

Franchising in Australia was the first article in Wiley Rein's International Franchise Development Series. Since it was published on February 25, 2014, there have been significant changes to the regulatory scheme in Australia, which are addressed below. The International Franchise Development Series offers a broad overview of franchise regulation and the legal issues confronting franchisors seeking to expand into certain countries from the combined legal perspective of U.S. and local counsel.

Franchising in Australia – The New Franchising Code of Conduct

By Robert A. Smith, Warren Scott, Bianca Guerrieri, and Maureen O'Brien

Recap of Australian Franchise Regulation

Franchising in Australia continues to be primarily regulated by the Franchising Code of Conduct (the Code), which is found in the *Competition and Consumer Industry Codes – Franchising Regulation 2014 (Cth)*. The Code is administered and enforced by the Australian Competition and Consumer Commission (ACCC), which investigates alleged breaches of the Code and takes enforcement action in appropriate circumstances.

Disclosure

The Code contains mandatory disclosure obligations for franchisors. Franchisors must provide a comprehensive disclosure document to all prospective franchisees, renewing franchisees, and, upon request, existing franchisees. A disclosure document must also be provided to an existing franchisee if the franchise agreement is materially amended. The Code sets out the specific information that a franchisor must provide to franchisees, including extensive details of the franchised business and its operating history.

The prescribed form of the Australian disclosure document is found in Annexure 1 of the Code. All Australian disclosure documents must be in this format. (The ACCC's recommended format for the Australian disclosure document is quite useful. It may be found on the ACCC's website - <https://www.accc.gov.au/>.) Due to the fact that the standard form Australian disclosure document varies substantially from the form of franchise disclosure document prescribed by the Federal Trade Commission Rule, U.S. franchisors cannot simply tweak their domestic disclosures to achieve compliance with the Code.

Franchisors must strictly adhere to certain initial and ongoing disclosure requirements, including:

- providing the disclosure document to a prospective or renewing franchisee at least 14 days before the franchisee signs the franchise agreement;
- ensuring that the disclosure document is accompanied by a copy of the franchise agreement in the form in which it is to be executed — not the template form of agreement as in the U.S; and

continued on page 2

- receiving an executed receipt from the franchisee, stating that the franchisee has had 14 days to read and understand the disclosure document before signing the agreement.

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The disclosure document must be updated annually within four months after the end of the franchisor's fiscal year.

The franchisor must provide an existing franchisee a current disclosure document within 14 days after the franchisee's written request (this request may only be made once every 12 months.) Consequently, even if the franchisor is no longer offering franchises in Australia, it will have to update its Australian disclosure document if an existing Australian franchisee requests a copy.

Franchise Agreements

In addition to disclosure obligations, the Code sets out certain requirements relating to franchise agreements, including:

- a franchisee may terminate the franchise agreement within seven days after the earlier of entering into the agreement or making any payment under the agreement; however, these cooling-off rights do not apply to renewals, extensions, or transfers;
- a franchise agreement may not contain or require a franchisee to sign a general release; and
- if the franchisees are required to contribute to an advertising fund, the fund must be audited annually unless 75% of Australian franchisees agree to waive this requirement.

Amendments to the Code

A revised version of the Code took effect on January 1, 2015. The key changes include:

- **Infringement Notices and Penalties** – the ACCC may issue infringement notices (AU\$8,500 per breach) or apply to a court to seek civil penalties up to a maximum of AU\$51,000 (per breach) for certain breaches of the Code. Examples of a breach that may result in the issuance of an infringement notice or a penalty include:
 - the franchisor or the franchisee not acting in good faith during the franchise agreement;
 - the franchisor failing to update its disclosure document within four months after the end of its fiscal year;
 - the franchisor not giving the franchisee a copy of the key ancillary agreements it will be required to sign before it signs the franchise agreement (*e.g.*, premises lease, equipment lease);
 - the franchisor not notifying the franchisee of its proposed end of term arrangements at least six months before the expiration of the term of the franchise agreement; and
 - failure to re-disclose materially relevant facts when they occur (*e.g.*, the insolvency of the franchisor, a change in the ownership in the intellectual property that is required in the franchise network).
- **Noncompetes** – a franchisor will not be able to enforce a post-term noncompete restriction against a franchisee without compensating the franchisee if the franchisee:
 - wanted to continue the franchise relationship;
 - was not then in breach of the franchise agreement; and
 - was willing to continue the franchise relationship on the terms of the franchisor's then-current franchise agreement.

continued on page 3

- **Marketing Fund** – the Code now requires all marketing funds to be kept in a separate bank account and all units owned by the franchisor to contribute to the marketing fund. As a matter of best practices, all stores within the franchisor group (*i.e.*, whether or not they are technically owned by the franchisor) should contribute to the marketing fund.
- **Information Statement** – franchisors are required to give all franchisees that express an interest in operating a franchised business an information statement. The information statement is located in Annexure 2 of the Code and must be formatted in the manner prescribed by the Code. As a matter of best practices, franchisors should give a prospective franchisee the information statement when the franchisor receives a completed application from the franchisee candidate.
- **Master Franchising** – two separate disclosure documents are no longer required. The standard disclosure document now has a section where details of the relationship between the Australian franchisor (*i.e.*, the master franchisee) and its ultimate master franchisor can be detailed.
- **Significant Capital Expenditure** – a franchisor cannot force franchisees to incur significant capital expenditure during the term of the franchise agreement. This term is not defined in the Code. However, the Code does provide examples of what is not a “significant capital expenditure” (*e.g.*, expenditure detailed in the disclosure document, expenditure required to be made in order to comply with statutory requirements).
- **Dispute Resolution** – a franchisor cannot have a provision in the franchise agreement that expressly requires a franchisee to litigate in an Australian state other than where the franchise business is located or a provision that requires the franchisee to pay the franchisor’s costs associated with settling a dispute.

- **Good Faith** – each party to a franchise agreement (*i.e.*, the franchisor, franchisee and any guarantors) must act in good faith towards each other. The term “good faith” is not defined in the revised Code; however, the common law meaning of the term will be used to test whether a party has acted in good faith or not.

ACCC Enforcement

By all accounts, the ACCC will continue to take an aggressive enforcement stance against franchisors, particularly those in the health and fitness and takeaway food industries. The ACCC will focus on identifying breaches of the competition and consumer law and the Code within the franchising sector.

In Australia, in the event of an inadvertent breach of the Code, organizations that have a compliance plan and training in place may argue that penalties should be minimized. As stated above, franchisors could receive a maximum AU\$51,000 fine (per breach) if certain provisions of the Code are breached. Further, other breaches of competition or consumer law can result in fines of up to (and potentially greater than) AU\$10 million per offense for the corporation and up to AU\$500,000 for individuals.

It appears that the Australian government supports the ACCC’s efforts. Consequently, the Commission’s zealous enforcement activity and resultant slew of legal proceedings will likely continue. As a result, U.S. franchisors already in Australia, and those thinking about expanding to Australia, should continue to stay tuned.

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continued on page 4

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Bob Smith and Chris Connelly will be attending the 48th Annual International Franchise Association Legal Symposium in Chicago, IL from May 3-5, 2015, where Bob will be speaking on international franchising.

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