



Upcoming Changes to Franchise Law

Our firm advises a variety of businesses on their obligations, both locally and internationally, under the *Franchising Code of Conduct 1998* ("the Code") which is given the force of law by the *Trade Practices Act 1974 (Cth)* ("the Act"). The broad definition of what constitutes a 'franchise' under the Code has led to some financial services licensees authorising their representatives to provide financial services on their behalf under franchisee agreements.

In December 2008 a Parliamentary Committee submitted to Parliament a raft of recommendations for changes to the Code and the relevant sections of the Act. It is important that Licensees who authorise representatives to carry on the business of providing and implementing financial product advice where the arrangement constitutes a franchise, familiarise themselves with the requirements of the Code.

Licensees should carefully consider whether the agreements they have with their authorised representatives constitute franchise agreements under the Code.

The Code defines a 'franchise agreement' as an agreement in any form (including an implied agreement):

- in which the franchisor grants to the franchisee the right to carry on the business of offering, supplying or distributing goods or services in Australia under a system or marketing plan substantially determined, controlled or suggested by the franchisor or an associate of the franchisor; and
- under which the operation of the business will be substantially or materially associated with a trade mark, advertising or a commercial symbol:

(i) owned, used or licensed by the franchisor or an associate of the franchisor; or

(ii) specified by the franchisor or an associate of the franchisor; and

- under which, before starting business or continuing the business, the franchisee must pay or agree to pay to the franchisor or an associate of the franchisor an amount including, for example:

(i) an initial capital investment fee; or

(ii) a payment for goods or services; or

(iii) a fee based on a percentage of gross or net income whether or not called a royalty or franchise service fee; or

(iv) a training fee or training school fee.

It is not difficult to see why many arrangements where a financial planner operating as an authorised representative of a financial services licensee might conform with the franchise agreement definition.

On 1 December 2008, the Parliamentary Joint Committee on Corporations and Financial Services Franchising Code of Conduct submitted its 165 page report to Parliament. The report contained 8 recommendations which may impact upon the financial services industry. These are summarised below:

1. That the Code be amended to require that disclosure documents include a clear statement of the liabilities and consequences that apply to franchisees in the event of franchisor failure.

In light of the global economic meltdown and the subsequent increase in insolvencies, particularly within the financial sector, such a provision in an

- authorised representative agreement is prudent as a means of disclosing where the financial planner will stand if the licensee becomes insolvent. Such disclosure will limit the potential for disputes and litigation in the wake of franchisor failure.
2. That an online registration system be developed where franchisors must annually lodge a statement that they are meeting their obligations under the Code and the Act. This is a very onerous requirement particularly for financial licensees with hundreds of authorised representatives. If this recommendation is adopted licensees will need to carefully consider whether they are captured by the Code and consequently ensure they diligently comply with all of their obligations.
 3. The committee considered the difficulties which arise upon the expiry or termination of a franchise agreement. For instance, whether the franchisee should receive payment for the value of the goodwill they have created for the business. Licensees will need to consider these proposals with regard to the ownership of client lists upon the termination or expiry of an authorised representative agreement. The committee has also recommended that the Code includes a reciprocal right for the franchisee to terminate a franchise agreement.
 4. That the Code be amended to require the franchisor to disclose what process will apply in determining end of term arrangements. In addition to the issues discussed in point 3 above, this process would include the potential transferability of equity in the value of the business as a going concern.
 5. The committee recommended that a general requirement of 'good faith' between franchisor and franchisee be incorporated in the Code as a means of minimising disputes and litigation.
 6. Franchisees made submissions outlining the perceived inaction by the ACCC in pursuing complaints against franchisors that are alleged to have breached the Code. The committee recommended that measures be taken to better educate franchisees as to the role of the ACCC. The regulator is not responsible for prosecuting franchising disputes that relate to contractual disputes between the parties. The committee did, however, acknowledge that there was room for improvement by the regulator in taking a more active role in the franchising sector.
 7. That pecuniary penalties for breaches of the Code be incorporated into the Act. From a risk management and financial perspective, this heightens the need for licensees to be aware of whether their activities are captured by the Code and what their compliance requirements are under the Code.
 8. That the ACCC be given broader investigatory powers when it has credible evidence that a party to a franchising agreement may be engaging in conduct that may be in breach of the Code. Licensees should make themselves aware of these provisions as they are in addition to the broad investigatory powers that are afforded to ASIC under the *Corporations Act 2001 (Cth)*.

There are a number of participants in the financial services industry, including several of our major clients, who grant authorisations to financial planners and other representatives, in the form of a franchise agreement. It may be that in the future, the ACCC will deem authorised representative arrangements between licensees and financial planners to fall with the definition of a franchise agreement under the Code. For this reason, it is

important that licensees and representatives respectively remain aware of their obligations under the Code. As indicated above, these obligations are currently in a state of flux as Parliament and the ACCC attempt to establish a balance between the freedom to contract and the regulation of relationships of inequitable bargaining power.

The law is current as at January 2009.

Please note that this paper is a summary of the law only and is not a substitute for legal advice. Holley Nethercote is able to assist companies in meeting their obligations in this area by providing practical and prompt legal advice. Licensing, training and creation of compliance programs are also available via an associated business, Compact- Compliance and Corporate Training – www.compliance-training.com.au.

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