is related to the sale or distribution, pursuant to a marketing plan or system prescribed substantially by the grantor (the franchisor) of a multiplicity of products obtained from competing sources of supply and a multiplicity of suppliers, and no one product dominates the business.

Mergers

In the case of a merger, if the parties and the transaction are both sufficiently large, the Act requires the parties to give the Commissioner of Competition (the "Commissioner") advance notice about the proposed transaction. Subject to limited exemptions, the parties must provide a pre-merger notification to the
Commissioner of a proposed transaction involving the acquisition of assets or voting shares of an operating business in Canada where both of the following tests are met:

(a) size of parties test: the parties to the transaction, together with their worldwide affiliates, have altogether either assets in Canada or annual gross revenues from sales in, from or into Canada, of C$400 million or more; and

(b) size of deal test: the target operating business has either assets in Canada or annual gross revenues from sales in or from Canada, of C$80 million or more.

In the case of the acquisition of shares, there is a further question about the level of share interest acquired. The acquiror, together with its affiliates, as a result of the proposed transaction must acquire greater than a 20% voting interest in a publicly-traded company or greater than a 35% voting interest in a private company (or if the 20% or 35% threshold, as the case may be, is already exceeded, greater than a 50% voting interest in the target company).

A notifiable pending transaction may not be closed until the expiry of a prescribed waiting period. This allows the Competition Bureau time to assess whether the transaction raises any anti-competitive issues. Most franchise transactions fall below the thresholds and therefore are not subject to regulatory approval.

E. Income Tax (Adrienne Woodyard, Toronto)

The Income Tax Act of Canada deals with tax payable to the federal government based on income derived from business, property, or an office or employment in Canada. Each provincial government also levies tax on such income that is attributable to the province (for the purposes of this discussion, “Canadian Income Tax” refers to combined federal and provincial income tax).

Franchisors which are not resident in Canada are liable for Canadian Income Tax on income earned from carrying on business in Canada and from dispositions of taxable Canadian property (generally real estate or immovable property situated in Canada, inventory of a business carried on in Canada and shares of unlisted Canadian corporations). However, the domestic rule is superseded by most of Canada’s bilateral tax treaties which provide that the business income of a non-resident may only be taxable in Canada to the extent that the non-resident carries on the business through a “permanent establishment” (“PE”) in Canada and the income is attributable to such PE. A foreign franchisor will have a PE in Canada if it has a branch, office or other fixed place of business in Canada (whether owned or rented), or it habitually enters into contracts in Canada either directly or through a dependent agent who has the authority to bind the franchisor. Under most of Canada’s bilateral tax treaties, a foreign franchisor will not have a PE in Canada solely because the franchisor stores or displays goods in Canada or owns shares of a Canadian subsidiary.

Every foreign franchisor is subject to a general non-resident withholding tax of 25% on the gross amount of all payments made to it by a Canadian resident on account of rent, interest, royalties and dividends, regardless of the existence or non-existence of a Canadian PE. However, the rate of withholding tax is often reduced by Canada's bilateral tax treaties. For example, pursuant to the Canada-U.S. Tax Convention, the withholding rate is 10% on franchise royalties (although some types of payments are exempt) and 5% on dividends (where the recipient is a corporation that owns 10% or more of the payor corporation; otherwise the dividend withholding rate is 15%). Interest payments are generally exempt from withholding tax under the Canada-U.S. Tax Convention. A foreign franchisor may seek a refund of the tax withheld by filing a tax return in Canada for the taxation year in which the withholding was done.

For taxation purposes, royalties are essentially payments for the use of or for the right to use in Canada any property, patent, trade-mark, design, model, plan, secret formula or process, or the right to use processes. Royalties also include payments for information concerning industrial or commercial experience, where the consideration payable for that information is dependent, in whole or in part, on (a) the use to be made of, or the benefit derived from, that information; (b) production/sales of goods or services; or (c) profits.

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In practice, the Canadian income tax rules mean that a foreign franchisor that has no PE in Canada will generally not be subject to Canadian Income Tax on payments made to it by a Canadian franchisee for services rendered by the franchisor outside of Canada, for products sold by the franchisor to the franchisee or for services which are not rendered by the franchisor in Canada. However, sales to a Canadian resident franchisee will generally trigger the obligation to file a Canadian income tax return, even if no Canadian tax is actually payable. In addition, a foreign franchisor will be subject to Canadian withholding tax on payments from Canadian franchisees for the use of know-how and trade-marks. Accordingly, a foreign franchisor may wish to structure its franchise agreements to separate payments which are on account of royalties from payments which relate to services which are not subject to Canadian withholding tax.

The Income Tax Act also contains a regime of transfer pricing rules which may be applicable to dealings between a foreign franchisor and a Canadian party which do not deal with each other at arm’s length (e.g., parent and subsidiary).

The Canadian government also imposes a tax of 5% on goods and services (“GST”) that are acquired in Canada. In provinces that have harmonized (combined) their provincial retail sales taxes with the GST (Ontario, New Brunswick, Newfoundland, Nova Scotia and Prince Edward Island) the tax is known as the “harmonized sales tax,” or “HST,” and ranges from to 13% to 15%. The question whether the supply of franchise rights by a non-resident franchisor will be subject to GST/HST depends on whether the franchisor is a GST/HST registrant and whether the supply was made in the course of business carried on by the franchisor in Canada. The supply of franchise rights by a non-resident franchisor who is not registered for GST/HST and does not carry on business in Canada will generally be exempt from GST/HST.

A non-resident franchisor which is not carrying on business in Canada may still consider registering voluntarily for GST/HST, because this will enable the franchisor to claim a full refund of GST/HST which it pays to third parties in the course of carrying on its business; this would include GST/HST paid for business travel expenses incurred in Canada, such as hotels and airline tickets. However, non-registrant GST/HST registrants must weigh this advantage against the costs of preparing and filing regular GST/HST returns. In addition, the Canadian government may require a non-resident GST/HST registrant to post security equal to one-half of its estimated GST/HST remittances for the preceding year.

F. Privacy (Tamara Hunter, Vancouver)

Privacy is becoming an increasingly important issue in Canada. In 2004, our federal government’s private-sector privacy legislation called “Personal Information Protection and Electronic Documents Act” (or “PIPEDA”) came into effect. PIPEDA protects all “personal information” about individuals (not corporations or partnerships) collected by companies and other organizations during the course of “commercial activities”.

“Personal information” is very broadly defined to include information regarding race, age, marital status, religion, employment history, address, telephone number, biology and personal opinions. Franchisors which collect personal information during the course of franchising activities must comply with the following requirements of PIPEDA (or other substantially similar provincial privacy legislation, where applicable):

1. the franchisor must designate an individual as its privacy officer; that individual will then be accountable for the franchisor’s compliance with PIPEDA;
2. the franchisor must explain why personal information is being collected from any person. The franchisor must also obtain the person’s consent before collecting, using or disclosing the information unless the applicable legislation authorizes collection, use or disclosure without consent;
3. the franchisor must also have a written privacy policy dealing with its management of personal information. The policy must be made available to individuals upon request. (Often, franchisors publish such policies on their websites); and
4. PIPEDA imposes other rules regarding the ways in which information may be collected, how the information must be protected, and how the information may be accessed or corrected.

British Columbia, Alberta and Québec each have their own privacy legislation which is substantially similar to the federal PIPEDA. The federal legislation applies in the other provinces and territories and to inter-provincial activities.

Franchisors involved in a health-related business should also be aware of health information protection legislation, such as the Alberta Health Information Act and the Ontario Personal Health Information Protection Act.

G. “Anti-Spam” Legislation (Tamara Hunter, Vancouver)

Federal Bill 28, commonly referred to as “Canada’s Anti-Spam Law” or (“CASL”) received Royal Assent on December 15, 2010 although it has not yet been completely proclaimed into force. It is expected to become law in late 2013 or 2014. CASL calls for a three-year transition period once it is proclaimed in force.

As drafted, the CASL is among the strictest of the world’s anti-spam laws. The legislation would impose significant restrictions on the use of electronic messages to carry out commercial activities, with the express goal of creating a more secure online environment. In light of concerns raised by various business groups who opposed the broad scope of the legislation in submissions filed with Industry Canada and the Canadian Radio-Television Commission (“CRTC”), revised draft regulations have been issued for comment.

Scope

The CASL will apply to entities that send commercial electronic messages (“CEMs”), such as emails, short message service (“SMS”) or instant message (e.g. Skype, Gmail chat) to “communicate, market or solicit services and products” to Canadians. This is a USA Law. The central factor in considering whether the CASL will apply is whether a transaction, act or conduct is commercial in nature, regardless of whether an expectation of profit exists. The broad scope of a CEM as defined may be modified as a result of lobbying efforts.

The CASL generally applies to CEMs that are sent from, or received by a computer in Canada. Businesses are permitted to send CEMs to recipients who have provided their implied or expressed prior consent.

Enforcement

Enforcement of the CASL will be handled by these regulators: the CRTC, the Competition Bureau and the Office of the Privacy Commissioner of Canada. These enforcing bodies will have authority to impose a wide variety of sanctions on individuals and businesses that contravene the CASL. Once it is found that someone has contravened the legislation, a number of immediate steps may be taken to bring them into compliance. If the contravener does not rectify the violation, the CASL authorizes the enforcing bodies to issue some of the most severe fines of any anti-spam legislation in the world through the Administrative Monetary Penalty System (“AMPS”). Individuals may be fined up to $1,000,000 per violation and corporations may be fined up to $10,000,000 per violation. The fines may be imposed daily for up to 10 days if the violation continues to occur. It should be noted, however, that the CRTC has recently stated that AMP penalties will only apply as a last resort.

The CASL also creates a private right of action that permits an individual to take civil action against anyone who violates the legislation.

H. Packaging and Labelling (Bill Hearn, Toronto)

There are various federal packaging and labelling laws which apply to the sale of products in Canada. For example, the Consumer Packaging and Labelling Act requires that pre-packaged consumer products bear labels which are accurate and meaningful, to help consumers make informed purchasing decisions. Accordingly, “false and misleading” representations are prohibited under section 7 of the Act. Where an
Industry Canada inspector believes on reasonable grounds that a provision of the Act or its regulations has been contravened, the inspector may seize and detain any product related to the contravention.

The Textile Labelling Act has similar requirements, however, it also provides specifications for mandatory label information such as the generic name of each fibre present, the manufacturer’s full name and an identification number.

The Precious Metals Marking Act has similar requirements; it provides for the uniform marking of articles made with gold, silver, platinum or palladium. In addition, it requires dealers who choose to mark their articles with representations related to the previous metal quality, to do so in the manner prescribed by the Act and its Regulations.

Other regulations apply to environmental products and products containing feathers or down. Except for certain “local or specialty products”, all labels must be in both of Canada’s official languages (English and French) and weights and measures must be expressed in metric units.

Special rules also apply to federal approval, marketing, content and sale of food, drugs and medical devices.

I. (Federal) Immigration Visas for Americans (Brian Tsuji, Vancouver)

In general, Americans are visa exempt. This means they can visit Canada without formally applying for a permit or visa. When entering Canada, an American would simply go to a port of entry at a land border crossing or the port of entry at an airport to obtain an entry date stamp in his/her passport. Unless any other notations are made in the passport by the entry stamp, there is an implied visitor permit for 6 months. This assumes the person is not coming to Canada to engage in activities that are considered “work”. This type of implied visitor permit usually applies if an American is entering Canada to do such activities as sightseeing, shopping or tourism.

“Work” is any activity that if done by a Canadian would result in the Canadian being paid. Even if the American is “volunteering”, this may be considered work if a Canadian would be paid for performing the same activity.

The “Business Visitor” category will be useful for an American who is entering Canada to perform activities that are more business-like than tourism, although not so business-like that an actual “Work Permit” would be required. Some examples of business activities that would be eligible for a Business Visitor permit are: business research for a Canadian location; meeting with staff from the same organization; providing information on direction and results that are expected; meeting with potential investors; meeting with potential purchasers of services or systems; and providing after sales service advice to purchasers of services. Some of the other key requirements for a Business Visitor permit are that the American be paid by an entity outside of Canada during the visit to Canada, and that a Business Visitor may not negotiate and close deals and receive money for services provided or products sold during the visit to Canada. It is also helpful if the visits to Canada are for periods of time that are shorter (2 to 3 days) and the frequency of the trips is fewer (once or twice a month). However it is possible to obtain a Business Visitor permit for up to 6 months and then apply to renew the permit.

A “Work Permit” is required if the American is doing an activity which would be deemed to be work. For example if the American enters Canada to establish a new enterprise, signs leases, hires staff, signs supplier contracts, signs contracts to sell services or products and is to be paid while in Canada, all of these would be considered work in Canada. Also, if the American is being paid by the enterprise in Canada this also would indicate the activities in Canada to be working in Canada.

There are several methods for an American to obtain a work permit:

Under the NAFTA there is an Intra-Company Transferee work permit category. NAFTA applies to citizens of the US, Canada and Mexico and allows an employee from a US company to transfer to a related company in Canada and obtain a Work Permit. A “related company” would be a company that has common shareholders.
such as an American parent and Canadian subsidiary or two subsidiaries of the same American parent company. The American employee to be eligible needs to have worked for a minimum of 1 year in the past 3 years for a related company in a position that is either a senior manager position or a specialized knowledge and experience position. A senior manager position requires the person to have managed staff or a function in the company. Specialized knowledge and experience could involve the employee having worked with the US entity using its specialized systems and techniques. This work permit can be applied for at the land or airport port of entry. The processing time is approximately 30-60 minutes.

Under NAFTA there is also a work permit category for “professionals”. NAFTA lists a number of professions which are eligible. Some categories which may be useful include accountant, computer systems analyst, economist, engineer, hotel manager, lawyer, management consultant, dietitian, nutritionist, pharmacist, scientist, and teacher. This work permit can be applied for at the land or airport port of entry. The processing time is approximately 30-60 minutes.

Under NAFTA, there is also a Treaty Trader category. If the applicant will make a significant investment in Canada, a work permit will be issued to him or her.

Under The General Agreement on Trade in Services (“GATS”) there is also an Intra-Company Transferee work permit category. GATS applies to more countries than NAFTA.

There is also a general intra-company transferee category available under the Immigration and Refugee Protection Act (Canada) for all nationalities having the same eligibility requirements as those holding the NAFTA Intra-Company Transferee work permit requirements.

There are some other routes that may be taken to obtain a business visa, such as a labour market opinion that no Canadian has the necessary qualifications for a specific job.

In conclusion, there are a number of different Canadian immigration options that can be used by an American employee to enter Canada and legally conduct the business activities that are necessary. It is very important the appropriate category be selected, that thorough documentation be prepared and that the American employee be properly prepared for an interview with the Canadian immigration officer at the port of entry or Canadian Consulate or Embassy in the USA. If it is possible to use an exemption that allows the American employee to enter Canada and conduct the required activities without having to obtain a work permit or having to advertise a position to obtain a work permit, this is strongly preferred.

IV. PROVINCIAL LAWS

The laws of Canadian provinces with franchise legislation are very important. At present, 5 of the provinces (Ontario, Alberta, Manitoba, New Brunswick and PEI) have franchise legislation. As well, a 6th province, British Columbia, has expressed an intention to draft franchise legislation. Currently, the remaining 4 provinces neither have franchise-specific legislation nor do they have other legislation which is relevant to franchising.

A. ALBERTA (Dana Schindelka, Calgary)

The Alberta Franchises Act (the “Alberta Act”) applies to the sale of any franchise that will be operated in Alberta, however only if the franchisee is an Alberta resident or has a PE in Alberta. The Alberta Act governs all franchise-related agreements and imposes a duty of “fair dealing” on both franchisor and franchisee with respect to their ongoing business relationship in Alberta.

The Alberta Act does not require registration of a franchisor or regulatory approval of its franchise disclosure document (“FDD”), although these were requirements before amendments were made in 1995.

Under the Alberta Act, franchisors are required to give prospective franchisees a FDD at least 14 days before any payment is made or any agreement is signed relating to the franchise, whichever is earlier. The FDD must
contain all material facts about the franchise, including (although not limited to) those facts required by regulation. Some facts to be disclosed are the business form of the franchisor, its financial statements, the initial franchise fee and other amounts charged by it and the form of franchise agreement (“FA”) and related documents which must be attached. Two directors or officers of the franchisor must sign a jointly and severally binding certificate that the representation in the FDD are true. The franchisor is required to keep its FDD updated with all subsequent material changes to itself or its franchise system.

If a franchisor provides its FDD less than 14 days before any franchise-related agreement is signed, the franchisee may cancel all franchise-related agreements within 60 days after receiving the FDD. If the franchisor fails to provide a FDD, the franchisee may cancel the FA within 2 years after it was signed. In both cases, the franchisor must compensate the franchisee for its net losses incurred in acquiring, setting up and operating the franchise. The franchisee may also sue the franchisor for damages for any misrepresentation made in the FDD.

The Alberta Act’s restriction on deposit-taking does not apply if the franchisor only takes a deposit not exceeding 15% of the initial franchise fee which is fully-refundable if the prospective franchisee does not proceed, so long as the prospective franchisee does not at the same time become bound to enter into a FA. The prohibition on signing any franchise-related agreement does not apply to an agreement dealing with the foregoing deposit, a confidentiality covenant or the designation of a location or territory for the prospective franchised business.

The Alberta Act requires the franchisor’s FDD to disclose statutory rights of franchisees to cancel and obtain damages for misrepresentation.

B. ONTARIO (John Rogers, Toronto)

Ontario’s Arthur Wishart Act (Franchise Disclosure), 2000 (the “Ontario Act”) is similar to the Alberta Act (the first franchise statute in Canada), although there are some important differences.

Firstly, the Ontario Act may apply even if the potential franchisee does not reside in Ontario or have a PE in Ontario. The Ontario Act only requires that the franchise itself be intended to be operated in Ontario.

Secondly, the content of the FDD required in Ontario is different. For example, an Ontario FDD must include various warnings, including that “Independent legal and financial advice in relation to the FA should be sought prior to entering into the FA” and “A prospective franchisee is strongly encouraged to contact any current or previous franchisees prior to entering the FA”. The Ontario Act requires disclosure of information about all directors and officers of the franchisor, while Alberta restricts disclosure to those directors and officers who are active in management of the franchise system. The Ontario Act also requires a franchisor to disclose various regulatory licenses and permits that the franchisee will need to operate.

Unlike Alberta, Ontario requires a franchisor to provide a FDD to a prospective franchisee at least 14 days before taking any deposit, or signing any deposit agreement or any confidentiality agreement.

The effect of failing to provide the FDD on time (or at all) is the same as in Alberta, however, the Ontario Act gives the franchisee more potential compensation than the Alberta Act. The Ontario Act requires a franchisor to refund all money received from the franchisee, to re-purchase inventory, supplies and equipment at a price equal to the purchase price (invoice price) paid by the franchisee, and to compensate the franchisee for any losses it has incurred in acquiring, setting up and operating the franchise. The Ontario Act also extends liability from the franchisor to a “franchisor’s associate” (i.e., someone who, among other things, exercises significant operational control over the franchise) for any misrepresentations contained in the FDD. The Ontario Act does not relieve a franchisor of liability (as Alberta does) if the FDD has some minor defects, however, is “substantially complete”.

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As in Alberta, Ontario does not require registration of the franchisor or vetting of the disclosure document. The same applies to Manitoba, New Brunswick and PEI, so that neither registration nor vetting is currently required in any of the 5 Canadian provinces with franchise laws.

C. Recent Trends in Ontario Franchise Cases (Susan Friedman, Toronto)

Ontario Courts have issued a number of decisions interpreting the *Ontario Act* which clearly favour the franchisee. The most significant of these is 405341 Ontario Limited v. Midas Canada (“Midas”).

The Midas decision was rendered by Ontario’s highest Court, the Court of Appeal, on an appeal of a Superior Court decision certifying a class proceeding against Midas (the franchisor) and an alleged breach of Midas’ statutory and common law duties when it outsourced product supply to a third-party supplier. The franchisees complained that the outsourcing resulted in products of inferior quality, along with increased prices. The Court of Appeal in upholding the Trial Judge’s certification of the class proceeding, stated that (*emphasis added*):

**The purpose of the Act is to protect Franchisees.** The provisions of the Act are to be interpreted in that light.

In *Midas*, the Ontario Court of Appeal held that a FA’s requirement for a release of all potential claims the franchisee may have against the franchisor as a condition of renewal will normally be found unenforceable under section 11 of the *Ontario Act*. The Court went on to find that such a condition offends the purpose and spirit of the Act:

“To permit the appellant [Midas] to require the class members [franchisees] to release any claims they might have against the appellant in order to take advantage of any other rights they might have under the [Franchise] Agreement, in my view, is simply contrary to the spirit, intent and letter of the Act. Where a franchisor insists upon such a waiver or release, s.11 makes it clear that any such waiver or release will be void…”

Ontario Courts have also recently given an expansive interpretation to the franchisor’s duty of fair dealing which is established in section 3 of the *Wishart Act*. In 6792341 Canada Inc v. Dollar It Limited, the Ontario Court of Appeal considered the right of a franchisee to rescind or terminate a deficient FA under section 6(2) of the Act. The numbered company had entered into a FA with the franchisor in 2007. Both parties agreed that the franchisor’s disclosure was deficient, however, differed on the true effect of the deficiencies. In arriving at a decision that the franchisee was able to rescind, the Ontario Court of Appeal reaffirmed that a franchisor’s ability to exercise its sole discretion cannot be applied to take an action that is against the “express rules as well as the spirit, letter and intent of the Act.”

In *Salah v. Timothy’s Coffees of the World Inc*[^6], the Chief Justice of Ontario held that the *Ontario Act* permits an award of damages for the breach of the duty of fair dealing that is separate and in addition to any award that may be made in compensation of pecuniary losses.

In response to this judicial trend favouring franchisees, it is imperative that franchisors doing business in Ontario be given current legal advice with regard to all aspects of their FDD’s and FA’s.

[^2]: Supra, note 2 at para 30.
[^3]: Midas, Supra note 3, at para. 29.
[^4]: 6792341 Canada Inc v. Dollar It Limited, 2009 ONCA 385 (“Dollar It”)
[^5]: Midas, Supra note1, at para 29 and Dollar It, Supra note 3, at paras 5, 6.
[^6]: (2010 ONCA 673)
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D. Provincial Franchise Laws Generally (John Rogers, Toronto)

Again, there is no federal statute stated in Canada regulating franchising.

Several Canadian provinces do have statutes regulating franchising. Currently 5 provinces (Alberta, Ontario, Manitoba, Prince Edward Island and New Brunswick) have franchise legislation. Another province, British Columbia, has expressed an interest in tabling franchise legislation. At present, then, none of the other 5 provinces (Ontario, Saskatchewan, Québec, Nova Scotia and Newfoundland and Labrador) have legislation specifically relating to franchising, although they do have other legislation which is relevant to franchising.

The franchise laws in Alberta, Ontario, PEI, New Brunswick and Manitoba all require a FDD, however, there are important differences between such laws. Major differences in disclosure requirements are summarized in the following table:

<table>
<thead>
<tr>
<th>Issue:</th>
<th>Ontario</th>
<th>Alberta</th>
<th>PEI(^7)</th>
<th>New Brunswick(^8)</th>
<th>Manitoba(^9)</th>
</tr>
</thead>
<tbody>
<tr>
<td>When is a disclosure document required?</td>
<td>When a proposed franchise business will be operated “partly or wholly in Ontario”(^{10})</td>
<td>When a proposed franchise is to be operated wholly or partially in Alberta AND the prospective franchisee is an Alberta resident (or has a PE in Alberta)(^{11})</td>
<td>The proposed franchise is to be operated “partly or wholly in Prince Edward Island”</td>
<td>The proposed franchise is to be operated “partly or wholly in New Brunswick”(^{12})</td>
<td>The proposed franchise “is operated, or is to be operated, partly or wholly in Manitoba.”(^{13})</td>
</tr>
<tr>
<td>Can a franchisor take a deposit before providing disclosure?</td>
<td>No</td>
<td>Yes, provided it is fully refundable and does not exceed 15% of the initial franchise fee.</td>
<td>No.</td>
<td>No.</td>
<td>Yes, provided it is fully refundable and does not exceed 20% of initial franchise fee (up to $100,000.)(^{14})</td>
</tr>
</tbody>
</table>

\(^8\) Franchises Act, S.N.B. 2007, c. F-23.5  
\(^9\) Bill 15 - Franchises Act and draft Franchise Regulations current as of December 21, 2011  
\(^10\) subsection 2(1)  
\(^11\) subsection 3(1)  
\(^12\) subsection 2(2)  
\(^13\) Supra, note 5, s.2(1)(a)  
\(^14\) Supra, note 5, s.5(14).  

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<tr>
<td>Can a franchisor require a potential franchisee to sign a confidentiality agreement?</td>
<td>Likely no - would be captured under “any other agreement relating to the franchise”</td>
<td>Yes.16</td>
<td>Yes, provided the agreement does not prohibit use of information that comes into the public domain, etc.17</td>
<td>Yes, provided it only contains terms related to keeping confidential information provided to the prospective franchisee and/or designating a location to a prospective franchisee.18</td>
<td>Yes, similar conditions to New Brunswick.</td>
</tr>
<tr>
<td>Is electronic disclosure permitted?</td>
<td>No - since not prescribed by the regulations.</td>
<td>No.</td>
<td>Yes.19</td>
<td>Yes.20</td>
<td>Yes.21</td>
</tr>
<tr>
<td>Is use of a “wrap around” document permitted?</td>
<td>No.</td>
<td>Yes.23</td>
<td>Yes.24</td>
<td>Yes.25</td>
<td>Yes.</td>
</tr>
<tr>
<td>May a “substantially complete” document provide sufficient disclosure?</td>
<td>No.</td>
<td>Yes.26</td>
<td>Yes.27</td>
<td>No.</td>
<td>Yes.28</td>
</tr>
</tbody>
</table>

15 s.5(1)(a).
16 s.4(7)(b).
17 Supra, note 3, s.5(9).
18 Supra, note 4, s.5(11).
19 P.E.I Reg. ECS232/06 s.2(b)
20 N.B. Reg. 2010-92 s.3(b)
21 Manitoba draft
22 a “wrap around” document is defined as an addendum to a foreign disclosure document which adds any information required under the relevant provincial statute that is missing.
24 P.E.I Reg. ECS232/06 s.3(2)
25 N.B Reg. 2010-92 s.4
26 subsection s.2(4).
27 Supra, note 3, s.2(4)
28 Supra, note 5, s.5(10).
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<tr>
<td>Dispute Resolution provision</td>
<td>Regulations prescribe language to be included in disclosure document regarding any availability of mediation(^{29})</td>
<td>No.</td>
<td>Regulations require description of any requirements or restrictions relating to dispute resolution in the disclosure document.</td>
<td>Yes, section 8 of the Act and a form is prescribed by regulation(^{30}).</td>
<td>If FA provides disputes may be subject to mediation/arbitration, the disclosure document must include information about the procedures.</td>
</tr>
</tbody>
</table>

**F. Leasing (Justin Mooney, Toronto)**

Typically, the relationship between a landlord and a franchisor will either be:

1. A direct relationship with the landlord and the franchisor, as tenant, being the parties to the lease. In this scenario, the franchisor will then sublet the premises to its franchisee pursuant to a written sublease. Ideally, the lease itself will grant the franchisor the right to sublet to any franchisee without the landlord’s consent.

2. An indirect relationship with the landlord and the franchisee, as tenant, entering into the lease. In this scenario, it is important that the franchisor obtain a right, in the event that the franchisee/tenant defaults in its obligations under the lease, to cure such default, assume the franchisee/tenant’s obligations under the lease and, ideally, to have the right to substitute a new franchisee as tenant and then ‘step out’ (be released). It is often a challenge for the franchisor to obtain all of these rights from a landlord, who may insist on the franchisor providing an ongoing guarantee of any tenant/franchisee’s obligations under the lease. If a guarantee is agreed to, the franchisor should try to limit it to say 3 months arrears of rent. To be enforceable, this ‘step-in’ right must be granted directly by the landlord to the franchisor, either in a separate agreement or in the lease itself; in either case, the landlord will need to be a party to enforce the rights it is given. Ideally, the ‘step in’ right will be contained in a triplicate agreement, with the landlord, tenant/franchisee and franchisor as all signatories.

Real property matters are governed provincially in Canada. Accordingly, statutory and common law rights that benefit the landlord and tenant will vary somewhat from province to province and special attention must be given to identifying issues that may be unique to a particular provincial jurisdiction.

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\(^{29}\) O Reg. 581/00, s.5(2).

\(^{30}\) N.B Reg. 2010-93.

\(^{31}\) *Supra*, note 5 at s.5(6)

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G. QUÉBEC (Pablo Guzman and Felix Touzin, Montreal)

Although Québec does not currently have franchise disclosure legislation, there are various Québec-specific issues about which franchisors considering an expansion into the province of Québec must be aware. Davis LLP’s Montreal office deals with these issues, of which the following 5 may be the most relevant:

1. Duty to Act in Good Faith

The Code governs franchising as it does all business relationships in the province. (Québec is the only province of Canada to be governed by a civil code.) The Code imposes a duty of good faith upon parties to an agreement and forbids any party from exercising a contractual right primarily to harm another party. The duty to act in good faith may require a franchisor to reveal material facts to a franchisee in certain circumstances, for example when it is aware of a negative circumstance specifically affecting a proposed franchise location.

2. Contracts of Adhesion

The Code’s treatment of “contracts of adhesion” is particularly relevant to franchisors. A contract of adhesion is one in which the essential terms are drafted and imposed by one party upon the other without being subject to negotiation. Most FAs are contracts of adhesion because, with the possible exception of minor changes, they are non-negotiable in that they are drafted by the franchisor, for the franchisor, and the franchisee generally must “take it or leave it”.

When a FA is considered a “contract of adhesion”, the Code requires it to be drafted in clear and understandable language. Moreover, any external provisions referred to in the agreement, however not expressly brought to the attention of the franchisee, as well as any “abusive” or overly onerous terms, risk being deemed unenforceable by a Québec Court.

3. Franchisor Liability

Pursuant to the Code, manufacturers, distributors and suppliers of goods are all bound to warrant the quality and ownership of goods sold. On this basis, a franchisee buying goods from a franchisor or its associate may seek redress against the manufacturer and all parties involved in the chain of distribution, including and franchisor/associate-supplier. The Code and the Consumer Protection Act, of Québec may limit the extent to which franchisors are able to disclaim warranties in respect of such goods, for example, warranties that protect end consumers.


The Charter establishes French as the official language of Québec and requires the use of French in a variety of circumstances. Of particular note are requirements relating to commercial advertising. Pursuant to the Charter, all commercial advertising, including all catalogues, brochures, folders, commercial directories and similar publications, must be drawn up in French. An English translation of such advertising may be provided so long as the French version appears no less prominently.

The Charter has traditionally been interpreted by Québec Courts as covering the websites of entities doing business in Québec. If a franchisor outside Québec is found to be carrying on business in Québec, the Charter may require the franchisor to translate its website (or a portion thereof) into French.

The Charter states that employees have a right to carry on their verbal and written activities using French. Accordingly, every employer is required to draw up its written communications to employees in the French language and to publish offers of employment or promotion in French. On this basis, Québec jurisprudence suggests that all corporate policies and procedures, employment handbooks and miscellaneous written
communications addressed to employees must generally be drafted in French. The French version of these documents may be accompanied by an English version, provided the French version appears at least as prominently as the English one.

Québec has recently increased fines imposed on individuals and businesses found to have violated the Charter. A distinct offence has also been created for those (including directors and officers) who assist, advise, encourage or incite an individual or a business to violate the Charter.

5. **Taking Personal Property Security in Québec**

The Code governs personal property interests in Québec and establishes the “hypothee” (similar to a mortgage) as the primary form of personal property security available. A hypothec is a general or specific charge or lien on any kind of property which secures a legal obligation. The hypothec must be registered at the Québec Register of Personal and Movable Rights (the “RPMR”) to be enforceable against third parties and will rank according to the date and time when registered at the RPMR.

Instalment sale agreements (the Québec equivalent of a conditional sale) and personal property leases are other commercial instruments that could be used by franchisors to protect themselves in the case of default by a franchisee.

Although there are similarities between Québec’s personal property security regime and that of the other provinces, the foregoing are important distinctions that must be considered.

6. **Bertico v. Dunkin Donuts - 2012 Québec Decision**

Prior to the decision of *Bertico Inc. c. Dunkin’ Brands Canada Ltd.* (the “Dunkin’ Donuts decision”) in Québec in 2012, the responsibilities of franchisors with respect to brand protection and promotion in Québec were unclear at best. Historically, franchisors had been under no obligation to guarantee the success of their franchisees, for whom they had neither been considered as guarantors nor insurers. Now, according to the Dunkin’ Donuts decision, franchisors have a general responsibility to act competently to enhance their brands and to ensure their systems are viable as going concerns. In the Dunkin case, 21 former Dunkin’ Donuts (“DD”) franchisees sued the franchisor for its failure to protect and enhance the DD brand in Québec.

In the early 1990’s, DD was the market leader in coffee and donut sales in Québec, and had the greatest number of coffee and donut locations in the province. This dominance changed dramatically when Tim Horton’s entered the Québec market. Even though many franchisees expressed their concerns to the franchisor, little was done about the loss of sales to Tim Horton’s and by 1996, the DD franchisor had lost its position as market leader in Québec to Tim Horton’s. Things got worse for DD from there.

The plaintiff franchisees sued the franchisor for negligence and breach of contract. They argued that the franchisor had managed its system in such a way as to damage the brand, and that changes it had made in product offerings were unsuitable for the Québec market. Furthermore, they claimed the franchisor had failed to address the competition provided by Tim Horton’s, had allowed Tim Horton’s to capture the market and had driven many DD franchisees into insolvency. The plaintiffs sued DD for $16.4 million in damages.

DD denied any breach of its obligations, alleging instead that the franchisees were responsible for the demise of the brand in that they had failed to operate clean and modern facilities. It also took the position that it was not a guarantor of the franchisees’ success. Also, the franchisor pointed to a “Quittance générale” that franchisees had signed when they renovated their stores, as a complete bar to their right to bring a lawsuit against the franchisor.
The Court ruled that the franchisor had breached implied and express contractual obligations it owed to its franchisees, and awarded the full $16.4 million claimed. Since in Québec FAs are almost always characterized as “contracts of adhesion” (see G.2 above), the Code requires a FA to be drafted in clear language, failing which a clause, “is interpreted in favour of the adhering party”. The Court found that the most important obligation assumed by the franchisor in its FAs was protecting and enhancing its brand, that DD failed to do so in the Québec market, and that this was “an ongoing, continuing and successive obligation” of the franchisor. Moreover, the “Quittance générale” which most franchisees had signed, was not upheld by the Court because the failure to protect and enhance the brand was constant for more than a decade.

Although the Dunkin’ Donuts decision was rendered in Québec and is based on a lengthy set of facts, it still significantly expands the duties franchisors owe to franchisees with respect to brand promotion and protection, as well as liability for failure to discharge such duties. Justice Tingley noted that “Although not the insurer of the franchisees nor a guarantor of their success, [the franchisor] is nevertheless responsible to them for the harm it has caused by its civil faults.”. Moreover, Justice Tingley held that all FAs contain an “underlying assumption” that “the brand will support a viable commerce”.

Finally, the Dunkin Donuts decision highlights a lack of communication between the parties and sends a clear message to franchisors that they should have meaningful consultations with their franchisees when they raise valid concerns and that franchisors should move to redress such concerns in a timely manner.

H. British Columbia (John Rogers, Toronto)

The franchise-regulated provinces of Alberta, Ontario, New Brunswick, PEI and Manitoba, as well as the Code, all impose duties of good faith on franchisors and franchisees. The common law of the other 4 provinces may do so as well. Generally, in Canada it is likely that each party to a contract is required to act honestly, fairly and reasonably, and must not attempt to prevent the other party from enjoying its fruits of the contract.

In addition, most provinces of Canada have enacted laws regarding trade practices, consumer protection, advertising, income and sales tax, and other business and property-related matters.

On February 5, 2013, the British Columbia (BC) Branch of the Canadian Bar Association (the “BC Branch”) issued an “Agenda for Justice” which includes the following recommendations for legislation to the Government of BC:

“In 2012, the British Columbia Law Institute began a project on a Franchise Act for BC. Franchisees are usually run by small business owners operating businesses under licenses by franchisors. Franchisees are found in many industries: food, retail and services. Small business owners in BC make up 98 percent of all businesses in BC and many of these businesses are franchisees. These small businesses often lack the resources to fight unscrupulous franchisors. Where there are disputes, BC franchisees often have to litigate in Ontario or even the United States since it is common for FAs to require disputes to be resolved by the governing law of the franchisor, which is usually a foreign jurisdiction. Litigating outside of BC is often prohibitively expensive for BC franchisees. A Franchise Act for BC would fairly balance the interests of both parties and it would provide protection to small business franchisees.”

If BC does enact a Franchise Act, it would be the 6th of 10 Canadian provinces to do so (as noted earlier, Alberta, Manitoba, Ontario, New Brunswick and Prince Edward Island already have franchise legislation).

Presumably, a Franchise Act in BC would include a duty of good faith. In any event, another statute proposed by the BC Branch would apply such a duty to all types of contracts. The BC Branch has proposed the following:
“Enact the Contract Fairness Act as recommended by the British Columbia Law Institute. The Act creates a duty of good faith in the performance of contracts. This Act addresses remedies for misrepresentation. Currently, the law is a complicated patchwork of confusing rules. The Act would make it easier for business to resolve disputes, reduce Court cases, reduce Court time and increase clarity in the law.”

In October 2012, the British Columbia Law Institute (“BCLI”) began a project on bringing forth recommendations for a Franchise Act for British Columbia. This leaves British Columbia as the most populated province in Canada that has yet to enact franchise legislation. BCLI has stated that it will be publishing a consultation paper with a tentative recommendation in the near future. After public consultation, BCLI will produce a report with final recommendations and draft legislation.

I. Employment Considerations (Provincial) (Michael Richards, Toronto)

Employment law in Canada is generally an exclusive power of the provinces, except with respect to particular businesses that fall within the exclusive jurisdiction of the federal government (such as banking and telecommunications) or businesses that cross provincial or national boundaries (such as inter-provincial trucking).

Every FA should expressly provide that the franchisee is exclusively responsible for hiring, supervising and terminating its employees and that the franchisor has no responsibility for any such employees. The FA should also be clear that there is no employment relationship created between the franchisor and the franchisee and that the franchisee is an independent contractor. A franchisor should then ensure that its conduct is consistent with the FA and that it does not intervene in any aspect of the employment relationship between the franchisee and any of its employees or treat the franchisee as it would an employee.

If a franchisee’s employee were to bring a claim against the franchisee and the franchisor, a Court or administrative tribunal in Canada would consider the express terms of the FA, the operations manual and the actual conduct of the parties in deciding whether one or both of the franchisee and franchisor was liable to the employee. If the employee’s claim were to be made under an employment-related statute, the statute would also be considered, as some statutes may have the effect of extending liability in respect of employees beyond their franchisees to franchisors.

J. Personal Property Security - Security Agreements (Sandra Appel, Toronto)

Since many franchisors supply products or equipment to their franchisees, franchisors should consider taking a security interest in these assets and perhaps other assets of the franchisee to secure payment of monies owing to the franchisor or performance by the franchisee of certain obligations. A security interest may be taken by inserting specific security language in the FA or by obtaining a separate security agreement.

Security language in a FA or in a security agreement, which describes the security interest of the franchisor as a secured party in the assets of the franchisee debtor, is governed by provincial law. Although each provincial jurisdiction (other than Québec) has a personal property security statute which is similar to the US Uniform Commercial Code, the statutes are not all uniform. As mentioned, Québec has a civil law personal property instrument known as a hypothec.

Each Personal Property Security Act (“PPSA”) of a common law province establishes the regime for obtaining a security interest in personal property of the debtor (the collateral) and the priority rules for security interests in the same collateral or assets of the debtor. It is usually a two-step process to have a valid and enforceable security interest in the equipment or inventory provided by a franchisor to a franchisee. The first step is “attachment; the second step is “perfection.” Although these are terms of art, essentially attachment occurs when value is given, the debtor has rights in the collateral and the debtor has signed a security agreement (or FA) that contains a description of the collateral sufficient to enable it to be identified.
“Perfection” is usually accomplished by the registration of a financing statement in the appropriate Personal Property Security Registration System maintained by the relevant province.

Each PPSA establishes the requirements for registration of a financing statement, including what information must be included and the required format. Generally, the information includes the correct legal name of the debtor, the address of the debtor, the name of one secured party and its address, and a description of the collateral in which the secured party is claiming the security interest. Again, it is important to ensure that the collateral is sufficiently described so as to enable it to be identified. The Ontario PPSA still requires that the financing statement be completed by a “check the box” system, requiring the secured party to classify whether the collateral is “consumer goods”, “inventory”, “equipment”, “accounts” or that the classification is other than consumer goods, inventory, equipment or accounts, or any combination thereof. This provision therefore requires that the secured party understand the nature of the goods being supplied to the debtor and how these goods are considered under the Ontario PPSA. Additional descriptive language may also be provided. In most other provinces the equipment, inventory and any other assets are described by the insertion of descriptive language on the financing statement.

Unless the collateral is “consumer goods”, a financing statement may be registered before or after the security agreement is signed by the debtor. The ability to register in advance allows the franchisor to have a security interest in inventory or equipment before it is supplied to the franchisee. It is also significant since priorities are generally determined by the “first in time to register”, subject to some specific priority rules.

One very important specific priority rule is the purchase-money security interest or “PMSI” described below, which can be of value to a franchisor.

A PMSI is described in the Ontario PPSA (and similarly in the PPSA of 8 other provinces (not Québec)) as:

(a) a security interest taken or reserved in collateral to secure payment of all or part of its price,
(b) a security interest taken in collateral by a person who gives value for the purpose of enabling the debtor to acquire rights in or to the collateral, to the extent that the value is applied to acquire the rights, or
(c) the interest of a lessor of goods under a lease for a term of more than one year;

but does not include a transaction of sale by and lease back to the seller.

Although the PPSA grants a priority position to the vendor of equipment or inventory to a debtor or to the lender who provides funding to the debtor to enable the debtor to purchase inventory or equipment, the PPSA sets out the rules or steps that must be adhered to before this priority position may be attained. These steps are different for inventory and equipment suppliers. These steps are also in addition to the steps set out in the PPSA for obtaining a security interest.

In Ontario, for example, for inventory, a PMSI has priority over any other security interest in the same collateral of the same debtor, if:

(a) the PMSI was perfected (i.e. a financing statement registered) at the time the debtor or a third party, at the request of the debtor (like a warehouse), obtained or held possession of the inventory, whichever is earlier;
(b) before the debtor received possession of the inventory, the PMSI holder has given notice in writing to every other secured party who has, before the date of registration by the PMSI holder, registered a financing statement that describes the collateral as or including (i) items or types of inventory, all or some of which are the same as that of the PMSI holder, (ii) inventory, or (iii) accounts; and
(c) the notice referred to in (b) states that the person giving it has or expects to acquire a PMSI in inventory of the debtor, describing such inventory by item or type.

For equipment, a PMSI has priority if the security interest was perfected (i.e. a financing statement registered) before or within 15 days after (i) the debtor obtained possession of the collateral as a debtor, or (ii) a third party, at the request of the debtor, obtained or held possession of the collateral, whichever is earlier.
As noted, the general priority rule applies if no specific priority rule is available. The PMSI rules are special priority rules, however, will only apply if their requirements are met. So, for example, a supplier of goods to a debtor will have priority over a general lender to the debtor, even if the lender has registered in advance of the supplier, if the PMSI rules have been satisfied. In addition, the special priority rules usually provide that where more than one PMSI is given priority by the PPSA, that the PMSI, if any, of the seller has priority over any other PMSI given by the same debtor. (e.g. PMSI of a lender who gave value to enable the debtor to acquire rights.) Obtaining a security agreement and complying with the PMSI rules should enable a franchisor to obtain a first secured position with respect to the goods sold by the franchisor to a franchisee.

Finally, a secured party needs to be mindful that each PPSA sets forth a number of obligations for a secured party to ensure that it remains a secured party with a valid and enforceable security interest.

V. EXPANDING TO CANADA (John Rogers, Toronto)

For a foreign franchisor considering a Canadian expansion, the recommended first step is to obtain a detailed marketing study which will allow the franchisor to determine whether Canada might be a good market for its franchise system.

If the Canadian market looks favourable, the franchisor should next prepare a marketing plan to help target the most appropriate regions of what is a very broad country. The franchisor should then establish several pilot operations to determine the needs of local markets before extensive expansion is undertaken.

Once the franchisor has decided to proceed with a franchise expansion to Canada, it will need to determine how its franchise system will be structured here.

A. Who will run the Canadian operation?

The first issue is determining the vehicle to run the expansion. There are several possibilities:

1. Foreign Franchisor

The simplest alternative is for the foreign franchisor to grant franchise rights in Canada by using its existing sales and administrative staff. This approach is often called “direct franchising” and is attractive because it avoids additional start-up costs of establishing a presence in Canada. However, it does not allow the franchisor to shield itself from potential liability which may be incurred in Canada and it may be discomforting to potential Canadian franchisees who want ongoing support and contact with a local office. A longer term solution should be considered.

2. Canadian Branch

Another alternative is for a foreign franchisor to open a Canadian branch office. The franchisor could continue to grant franchises directly, although support and administration would be handled by the Canadian branch office. The branch would be a PE of the franchisor in Canada, which will make the franchisor subject to Canadian Income Tax on income attributable to such branch. (See, further, Part III.E above). However, start up losses may be offset against the income of the franchisor in its home country and, depending on where the franchisor is resident, the first $500,000 of net Canadian income from the branch may be remitted to the franchisor at a tax effective rate. Still, the use of a branch will do nothing to protect the franchisor’s assets from debts and liabilities of the Canadian operation.
3. Canadian Subsidiary

A third alternative is for the foreign franchisor to incorporate a Canadian subsidiary to operate the franchise system in Canada. This method is popular as it allows the foreign franchisor to establish a local presence and still insulate its home operation from potential liabilities, including any operating losses, in Canada.

The subsidiary would be a separate Canadian taxpayer and therefore any start up losses of the subsidiary could generally not be deducted against the income of the parent corporation. Payments of income or dividends from the subsidiary to the franchisor parent would be subject to Canadian withholding tax. The operation of the subsidiary would generally not constitute a PE of the franchisor parent corporation and therefore the parent could sell services to the subsidiary without incurring Canadian income tax liability, subject to pricing reasonableness under “transfer pricing” rules.

The subsidiary may either be incorporated under the federal laws of Canada or the laws of a particular province or territory. The advantage of incorporating federally is that the new corporation would be entitled to carry on business under its name throughout Canada (although it would be required to register separately in each province or territory when it began to carry on business there, and it might need to adopt a second French name in the province of Québec).

A Canadian corporation (including a subsidiary) may be incorporated using its incorporation number plus a descriptive word, for example “956871 Ontario Holdings Ltd.” In this case, the Corporations Branch will fill in the next available incorporation number when it receives incorporating documents. Later on, the numbered name may be changed to one that is more descriptive, for example, “Paris Diner Franchises Inc.”

There may be advantages to incorporating in a particular Canadian province or territory; each has some different rules. For example, companies incorporated in some provinces require a majority of directors to be resident in that province; however, there is no residency requirement for a company incorporated in British Columbia.

Regardless of where the franchisor decides to incorporate in Canada, under the federal Trade-marks Act, the Canadian subsidiary must have a license agreement with the parent, under which the subsidiary agrees to protect the parent’s Canadian trade-marks and confidential information of the franchise system.

4. Joint Venture or Partnership

Joint ventures or partnerships involving Canadian operations often involve a foreign franchisor granting a master franchise to a Canadian corporation. It is crucial for the franchisor to choose a Canadian joint venturer or partner with appropriate experience and knowledge of the Canadian market.

B. How should the Canadian franchise system be structured? (John Rogers, Toronto)

Setting up the structure of a new Canadian operation is important. There are at least 4 options for a foreign franchisor to choose from, depending upon the amount of participation it wishes to have in Canada:

1. Unit Franchise

The first option is for the franchisor itself to grant individual (or “unit”) franchises to individual franchisees in Canada.

2. Area Representation

The second option is to grant area representation rights to a particular territory in Canada to an area representative in exchange for a fee. The area representative would have a marketing function, and would
receive the exclusive right to market the franchise system within such territory, where it would be responsible for locating potential franchisees and potential franchise locations for the franchisor to act on.

Once the representative has located a potential franchisee and a potential location, it will be up to the franchisor to decide whether to grant a franchise; the area representative will have no authority to do so. If the franchisor approves of a potential franchisee and location, then the franchisor will enter into a unit FA directly with that franchisee, and the area representative will receive a portion of the initial franchise fee as well as a portion of ongoing royalties if it participates in ongoing administration.

3. **Area Development**

Under the third option, a number of Canadian entities may be granted rights to specific regions or territories, within which they will be required to open specific numbers of franchise outlets within specific time frames. The developers will participate personally in the franchise system, often acting as franchisees, either directly or through subsidiaries or affiliates.

4. **Master Franchise**

The fourth option is to grant franchise rights to a master franchisee which, in turn, will sublicense those rights to unit franchisees. Here, power to approve individual (sub)franchisees and approve individual locations is given to the master franchisee.

Nonetheless, the franchisor will want to ensure that it maintains ultimate control over the expansion. The master FA should limit the extent of the territorial rights granted to the master franchisee and impose minimum performance obligations (quotas) on openings to encourage timely expansion of the system within Canada.

An appropriate fee to be paid by the master franchisee and a formula for the franchisor and master franchisee to share initial fees and ongoing royalties to be paid by Canadian (sub)franchisees are important factors. The franchisor must ensure that the master franchisee receives sufficient remuneration to run the Canadian expansion and make a reasonable profit, while also ensuring that the franchisor itself is appropriately compensated for its costs and the expansion value of its system.

C. **“Canadianizing” an existing FA (John Rogers, Toronto)**

A foreign FA (or subfranchise agreement in the case of a master franchise arrangement) and related documents will need to be revised for use in Canada. There are several key issues to keep in mind when doing so. The above commentaries should be helpful in accessing the following issues:

1. **Trade-marks (see also III.A. 1 and 2 above)**

First, the FA must give the Canadian franchisee a license to use the franchisor’s trade-marks, copyrights, and any patents or other intellectual property in an exclusive or non-exclusive territory of Canada. It must expressly reserve to the franchisor direct or indirect control over the character and quality of the goods and services offered by franchisees under the franchisor’s trade-marks.

The FA will allow the franchisor to establish standards, policies, and rules governing all products and services sold in association with licensed trade-marks and to enter the franchisee’s premises and inspect the way the franchisee is actually using the Marks. The franchisee will be prohibited from challenging the validity of the Marks or claiming or using any other trade-mark that is confusingly similar to any of the franchisor's Marks. The agreement should also deal with graphic standards and other rules governing how the franchised Marks and other proprietary material may be reproduced and used. It should also address ownership issues, potential
lawsuits, infringements by third parties, assignments and sublicensing and “de-identification” with Marks and the franchise system by the franchisee upon a default and termination.

The franchisor should require the Canadian franchisee to display notices on the franchised premises that the franchisor has licensed use of the trade-marks to it. Under the Trade-marks Act, such notification gives the franchisor the benefit of a presumption at law that the franchisee’s use is licensed and that the character or quality of the related goods or services is under the franchisor’s control.

If the trade-marks are only pending for registration in Canada when the Canadian franchise documentation is prepared, the FA should say so and should give the franchisor the right to substitute different trade-marks if Canadian registration applications prove unsuccessful. The franchise documentation should also address the possibility and costs of changing signage and other branded items where change is necessary.

2. Domain Names (see also II.A.3 above)

Internet, intranet and extranet websites may be an effective way for franchisors to communicate with their franchisees, potential franchisees, and the public. The franchisor’s ability to maintain an effective Internet presence will depend largely on the domain names the franchisor has registered compared to ones third parties have registered. Therefore, the FA should specifically prohibit or limit the franchisee’s ability to register domain names incorporating any material part of the franchisor’s trade-marks.

It was once very difficult to register a top level Canadian (“.ca”) domain name, and there were once restrictions on the number of “.ca” domain names that one applicant could register. This changed in November 2000, and it is now much easier to register “.ca” domain names. It is now possible to register as many “.ca” domain names as an applicant pleases. Unfortunately, some “enterprising” individuals are registering domain names in Canada that incorporate well-known trade-marks and business names owned by others. If franchisors do not act expeditiously to register all of their trade-marks and business names as domain names, and if they do not prevent their franchisees from doing so, then they may lose control over a portion of their Internet presence in Canada.

In response to these issues, the Canadian Internet Registration Authority has established a domain name dispute resolution policy whereby owners of well-known marks and names may seek to have “pirated” domain names registered in Canada cancelled or transferred to themselves.

3. Applicable Law/Courts

The FA should set-out clearly which jurisdiction's laws and Courts will apply to any litigation that may occur between a franchisor and franchisee.

A foreign franchisor should think carefully before naming its own jurisdiction (laws and Courts) as the exclusive jurisdiction for litigation. For example, if a franchisee breaches the FA, the franchisor may need an injunction to prevent the franchisee from misusing intellectual property, competing or otherwise behaving inappropriately. It is difficult to “transport” an injunction from a foreign jurisdiction to Canada since a Canadian Court will have to rule whether the injunction is enforceable within a Canadian jurisdiction. It is also easier to enforce payment obligations in Canada through Canadian Courts.

In Alberta, Ontario, New Brunswick, PEI and Manitoba, franchise legislation requires that the laws and Courts of the home province be used for claims enforceable under their franchise legislation and the FA should reflect this fact for franchises located in one of those provinces. However, FAs for franchised businesses to be located in those provinces may still provide that non-statutory based claims will be governed by the law of another jurisdiction.

If the province where a particular franchise is located has adopted the Model Law on International Commercial Arbitration (formulated by the United Nations Conference on International Commercial Arbitration), disputes related to a FA (although not remedies specifically provided in franchise statutes)
may be made the subject of international commercial arbitration which may properly require a hearing in the franchisor’s home jurisdiction.

4. **Non-Competition and Confidentiality**

Canadian FA include restrictive covenants (non-competition clauses) to prevent franchisees from competing with the franchisor during the term of the FAs and for a period of time after their expiration or earlier termination. Canadian Courts will not enforce restrictive covenants that go further than necessary to protect the legitimate business interests of the franchisor. If any one of the three key elements of a restrictive covenant (i.e., territory, time and scope of restricted activity) is held to be excessive by a Canadian Court, then, generally speaking, the whole restrictive covenant will be declared unenforceable. Accordingly, it is wise for franchisors to act reasonably in drafting all elements of such covenants.

Also, Canadian FAs normally include clauses by which franchisees agree to maintain the confidentiality of their franchisor’s proprietary information such as trade secrets, many of which may be contained in the franchisor’s operations manuals.

5. **Statutory Warranties and Conditions**

Most provinces and territories in Canada have laws which imply specific warranties and conditions into contracts regarding the sale of goods. If a franchisor does not expressly disclaim these warranties and conditions, it may be sued if any products the franchisor supplies do not meet statutory standards of quality. Some of these warranties and conditions cannot be disclaimed, depending upon which province's laws apply, and whether the sale is a commercial transaction or a consumer transaction.

6. **Alternative Dispute Resolution (See also IV.H. above)**

There is an open question as to whether a franchisee may insist on an Ontario Court action if its FA requires arbitration of a dispute with the franchisor.

Many FAs contain provisions requiring the parties to engage in mediation before proceeding to arbitration which is private rather than public proceedings in a Court of law. Sometimes there is a ‘carve-out’ for the franchisor, permitting it to resort immediately to litigation when it wishes to seek an injunction to restrain a breach of a post-termination covenant by a franchisee.

*The Arbitration Act*, 1991\(^{32}\) (the “AA”) of Ontario provides in section 2(1)(a) that it applies to an arbitration under an arbitration agreement unless the application of the AA is excluded by other legislation. Typically, an Ontario Court will stay (discontinue) a law suit if the agreement at issue contains an arbitration provision. Section 7(2) of the AA provides, however, that the Court may refuse to stay a lawsuit commenced contrary to the provisions of an arbitration agreement where the agreement is invalid. There are similar provisions in arbitration legislation\(^{33}\) of other provinces.

The Ontario Court of Appeal has ruled that the fact that a FA might be rescinded (terminated) in reliance on the rescission provisions of the Arthur *Wishart* Act (“*Wishart*”) does not render the arbitration provisions of the FA “invalid” or void ab initio, such that an arbitration must be stayed.\(^{34}\) It is for the arbitrator to determine its own jurisdiction and the merits of the issues respecting rescission. Accordingly, arbitration provisions in FAs will be upheld by the Courts, generally speaking.

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\(^{32}\) S.O. 1991, c. 17.

\(^{33}\) e.g. *Arbitration Act*, RSA c. A-43, ss. 2 and 7.

\(^{34}\) *MDG Kingston Inc. v MDG Computers Canada Inc.*, 2008 ONCA 656 (CanLII), leave to appeal to the Supreme Court of Canada was refused 2010 CanLii 28785 (SCC).
Still, it must be borne in mind that section 10 of *Wishart* provides that a provision of the FA which restricts the application of Ontario law or restricts the venue of adjudication to a place outside of Ontario is void “in respect to a claim otherwise enforceable under this Act in Ontario.” Further, section 11 of *Wishart* provides: “Any purported waiver or release by a franchisee of a right given under this Act or of an obligation or requirement imposed on a franchisor or franchisor’s associate by or under this Act is void.” In the result, if an agreement provides that disputes are to be arbitrated in a forum outside of Ontario, whether an Ontario Court will recognize the resulting decision may turn on whether or not the claim was a statutory one enforceable under *Wishart* or whether it was purely a contractual or common law claim.

Further, when confronted with a class action in relation to FAs that contain an arbitration provision, the interplay between the AA, *Wishart* and the *Class Proceedings Act 1992* (“CPA”) must be taken into account. Although Canadian Courts see value in enforcing parties’ agreements to resolve disputes through arbitration in accordance with the provisions of the AA and similar legislation, they also acknowledge a competing interest in ‘access to justice’ concerns which led to the enactment of class proceedings legislation. The result has been the use of the “preferable procedure” criterion, a critical part of a certification motion, as being the analytic tool by which the Court determines whether to exercise its discretion and assert jurisdiction over the dispute or defer to an arbitrator. Accordingly, a franchisor cannot rely on the inclusion of an arbitration provision in a FA to preclude a class action suit against it.

A “no class action” provision in an Ontario FA will not be upheld by the Court. Section 4(1) of *Wishart* gives franchisees the right to “associate with other franchisees” and section 4(4) provides that any provision in an agreement that purports to interfere with this right is void. The Courts have held that this right of association includes the right to participate in a class action for the purpose of enforcing rights against a franchisor under *Wishart* or otherwise. It is therefore arguable that section 4 of *Wishart* is “other legislation” within the meaning of section 2(1)(a) of the AA, so that the AA precludes the application of *Wishart*.

In the end, it may be more convenient for a FA with an Ontario franchisee to provide for an arbitration to be heard in Ontario under AA rules, as this convenience may cause the franchise not to claim a right to litigate under *Wishart*.

### 7. Miscellaneous

There are a few other considerations to keep in mind for a Canadian FA. For example, the foreign franchisor will have to decide how to structure its advertising fund in Canada. Will contributions from Canadian franchisees be combined with those in an international fund, with a portion of such fund being used for Canadian advertising? Or will a separate fund be set-up for Canada? Canadian franchisees will normally prefer the second option. In the province of Québec, French language advertising will be required.

The agreement should also specify whether monetary amounts are expressed in Canadian dollars or a foreign currency. If payments are to be made in a foreign currency, the agreement should describe how and when currency conversion will occur and who bears the cost of conversion.

In addition, an annual interest rate for late payments must be expressed. If the franchisor fails to do so, the franchisee will only be required to pay interest at a statutory federal rate of 5% per year.

Provision also needs to be made for any non-resident withholding taxes on payments which are made on account of initial fees, royalties or interest. The agreement should specify whether such payments are net of withholding tax or whether they are to be grossed up. Moreover, the agreement should separate the types of

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35 *Wishart*, section 10.
36 S.O. 1992, c.6, as amended.
38 *405341 Ontario Ltd. V. Midas Canada Inc.*, 2009 CanLii 56298 (ON.SC), Aff’d 2010 ONCA 478.
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payments which are clearly subject to withholding taxes (i.e. royalties) from those which are not; if they are not separated, withholding tax may be applicable to the entire amount. (See further, III.E).

D. FDDs (John Rogers, Toronto)

A detailed FDD must be prepared and given to each potential franchisee at least 14 days before the FA is signed. FDDs used in other jurisdictions will not comply with provincial franchise legislation, although they will provide very useful information in drafting Canadian FDDs. Details concerning Alberta and Ontario FDDs are found under Part III. above.

E. Guarantees (John Rogers, Toronto)

It is generally recommended that franchisors obtain personal guarantees from principals of corporate franchisees so that the franchisor may not be prejudiced by the franchisee’s limited liability upon a default occurring.

The franchisor must pay special attention to the nature and form of the guarantees the franchisor uses in the provinces of Alberta and Québec. To be enforceable, Alberta guarantees must be notarized using a separate, statutory form of acknowledgement. This requirement is not onerous as the form is a single page.

A provision in the Code may make the franchisor question the extent to which it will be comfortable relying on a franchisee guarantee taken in Québec. The provision allows a guarantor to terminate the guarantee after 3 years, upon reasonable notice to the franchisor.

F. Operations Manual (John Rogers, Toronto)

The franchisor's operations manual should be revised to reflect differences in Canadian customs laws and laws applicable to franchise systems. These differences include use of the metric system of measurement and bilingual (English/French) labeling of products mentioned earlier.

VI. Conclusion

Canada has a well-established tradition of franchising and a Canadian expansion is a logical step for many domestic and foreign franchisors. However, careful planning is necessary for such an expansion to succeed. This paper has provided an overview of many planning considerations that will be important for a franchisor considering a Canadian expansion. In the planning and implementation phases, it will be important to seek advice from a Canadian franchise lawyer who is experienced in dealing with franchise systems expanding to or within Canada.

VII. Professional Biographies

(Attached)

Contact Details

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