



23 Marcus Clarke Street
Canberra ACT 2601
GPO Box 3131
Canberra ACT 2601
tel: (02) 6243 1111
www.accc.gov.au

11 May 2018

Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
PO Box 6100
Parliament House Canberra ACT 2600

By email: corporations.joint@aph.gov.au

Dear Secretary,

Re: The operation and effectiveness of the Franchising Code of Conduct

The ACCC welcomes the opportunity to make a submission to the Parliamentary Joint Committee on Corporations and Financial Services in relation to the operation and effectiveness of the Franchising Code of Conduct. We appreciate the extension of time provided to the ACCC to complete this submission.

Our submission is attached to this letter. If you require further information or wish to discuss any aspects of this submission, please do not hesitate to contact Tim Grimwade on (02) 6243 1298 or timothy.grimwade@accc.gov.au.

Yours sincerely

Rod Sims
Chairman



Inquiry into the operation and effectiveness of the Franchising Code of Conduct

ACCC Submission

11 May 2018

Introduction

The Australian Competition and Consumer Commission (ACCC) appreciates the opportunity to contribute to this inquiry. The ACCC has an important role in promoting compliance with and enforcing the *Competition and Consumer Act 2010* (CCA), including:

- the Franchising Code of Conduct (the Franchising Code)
- the Oil Code of Conduct (the Oil Code) and
- the Australian Consumer Law (ACL), which contains the small business protection against unfair contract terms.

The ACCC regards the Franchising Code and Oil Code (collectively, the Codes) as important and appropriate regulation in sectors that are not without risk. However, the ACCC is of the view that the incentives to comply with the Codes need to be strengthened by providing the ACCC with more options to detect breaches and seek higher penalties to deter non-compliance.

Compliance with the updated Franchising Code has been a Compliance and Enforcement priority for the ACCC since 2015. The ACCC's 2018 Compliance and Enforcement priorities include ensuring small business receives the protections of industry codes and the unfair contract terms (UCT) law, with a focus on Franchising Code issues involving large or national franchisors.

For ease of reference throughout this submission, franchisors and fuel suppliers will be referred to as Franchisors, and franchisees and fuel retailers will be referred to as Franchisees.

As prescribed mandatory industry codes under the CCA, the Codes apply to all agreements and parties that fall within their scope. A party does not need to agree to be bound by the Codes for the obligations to apply.

The purpose of the Codes is to address the stronger bargaining position enjoyed by Franchisors¹ in their dealings with Franchisees by imposing minimum disclosure requirements on the Franchisor and minimum behavioural requirements on both the Franchisor and Franchisee. While there are a range of organisations that can facilitate dispute resolution, the Codes are intended to inculcate and normalise improved levels of transparency, behaviour and dispute resolution without the need for frequent outside intervention.

However, even when a code is successful in lifting the standards of behaviour across a sector generally, there will always be those that do not comply. While the ACCC does not become involved in the vast majority of franchise disputes, it is critical that the ACCC is able to ensure that significant and systemic instances of non-compliance are identified, investigated and appropriately penalised.

The ACCC has a sound track record over the past two decades of addressing non-compliance with the Franchising Code. This includes 33 litigated matters and 16 court enforceable undertakings. Three infringement notices have also been issued and paid following amendments to the law in 2015 that allowed the ACCC to issue infringement notices for likely breaches of the Franchising Code.

For context, in 2016/17 the ACCC overall instituted 37 court proceedings. Three of those cases, or around 8 per cent, related to franchising. This reflects the high priority the ACCC places on franchising-related complaints, which account for less than one per cent of all contacts to the ACCC.

The ACCC is currently taking court action against Ultra Tune Australia Pty Ltd (Ultra Tune) and the former national franchisor Geowash Pty Ltd (subject to Deed of Company Arrangement) (Geowash),¹ alleging breaches of the good faith obligations that were introduced into the Franchising Code in 2015, as well as other breaches of the Franchising Code and ACL. In each case the ACCC is seeking pecuniary penalties and redress for affected Franchisees.

This litigation builds on three significant enforcement outcomes in 2017:

- In November 2017 Morild Pty Ltd (trading as Pastacup) paid \$100,000 for failing to disclose that the company's cofounder and former director had also managed and been a director of two previous franchisors of the Pastacup franchise system that each became insolvent.
- In May 2017 Domino's Pizza Enterprises Ltd (Domino's) paid \$18 000 after the ACCC issued it with two infringement notices. The ACCC alleged Domino's failed to provide Franchisees with copies of its 2015/16 marketing fund statement and auditor's report within the required timeframes under the Franchising Code.
- In November 2017, West Aust Couriers Pty Ltd (trading as Fastway Couriers (Perth)), paid \$9 000 after the ACCC issued it with an infringement notice. The ACCC alleged that a disclosure document provided to a prospective Franchisee did not include details of former Franchisees that had terminated or transferred their Fastway Courier franchises. Fastway Couriers (Perth) also provided the ACCC with a court enforceable undertaking to address the ACCC's concerns that it had made false or misleading representations regarding the future earnings.

Our enforcement action is complemented by regular compliance checks to assess whether Franchisors are complying with their Code obligations. To date, the ACCC has done 97 compliance checks on Franchisors.

In addition, the ACCC engages in extensive educational and outreach activities in the franchising sector; empowering franchising participants to comply with the Code, seek further information about their rights and obligations and make use of the Codes' dispute resolution mechanisms. The ACCC funds a free online education program to assist prospective Franchisees to better understand the due diligence process. Over 16 000 people have enrolled in the program since it was released and feedback has been overwhelmingly positive.

This submission is informed by the ACCC's extensive enforcement and compliance experience in relation to the Codes. In the ACCC's view, key issues that should be considered as part of the inquiry are:

- Ensuring appropriate penalties are available for all breaches of the Codes and for non-compliance with the ACCC's section 51ADD audit power and
- Ensuring the business-to-business UCT regime is effective.

This submission also sets out specific recommendations in relation to each of the Codes and a number of technical amendments that should be considered as part of any changes to the Codes arising out of this inquiry.

Attachments A - E to this submission provide details of the scope, key obligations and the available remedies for breach of the Codes and discuss the ACCC's enforcement and compliance activities in the franchising sector.

¹ See <https://www.accc.gov.au/media-release/accc-takes-action-against-ultra-tune-under-franchising-code> and <https://www.accc.gov.au/media-release/accc-takes-action-against-geowash-car-wash-franchisor>

For completeness, the ACCC notes that there are a number of matters that regularly arise in the franchising sector that an effective enforcement, compliance and education regime cannot address, including:

Starting a new franchise business is not risk-free: Even where the Franchisor and Franchisee comply with the Codes, starting a new franchise business always carries with it the risk that it will be unsuccessful, as with all businesses. The requirement in both Codes to provide a disclosure document assists prospective Franchisees by providing them with a range of information relevant to their decision whether to enter into the agreement. However, it is essential that prospective Franchisees conduct their own due diligence before entering into an agreement. Due diligence should involve carefully reading the information provided, consulting qualified advisers and undertaking independent research, to decide whether the franchise opportunity offered is likely to be a profitable and sustainable one. The fact that a franchise business is unsustainable for whatever reason, is not evidence, in itself, of a breach of the Codes, the ACL, or the CCA. However, the ACCC understands the significant investments franchisees make and the potential impacts on their financial and personal wellbeing when the business fails.

On a day-to-day basis the relationship between the Franchisor and Franchisee is governed by the franchise agreement: By its nature, franchising is restrictive; requiring Franchisees to roll out a model established or controlled by another party (the Franchisor). For example, it is common for franchise agreements to constrain which products a Franchisee can sell, who they can source them from, their hours of operation and the standards they must meet. The Franchisor's control over day-to-day operations can be a source of tension and dispute between Franchisors and their Franchisees.

Compliance with workplace laws: The failure of some Franchisees to meet their industrial relations obligations has been widely reported. The Codes, the ACL and the CCA do not impose any obligations to comply with workplace laws. Some Franchisors have claimed that the Codes prevent them from terminating Franchisees who are purposely not complying with their workplace obligations. This is incorrect. Provided that the franchise agreement contemplates termination for non-compliance with workplace laws and the Franchisor complies with the termination procedures in the Codes², then the Codes are no obstacle. Furthermore, the Codes specify that a Franchisor need not comply with the termination procedures where a Franchisee's conduct amounts to fraud, such as falsifying records (i.e. the Franchisor is not required to provide prior notice and / or an opportunity to remedy).

²Where a Franchisee is in breach of their agreement, the Codes require that, prior to terminating the agreement, the Franchisor must: notify the Franchisee of the breach; tell them what they must do to remedy the breach; and allow a reasonable time for the Franchisee to remedy the breach. Where a Franchisee remedies their non-compliance with the agreement, the Franchisor is unable to terminate on the basis of that breach.

ACCC Recommendations

The availability and quantum of penalties

Penalties for breach of the Codes

ACCC Recommendation 1: Civil pecuniary penalties (and, thereby, infringement notices) be made available for all breaches of the Codes. The quantum of penalties available for breach of an industry Code be significantly increased to ensure that penalties are a meaningful deterrent.

Currently the ACCC can only seek civil pecuniary penalties or issue infringement notices for breaches of a limited number of Franchising Code³ provisions and no provisions of the Oil Code. The ability to seek civil pecuniary penalties and issue infringement notices is a fundamental part of the ACCC's enforcement toolkit. The lack of consequences for breaching parts of the Franchising Code and all Oil Code breaches undermines our ability to ensure compliance with the Codes.

Further, the current maximum penalty available for a breach of a civil pecuniary penalty provision in an industry code is 300 penalty units⁴ (currently \$63 000⁵). By comparison, maximum penalties available under the ACL are \$1.1 million (for companies) and the Treasury Laws Amendment (2018 Measures No. 3) Bill 2018, currently before Parliament, will increase the maximum penalty for a breach of the ACL by a corporation to the greater of: \$10 million, three times the value of the benefit obtained from the offence (where the court can determine this value), or 10 per cent of the annual turnover of the business.

The availability of infringement notices is linked to the availability of civil pecuniary penalties as the ACCC can only issue an infringement notice where the ACCC has reasonable grounds to believe that a person has breached a civil pecuniary penalty provision of the Franchising Code.⁶ Infringement notices provide a timely and cost-effective way of resolving concerns and avoiding legal proceedings. The current value of an infringement notice is 50 penalty units for a body corporate (currently \$10 500).⁷

For the Codes to be effective, the consequences of breaching the Codes must be sufficiently serious to incentivise compliance. Where penalties are too low Franchisors are likely to factor the risk of a penalty in as a cost of doing business. Where penalties are unavailable there is no incentive for a Franchisor to comply with the Codes.

Therefore, the ACCC recommends that:

- civil pecuniary penalties (and thereby infringement notices) be made available for all breaches of the Franchising Code
- civil pecuniary penalties (and thereby infringement notices) be introduced for all breaches of the Oil Code and
- the amount of civil pecuniary penalties available under the CCA for a breach of a prescribed industry code be increased to *at least* reflect the penalties currently available under the ACL.

³ Since 1 January 2015, the ACCC has been able to seek civil pecuniary penalties for breaches of certain provisions of the Franchising Code. A list of Franchising Code provisions for which civil pecuniary penalties are available is at Attachment E.

⁴ Section 51AE(2) of the CCA.

⁵ The calculation of the monetary amount of a penalty is dependent on 'penalty units' that are set out in the *Crimes Act 1914*. From 1 July 2017 the value of a penalty unit is \$210.

⁶ Section 51ACD of the CCA

⁷ Section 51ACF of the CCA

Providing for meaningful penalties for all breaches of the Codes would significantly improve our ability to enforce them and improve conduct in the sectors.

Penalties for non-compliance with the ACCC's audit power

ACCC Recommendation 2: Civil pecuniary penalties (and, thereby, infringement notices) be made available for failure to comply with notices issued under s51ADD of the CCA.

A key tool that the ACCC uses to test compliance with the Codes is our information gathering power in s51ADD of the CCA. Under s51ADD, the ACCC can issue a notice requiring a Franchisor to provide information or documents that they are required to keep, generate or publish under the Codes. Currently, if a Franchisor refuses or fails to comply with a s51ADD notice, the ACCC's only option is to apply to a court for an injunction. This is a costly and inefficient method of securing compliance and only provides a weak incentive for Franchisors to comply with a s51ADD notice.

The availability of a civil pecuniary penalty and infringement notices for failing to comply with a s51ADD notice would be significantly stronger incentive for Franchisors to comply with the notice and significantly improve the ACCC's ability to effectively monitor compliance with prescribed industry codes.

Therefore, the ACCC recommends that:

- the CCA be amended to provide for civil pecuniary penalties and infringement notices for non-compliance with s51ADD notices.

Unfair contract terms

The terms of reference for this inquiry invite comments on the impact of the ACL UCT provisions on franchising since 12 November 2016 when the UCT provisions were extended to cover business-to-business contracts, including whether changes to standard franchise agreements have resulted.

While the ACCC's industry engagement has resulted in some changes to franchise agreements, the ACCC remains concerned that the UCT regime does not appropriately protect Franchisees and other small businesses; and does not sufficiently deter Franchisors or other businesses from including UCTs in their standard form contracts.

The Explanatory Memorandum to the *Treasury Legislation Amendment (Small Business and Unfair Contract Terms) Bill 2015* recommended that a review of the legislation be undertaken within five years of the legislation coming into force⁸ and the government has since committed to a review being commenced two years after the protections came into effect on 12 November 2016.⁹ The ACCC looks forward to the opportunity to provide more detailed consideration at that time, however, our concerns are outlined briefly below.

Industry engagement during UCT transition period

In the lead-up to the business-to-business UCT law taking effect, the ACCC reviewed a sample of franchise agreements for compliance with the forthcoming laws. The franchising sector was selected for review because of the prevalence of standard form contracts, together with the fact that franchising relationships are characterised by an inherent imbalance of power between Franchisees and Franchisors.

⁸ See paragraph 3.212

⁹ See Australian Government response to the Productivity Commission Inquiry into business set-up, transfer and closure, May 2017, page 5. Available at: <https://static.treasury.gov.au/uploads/sites/1/2017/06/Final-Government-Response.pdf>.

During the review, the ACCC engaged with selected Franchisors about amending or removing problematic terms that the ACCC considered were likely to be unfair. The ACCC identified four common types of problematic terms in franchise agreements relating to:

- the right to unilaterally vary operations manuals
- liquidated damages clauses
- restraints of trade and
- termination clauses that grant a Franchisor an unreasonable power to terminate.

In response to the ACCC raising concerns, some, but not all, Franchisors amended the relevant terms.¹⁰

The ACCC continues to monitor potentially unfair terms in the franchising sector through the ACCC's section 51ADD compliance check program (discussed in **Attachment A** of this submission) and escalates instances of concerning terms for further investigation where appropriate.

Civil Pecuniary Penalties and Infringement Notices

ACCC Recommendation 3: Currently, including a UCT in a standard form contract is not illegal. The ACCC recommends making this illegal and providing for civil pecuniary penalties and infringement notices for breach of that prohibition.

UCTs can cause significant hardship for Franchisees and other small businesses. By definition, unfair contract terms go beyond what is reasonably necessary to protect a Franchisor's, or other business', legitimate commercial interests.

While s23 of the ACL allows parties to the contract or an ACL regulator to challenge a potentially unfair contract term in a court and have the term declared void, it is not a contravention of the ACL to include a UCT in a standard form contract (i.e. it is not itself prohibited). The ACCC recommends that the ACL be amended to expressly prohibit the inclusion of UCTs in a standard form consumer or small-business contract.

As including a UCT in is not illegal, the ACCC cannot seek civil pecuniary penalties when a term of a contract is declared unfair, and cannot issue infringement notices in relation to contract terms that are likely to be unfair. The fact that the only recourse is that a term of a contract could be declared void without any other penalty provides little incentive for Franchisors and other businesses to ensure that their standard form contracts do not contain UCTs.

Indeed, the ACCC effectively becomes a "compliance department" for those issuing standard form contracts. Under the current arrangements, when approached by the ACCC, companies can simply amend their UCTs and there is little that the ACCC can do to hold them to account for prior conduct.

Therefore, the ACCC recommends that:

- including a UCT in a standard form contract be made illegal under the CCA and
- civil pecuniary penalties and infringement notices be made available for breaches of that UCT prohibition.

¹⁰ For further details see Unfair terms in small business contracts: A review of selected industries, ACCC, November 2016. Available at : https://www.accc.gov.au/system/files/B2B%20UCT%20-%20Final%20-%20Unfair%20terms%20in%20small%20business%20contracts%20%20A%20review%20of%20selected%20industries_0.PDF

Making the inclusion of a UCT in a standard form contract illegal, and providing for penalties and infringement notices, would significantly increase the incentives for compliance and ensure that consumers and small business get meaningful protection.

Threshold to be considered a ‘small business’

ACCC Recommendation 4: Consideration be given to increasing the qualifying thresholds for UCT protections to ensure that they apply appropriately to small businesses.

When the unfair contract term provisions were extended to cover small businesses, the extension was limited to lower-value transactions to recognise that small businesses, while comparable to consumers in many ways, differ from consumers in that they can engage in high-value commercial transactions that are fundamental to their business and where they should undertake appropriate due diligence.¹¹ However, based on industry consultations, the thresholds in the law were expected to cover most small business transactions.¹²

In the ACCC’s experience, a number of important small business transactions are excluded from the business-to-business UCT provisions. In the franchising context, for example, we consider it is likely that the majority of authorised motor dealers fall outside the current thresholds because of the high value of the products sold and perhaps also the number of employees.

As another example, as part of the ACCC’s Dairy Inquiry¹³ we examined a number of milk processing contracts and identified some potentially unfair terms, including terms allowing retrospective changes in farmgate milk prices during a season. However, UCT laws may not apply to contracts for the supply of milk where there is a fixed volume and price for the duration of the contract, and the upfront price exceeds the relevant threshold. Given the potentially significant impact of these terms on a large number of small businesses, the ACCC considers that there is no logical reason that contracts of this nature should be excluded from the protections of the UCT legislation.

Therefore, the ACCC recommends that:

- consideration be given to increasing the threshold for the up-front value of the contract.

The ACCC will consider this issue more closely in the coming months and be in a position to provide more detail on an alternative threshold when the scheduled review of unfair contract term legislation commences.

The ACCC also has concerns with the requirement that a business employ fewer than 20 people before a contract can be considered a ‘small business contract’. The ACCC’s experience to date suggests that there are a number of businesses that manage a large volume of standard form contracts with large suppliers as part of their core work, and are in significantly weaker bargaining positions compared to those suppliers, but are not protected by the UCT provisions because they employ more than 20 people. For example, in 2017 the ACCC considered potentially unfair contract terms relating to payment in standard form contracts in the transport industry, however, many of the affected businesses we engaged with employed more than 20 people and so were not protected under the law.

¹¹ Treasury Legislation Amendment (Small business and unfair contract terms) Bill 2015, Explanatory Memorandum, paragraph 2.7. Available at: <https://www.legislation.gov.au/Details/C2015B00109/Download>

¹² Ibid, paragraph 2.20

¹³ Dairy Inquiry Final Report, ACCC, April 2018, see: https://www.accc.gov.au/system/files/1395_Dairy%20inquiry%20final%20report.pdf

- The ACCC has not yet formed a conclusive view on the appropriateness of this threshold, and will consider this issue more closely in the lead up to the review of the UCT regime.

Compulsory information gathering powers

ACCC Recommendation 5: Section 155 notices be available to allow the ACCC to obtain evidence about whether a standard form contract contains an unfair term.

In relationships of unequal bargaining power, as is inherent in the franchising relationship and is often present between other small businesses and their suppliers, the small business party often feels unable to raise concerns with their Franchisor or lodge a complaint with a regulator for fear of commercial retribution.

When parties are fearful of, or otherwise unwilling to cooperate, the ACCC can usually rely on its compulsory information gathering powers under section 155 of the CCA to ensure that we can access the information we need to investigate potentially problematic conduct.

The ACCC can only use its s155 compulsory powers to require a person or business to produce information or attend an interview where the ACCC chairperson or deputy chair person has a reason to believe that the person or business is capable of producing information relating to a matter that may constitute a breach of the CCA or ACL.

However, because including an unfair contract term in a standard form contract is not currently illegal under the CCA, the ACCC cannot use s155 to investigate whether a term is unfair and, instead, we must rely on information being provided voluntarily. In circumstances where the Franchisee or other small business is not willing to cooperate for fear of commercial retribution, it is difficult for the ACCC to effectively enforce the UCT regime.

The Final Report of the recent Review of the ACL recognised the practical challenges when a regulator is not able to collect evidence as to whether a term is unfair.

In August 2017 consumer affairs ministers agreed that ACL regulators, including the ACCC, should be allowed to use their existing powers to obtain information and evidence to determine whether a standard form contract term is unfair. Legislation was introduced to give effect to this proposal in March 2018 and it is still before Parliament.

The ACCC recommends that:

- s155 notices be available to allow the ACCC to obtain evidence about whether a standard form contract contains an unfair term.

Recommendations specific to the Franchising Code

Ability to assess financial viability and responsibility for legal costs

ACCC Recommendation 6: Amend the disclosure requirements of the Franchising Code to require Franchisors to disclose meaningful information about establishment costs and other expenses to prospective Franchisees.

A clear understanding of a business's anticipated costs assists prospective Franchisees to determine if the business is likely to be sustainable and whether they are paying the right price for it.

Under the Franchising Code, a Franchisor must provide a prospective Franchisee with a disclosure document setting out the establishment costs of the business and other anticipated recurring or one-off costs to the Franchisor, one of its associates or a third party. The Franchising Code requires Franchisors to specify the amount of the relevant costs or

provide the formula used to calculate it. If the costs cannot be easily calculated, the Franchisor can provide the likely upper and lower range of the cost.

It is not uncommon for Franchisees to raise concerns about higher than expected costs when reporting potential misconduct by their Franchisor to the ACCC. During the ACCC's compliance checks, we have seen that that some Franchisors provide very wide ranges in their cost estimates. For example, the table below provides an example of wide ranges provided by a Franchisor found in a recent compliance check.

Upper and lower limits of cost estimates

| Item | Lower limit range | Upper limit range |
|---|-------------------|-------------------|
| Construction, remodelling, leasehold improvements, decorating costs | \$5 000 | \$350 000 |
| Inventory to establish the business | \$1 000 | \$20 000 |
| Insurance | \$1 500 | \$20 000 |
| Additional funds, including working capital, required by the franchisee before operations begin | \$20 000 | \$150 000 |

The effect of this practice is that prospective Franchisees end up receiving "almost meaningless" information,¹⁴ with costs able to vary by hundreds of thousands of dollars. While best practice would suggest Franchisors provide further context as to this variance, they are not required to and often choose not to do so.

The ACCC recommends that the Franchising Code be amended to:

- ensure Franchisors disclose meaningful information about establishment costs and other anticipated recurring or one-off costs

This information could take the form of information about the facts and assumptions that underlie cost ranges provided in the disclosure document and the average / median costs based on other Franchisees' experiences.

Disclosure of the facts and assumptions underlying Franchisors claims and estimates based on other Franchisee's experiences would provide more meaningful information to prospective Franchisees. This would enable prospective Franchisees to more accurately estimate the total costs of the business.

Requiring Franchisors to provide more meaningful information as to costs will assist prospective Franchisees to more accurately budget and forecast the costs of the business. Under the ACL, Franchisors that do not have a reasonable basis for the claims they make as part of their disclosure document risk breaching the key provisions against misleading or deceptive conduct. Accordingly, the ACCC considers that it should not be overly burdensome to require Franchisors to provide this additional information to prospective Franchisees as they should already be taking into account such information when preparing their disclosure documents.

Purchasing an existing franchised business

ACCC Recommendation 7: Amend the Franchising Code to require Franchisors to disclose certain financial information where a prospective Franchisee is considering taking over an existing business.

Currently, if a territory or site to be franchised has, in the previous 10 years, been operated by another Franchisee, the Franchisor must provide the prospective Franchisee with the circumstances in which the previous franchisee ceased to operate. The Franchisor is currently not required to provide details about the profitability of the former franchise.

The Oil Code contains a similar obligation to disclose site history (albeit limited to the previous three years). However, the Oil Code also requires the Franchisor to disclose:

- details of the profitability of the business and
- any limitations on the basis and reliability of the profitability calculation provided.

In the ACCC's view, the ability of a prospective Franchisee to make an informed decision about whether to take over an existing / previously franchised business would be improved by requiring Franchisors to provide information similar to that that is required by the Oil Code. This could take the form of profit and loss statements and balance sheets for the franchise business.

Therefore, the ACCC recommends that:

- The Franchising Code be amended to require Franchisors to disclose certain financial information where a prospective Franchisee is contemplating purchasing an existing or previously franchised business.

Passing on Franchisors' legal costs

ACCC Recommendation 8: Amend the Franchising Code to prohibit Franchisors from passing on to the prospective Franchisee the legal costs of preparing, negotiating and executing documents.

Many Franchisors include a term in their agreements that require the prospective Franchisee to reimburse the Franchisor for the Franchisor's costs for preparing, negotiating and executing the agreement.

The ACCC considers that the ability for Franchisors to pass on their initial legal costs to a prospective Franchisee may disincentivise many prospective Franchisees from:

- seeking their own independent advice
- attempting to negotiate the terms of the arrangement, since doing so will increase the Franchisor's costs of negotiating and drafting any changes.

Therefore, the ACCC recommends that:

- The Franchising Code be amended to prohibit Franchisors from passing on to the prospective Franchisee the costs of preparing, negotiating and executing the agreement or other documents.

Recommendations relating to the Oil Code

Ability to monitor compliance using the section 51ADD power

ACCC Recommendation 9: Amend the Oil Code to include a record-keeping obligation and to require that, where a Franchisor is required to give notice to a Franchisee the notice must be in writing.

The Oil Code currently requires a Franchisor to give notice to a Franchisee in a range of scenarios, including:

- where a Franchisor proposes to terminate an agreement due to a breach of that agreement by the Franchisee¹⁵
- where a Franchisor proposes to terminate an agreement with an initial non-refundable amount payable by the Franchisee of less than \$20 000¹⁶
- when informing a Franchisee of their rights during an agreed early termination¹⁷ and
- when disclosing materially relevant facts to a Franchisee e.g. a change in the majority ownership of the franchisor, or a judgement made in a criminal or civil proceeding.¹⁸

However, the Franchisor is not required to keep, generate or publish these notices. Therefore, the ACCC is unable to use its section 51ADD compliance check power to determine whether the Franchisor has complied with these obligations.

Further, the Oil Code does not currently require Franchisors to keep the following documents:

- statements provided to the Franchisor by prospective Franchisees and
- documents / information that the Franchisor relies upon to make a claims in its disclosure document.

While a Franchisor is, in practice, likely to keep these documents, at present the ACCC cannot compel the Franchisor to provide copies of these documents under a s51ADD compliance check.

The ACCC raised similar concerns during the 2013 Wein Review, which led to the introduction of a record-keeping obligation in the Franchising Code.¹⁹ Under the Franchising Code, Franchisors must keep documents for six years.

Therefore, the ACCC recommends the Oil Code be amended to:

- require the Franchisor to provide notice to the Franchisee in writing and
- include a record-keeping obligation as specified under the Franchising Code.

¹⁵ Clause 35(2) Oil Code

¹⁶ Clause 37(2) Oil Code

¹⁷ Clause 38(2) Oil Code

¹⁸ Clause 29 Oil Code

¹⁹ Clause 19 Franchising Code.

Ensure the Oil Code is effective

ACCC Recommendation 10: Amend the Oil Code's fuel-reselling provisions to incorporate relevant rights and obligations contained in the updated Franchising Code, including a general obligation of good faith dealing.

At its commencement, the Oil Code was intended to build upon and strengthen many provisions of the Franchising Code.²⁰ For example, the Oil Code contains similar provisions regarding disclosure, marketing funds and termination to the old 1998 Franchising Code. However, the Franchising Code has been reviewed and amended several times since 1998. The Oil Code has not been similarly amended and has therefore fallen behind the Franchising Code.

In our submission to the 2015 review of the Oil Code, the ACCC noted that the updated Franchising Code introduced significant changes to the rights and responsibilities of Franchisors and (current or prospective) Franchisees.

At the time the ACCC recommended that consideration be given to introducing increased disclosure obligations and a good faith obligation into the Oil Code similar to the updated Franchising Code. Such amendments were not made to the updated Oil Code. The outcome is the existence of two Codes that govern similar relationships, but impose different rights and obligations on the parties involved.

Whilst industry codes must of course reflect the unique commercial characteristics of the industries they regulate, the ACCC considers that the Oil Code would benefit from amendments to reflect the updated provisions in the Franchising Code. Such amendments could help to ensure the Oil Code is operating effectively, achieving its stated purpose and making sure participants in the industry follow best practice principles.²¹

Therefore, the ACCC recommends that:

- the Oil Code be amended to include provisions similar to the Franchising Code, including:
 - requiring Franchisors to provide prospective Franchisees with an information statement outlining key information about franchising as soon as practicable after the prospective franchisee expresses an interest in acquiring a franchised business.²²
 - requiring Franchisors to provide prospective Franchisees with a copy of the franchise agreement in its final form at least 14 days before the prospective Franchisee makes a non-refundable payment or enters into an agreement (or an agreement to enter an agreement).²³
 - restricting how Franchisors may deal with Franchisees' marketing fees.²⁴
 - prohibiting Franchisors from requiring Franchisees to undertake significant capital expenditure during the term of the agreement.²⁵

²⁰ <https://www.legislation.gov.au/Details/F2006L03714/Explanatory%20Statement/Text>

²¹ The Future of Franchising statement, April 2014, www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/Franchising-Code

²² Clause 11 Franchising Code.

²³ Clause 9(1) Franchising Code.

²⁴ Clause 31 Franchising Code.

²⁵ Clause 30 Franchising Code.

Good faith dealing

The updated Franchising Code,²⁶ Food & Grocery Code,²⁷ Wheat Port Code²⁸ and Horticulture Code²⁹ all include a general obligation for parties to act in good faith. The Oil Code currently only requires parties to act in good faith when:

- mediating a dispute³⁰
- making changes to the terms and conditions of a renewed franchise agreement.³¹

Including a general obligation of good faith would encourage greater fairness in dealings between Franchisors and Franchisees. The ACCC can see no legitimate reason why Oil Code Franchisors and Franchisees should not be afforded a similar level of protection or bound by a similar obligation in their dealings with one another as other Franchisors and Franchisees. Its inclusion would also bring the Oil Code into alignment with the other industry codes.

The ACCC recommends that:

- The Oil Code be amended to include a general obligation of good faith.

Other considerations

Consolidation of mediation services

The Franchising Code specifically provides for the appointment of a mediation advisor. Where a dispute arises and the parties cannot agree on a mediator, the Franchising Code provides that either party may ask the Office of the Franchising Mediation Adviser (OFMA) to appoint a mediator. Currently, OFMA maintains a panel of qualified mediators in each state who can assist the parties for a capped fee. The Oil Code also provides for a separate Dispute Resolution Adviser (DRA). In addition to maintaining a register of suitably qualified mediators, the DRA can also make non-binding determinations in relation to disputes.

The ACCC considers that there is duplication in the current mediation arrangements and consideration should be given to consolidating mediation advisory services to a single entity. For example these roles could be consolidated into the Australian Small Business and Family Enterprise Ombudsman's office.

²⁶ Clause 6 Franchising Code

²⁷ Clause 28 *Competition and Consumer (Industry Codes—Food and Grocery) Regulation 2015*.

²⁸ Clause 6 *Competition and Consumer (Industry Code—Port Terminal Access (Bulk Wheat)) Regulation 2014*.

²⁹ Clause 8 *Competition and Consumer (Industry Codes—Horticulture) Regulations 2017*.

³⁰ Clause 45 Oil Code

³¹ Clause 32(8) Oil Code

Technical amendments

The ACCC notes that the findings of this inquiry may be used to inform further changes to the Franchising Code and / or the Oil Code. The ACCC recommends that the following technical amendments to improve the clarity or operation of the Codes.

| Reference | Issue | Suggestions |
|---|---|--|
| <p>Disclosure of former franchisees' contact details</p> <p>Item 6.5 of Annexure 1, Franchising Code</p> <p>Item 6.4 of Annexure 1, Oil Code</p> | <p>Franchisors are currently required to disclose contact details for certain former franchisees that have left the system. This enables prospective franchisees to contact them to obtain further information about the franchisor and the system. It appears to be becoming increasingly common for Franchisors to only disclose the former franchised business's phone number, email address or physical address as the former franchisee's 'contact details'. This has the practical effect that prospective Franchisees are unable to speak to former Franchisees about the Franchisor and system.</p> | <p>Amend the Codes to make it clear that franchised business details are not a substitute for the former franchisee's actual contact details.</p> |
| <p>Disclosure of third party payments under the Oil Code</p> <p>Item 13 of Annexure 1 and item 7 of Annexure 2</p> | <p>The Oil Code does not require Franchisors to disclose to prospective Franchisees third party payments that are reasonably foreseeable or within the Franchisor's knowledge. This is likely to make it difficult for a prospective Franchisee to assess the ongoing costs of the business.</p> | <p>Require Franchisors under the Oil Code to disclose third party payments that a Franchisee will be expected to make.</p> |
| <p>Marketing funds and marketing fees</p> <p>Clauses 15 and 31 Franchising Code</p> | <p>There are drafting differences between the marketing fund provisions of the Franchising Code; clause 15 refers to a requirement to contribute to a 'marketing fund' and clause 31 refers to 'marketing and advertising fees'. These language inconsistencies have been used by some Franchisors who collect regular payments from Franchisees for marketing expenditure incurred to suggest they are not required to comply with the clause 15 reporting obligations because they do not operate a 'marketing fund' per se.</p> | <p>The drafting of clauses 15 and 31 of the Franchising Code should be amended to make it clear that both apply where a Franchisee is required to make regular payments to the Franchisor to cover marketing or advertising activities.</p> <p>Similar changes should be considered for the Oil Code as necessary.</p> |

| | | |
|--|--|--|
| <p>Time period to commence mediation</p> <p>Franchising Code and Oil Code</p> | <p>Both Codes establish a process for referring a dispute to a mediator. However, the Codes do not specify a time period within which mediation must commence. Whilst timing is dependent on factors such as the availability of the appointed mediator, delays in the commencement of mediation have the potential to cause real hardship for the affected parties.</p> <p>Currently, parties can conceivably delay mediation by consistently claiming they are unavailable to attend on certain dates. While the obligation to mediate in good faith is relevant in the event a party vexatiously seeks to delay mediation, this provides no recourse at the time for the affected party who is seeking to address the cause of their initial dispute.</p> | <p>Amend the Codes to require that mediation commence within a specified period once a mediator has been appointed.</p> |
| <p>Multi-party mediation</p> <p>Franchising Code</p> | <p>The Franchising Code does not expressly state that mediators may undertake multi-franchisee mediation when disputes of a similar nature arise within a franchise system. The ACCC is aware of Franchisors refusing to attend multi-party mediation on this basis and insisting on addressing disputes on an individual basis. Multi-party mediation has a number of benefits, such as:</p> <ul style="list-style-type: none"> • assisting to shift the imbalance of bargaining power that exists between the Franchisor and Franchisee when resolving disputes • creating a more efficient process and use of resources. | <p>Amend the Franchising Code to allow a mediator to undertake multi-franchisee mediations when disputes with similar issues arise.</p> <p>The ACCC notes that the application of any such provision would need to be considered in conjunction with the other requirements under the Franchising Code e.g. that parties not be compelled to attend mediation in states and territories other than where their franchised business is based.</p> |
| <p>Termination in special circumstances</p> <p>Clause 36(1) Oil Code</p> | <p>There are different interpretations within the fuel-reselling industry as to whether clause 36 of the Oil Code creates a statutory right of termination. When the Franchising Code was updated in 2015, an express statement was inserted to make it clear that no right of unilateral termination for special circumstances exists in the Code and that for a right of unilateral termination to exist it must be contained within the agreement.</p> | <p>Amend the Oil Code to make it clear that Franchisors can only terminate in the special circumstances listed in clause 36(1) if this is expressly provided for in the franchise agreement.</p> |

Attachment A - Enforcement and compliance activities

Contacts to the ACCC

The ACCC has received 2466 contacts relating to the Franchising Code since 1 January 2015.³² Contacts include both enquiries relating to the Franchising Code and reports about potential misconduct under the Franchising Code. In the same time period, the ACCC received 20 contacts relating to the Oil Code.

On average, the ACCC receives over 264 000 contacts per year. Of those, about 14 000 relate to small business matters generally. These contacts are triaged and may go through a series of increasingly intensive investigations.

An Initial Investigation is the first stage of a detailed complaint assessment. The most serious matters are escalated to an In-depth Investigation while others are resolved administratively. The remainder of contacts are recorded in the ACCC's database so the ACCC can analyse the data to establish complaint trends, identify issues and develop compliance responses.

The table below shows the total number of contacts each year recorded as relating to the Franchising Code and, of those contacts, the number of cases that ended at each investigative stage.

| Franchising Code contacts | | | |
|---------------------------|----------------|-----------------------|------------------------|
| Year | Total contacts | Initial Investigation | In-depth Investigation |
| 2015 | 1028 | 6 | 4 |
| 2016 | 655 | 11 | 5 |
| 2017 | 608 | 6* | 5* |
| 2018 so far | 175 | 3* | 0 |
| Total | 2466 | 26 | 14 |

* Figure includes some matters that are ongoing as of May 2018 and may be escalated further.

ACCC approach to compliance and enforcement

The ACCC does not seek to resolve individual disputes. Many of the franchising business-to-business matters raised with the ACCC are more effectively dealt with under the Codes' dispute resolution procedures, or through the services provided by state fair trading agencies, the Australian Small Business and Family Enterprise ombudsman (ASBFEO) or by state Small Business Commissioners. Where this is the case, the ACCC will refer the complainant to the appropriate agency or service.

Instead, the ACCC focusses on addressing those circumstances that will, or have the potential to, harm the competitive process or result in widespread consumer or small business detriment. That said, the ACCC has a strong enforcement record in the franchising sector.

³² To 19 April 2018.

ACCC enforcement action

Since the Franchising Code was first introduced 20 years ago, the ACCC has litigated 33 franchising-related matters. In 2017, the ACCC took action in relation to a number of alleged breaches of the Franchising Code. These are outlined in further detail below.

The ACCC has not litigated any cases under the Oil Code. As indicated above, the ACCC receives very few reports relating to potential misconduct under the Oil Code. In addition, if the ACCC was to receive evidence of a potential breach of the Oil Code, the matter is more likely to be resolved administratively as the ACCC cannot seek a civil pecuniary penalty under the Oil Code or issue infringement notices.

The ACCC has obtained three recent enforcement outcomes in relation to the updated Franchising Code:

1. Pastacup

In November 2017, the Federal Court ordered Morild Pty Ltd (trading as Pastacup), and its former director to pay penalties of \$100 000 and \$50 000 respectively for breaches of the Franchising Code. These were the first court-issued civil pecuniary penalties for breaches of the Franchising Code.

The Court found that Morild Pty Ltd failed to provide a Franchising Code-compliant disclosure document, because it did not disclose the former director's previous directorship of the insolvent Pastacup Franchisors.

Media release: [Pastacup to pay \\$100,000 for breaches of new Franchising Code](#)

2. Domino's Pizza

On 4 May 2017, Domino's Pizza Enterprises Ltd paid \$18 000 after the ACCC issued it with two infringement notices. The ACCC alleged that Domino's had failed to provide Franchisees with copies of its 2015/16 marketing fund statement and auditor's report within the required timeframes under the Franchising Code.

Domino's was the first company to pay an infringement notice in relation to alleged non-compliance with the Franchising Code since infringement notices were made available for alleged breaches of the Franchising Code in 2015.

Media release: [Domino's pays penalty for alleged Franchising Code breach](#)

3. Fastway Couriers

In November 2017, West Aust Couriers Pty Ltd (trading as Fastway Couriers (Perth)), paid \$9 000 after the ACCC issued it with an infringement notice.

The ACCC alleged that Fastway Couriers (Perth) breached the Franchising Code by providing a disclosure document to a prospective Franchisee that did not include details of former Franchisees that had terminated or transferred their Fastway Courier franchises.

Fastway Couriers (Perth) also provided a court enforceable undertaking to address the ACCC's concerns that it had made false or misleading representations regarding the future earnings of Franchisees by advertising an "income guarantee" of \$1 500 per week for 30 weeks. The ACCC was concerned that prospective Franchisees would understand this representation to be the likely income they could expect to earn at the end of the stipulated period in circumstances where this was not the case.

The Franchisor undertook to provide actual earnings information to prospective Franchisees, and not to describe the offered financial support as an “income guarantee” in future marketing of its courier franchises.

Media release: [Fastway Couriers \(Perth\) pays penalty for alleged Franchising Code breach](#)

Current court action

1. Ultra Tune

In May 2017, the ACCC instituted proceedings against Ultra Tune Australia Pty Ltd for alleged contraventions of the Franchising Code and the ACL. Ultra Tune is a Melbourne-based Franchisor of a vehicle repair system with over 200 motor repair franchises throughout the ACT, NSW, Queensland, Victoria and Western Australia.

The ACCC alleges that Ultra Tune breached the ACL by making false or misleading representations to prospective Franchisees and breached the Franchising Code by failing to:

- act in good faith by applying undue pressure to pay a deposit, refusing to release critical information about a franchise site and making false representations about that site and the refundable nature of the deposit
- provide a disclosure document, franchise agreement (in executable form) and a copy of the Franchising Code to the prospective Franchisees before accepting a non-refundable payment
- prepare, audit and provide marketing fund statements to Franchisees
- update its disclosure document, or provide copies of it, within the time periods set in the Franchising Code.

This matter is the first court action initiated by the ACCC alleging that a Franchisor has breached their obligation to act in good faith.

The matter is still before the court. The ACCC is seeking pecuniary penalties and other orders including a repayment of the prospective Franchisee’s deposit amount.

Media release: [ACCC takes action against Ultra Tune under Franchising Code](#)

2. Geowash

In May 2017 the ACCC instituted proceedings against Geowash, a former national franchisor that marketed and sold car wash franchises across Australia between 2013 and 2016.

The ACCC alleges that Geowash:

- breached the ACL by making false or misleading representations about the revenue and profit Franchisees could earn, and that Geowash had commercial affiliations with certain major brands when it did not
- breached its good faith obligations under the Franchising Code and engaged in unconscionable conduct by directing a substantial portion of Franchisee funds for purposes not permitted under the franchise agreement and not disclosed to Franchisees, including payment of commissions to the director and national franchising manager.

The ACCC also alleges that Geowash’s director and national franchising manager engaged in and were knowingly concerned in the conduct.

This matter is still before the court. The ACCC is seeking pecuniary penalties, disqualification orders, and orders that Geowash's director and national franchising manager compensate affected franchisees for losses suffered from the conduct.

Media release: [ACCC takes action against Geowash car wash franchisor](#)

ACCC industry code compliance checks

The ACCC has the power under section 51ADD of the CCA to randomly audit traders for compliance with prescribed industry codes. Using this power, the ACCC can require a corporation to produce any information or documents it is required to keep, generate or publish under a prescribed industry code within 21 days.

Use of the s51ADD power

Unlike the information gathering powers under s155 of the CCA,³³ the ACCC does not require a 'reason to believe' that a corporation may have breached a prescribed code before issuing a s51ADD notice. That said, the ACCC takes a considered approach when selecting traders for audit and targets traders that fit at least one of the following:

- traders with a significant number of Code-related reports made against them
- traders with a history of non-compliance (e.g. a trader against whom the ACCC has taken court action or who has provided the ACCC with a s87B undertaking)
- traders from industries that appear to generate a disproportionate volume of reports and/or
- traders identified as potentially not complying with the applicable Code or the CCA through intelligence received from franchisees, industry associations, other Government agencies, or members of one or more of the ACCC's consultative committees.

Since the ACCC was given the power to conduct industry code compliance checks, the ACCC has issued 133 notices³⁴, 97 of which related to the Franchising Code. Compliance issues have been found in approximately half of the franchising compliance checks.

The ACCC considers each instance of potential non-compliance on a case-by-case basis taking account of the ACCC's Compliance and Enforcement Policy³⁵ and factors such as the alleged contravention(s), the business involved and harm to Franchisees. A summary of the outcomes of the 97 Franchising Code-related compliance checks undertaken is set out in the below table:

³³ Section 155 of the CCA is the ACCC's most widely used mandatory information-gathering power. The ACCC can issue a notice requiring a person to provide information or documents or to give evidence if the ACCC, its chair or deputy chairs have reason to believe that person is capable of providing information, documents or evidence about a matter that constitutes, or may constitute, a contravention of the CCA.

³⁴ Section 51ADD notices have been issued under the Franchising Code, Horticulture Code and the Food and Grocery Code.

³⁵ www.accc.gov.au/about-us/australian-competition-consumer-commission/compliance-enforcement-policy-priorities

| Outcome of Franchising Code-related compliance check | Number |
|---|-----------|
| Compliant | 45 |
| Warning letter sent | 25 |
| Concerns resolved during course of audit (e.g. trader corrected issues or undertook to review practices to ensure compliance going forward) | 13 |
| Discontinued (due to insolvency, liquidation or traders falling outside the scope of the Franchising Code) | 8 |
| Remain under assessment | 6 |
| Total | 97 |

In addition to improving individual traders' compliance with their applicable Code, the ACCC uses the information gathered from compliance checks to identify common issues and opportunities to provide general industry guidance.

Common issues identified during the compliance check program include:

- missing, incomplete or insufficient information in the disclosure document
- no former Franchisee contact details provided or the contact details provided relate to the former franchised business (see p15)
- incorrect form, order or numbering of the disclosure document
- possible third line forcing³⁶
- insufficient detail in the marketing fund statement to provide meaningful information to Franchisees
- marketing fund statement not audited within four months of the end of the Franchisor's financial year.

The ACCC will issue further s51ADD notices to Franchisors in the June 2018 quarter.

ACCC education and engagement activities

The ACCC seeks to educate franchise participants and small businesses about their rights and obligations under the Codes and the CCA more broadly. The ACCC has a Small Business and Industry Codes team tasked with developing resources and information to educate and provide guidance to Franchisees, Franchisors and other small business operators.

Available resources

The ACCC's website provides information and educational resources including webpages on the Codes (www.accc.gov.au/industrycodes). The ACCC's key franchising publications are also available on our website:

- [Franchisor Compliance Manual](#)
- [Franchisee Manual](#)
- [Franchising: what you need to know factsheet](#).

Every six months the ACCC publishes a *Small Business in Focus* report to share information on the latest developments and outcomes related to franchising, including recent

³⁶ Up until 6 November 2017, engaging in third line forcing (a form of exclusive dealing) was a per-se breach of the CCA. A franchisor who wished to engage in third line forcing could lodge a 'notification' with the ACCC, which provided it with protection from legal action under the CCA. Third line forcing will now only breach the CCA where the conduct has the effect of substantially lessening competition in the relevant market.

enforcement action, and new resources and tools. The report also includes data on reports and enquiries the ACCC has received. The latest report is at **Attachment F**.

The ACCC also has free email subscription services for Code-related material which the ACCC uses to distribute updates about relevant enforcement action, new guidance material, events, changes to the law and best practice tips for compliance with the CCA. As of 16 April 2018, there were almost 3 000 subscribers to the ACCC's Franchising Information Network and over 600 subscribers to the Oil Code Information Network. In 2017, the ACCC sent over 30 emails to the Franchising Information Network and one email to the Oil Code Information Network about the updated Oil Code.

Bulletins for the ACCC's Franchising Information Network are informed by the ACCC's enforcement and compliance activities. For example, in light of ongoing compliance issues in relation to marketing funds, the ACCC sent a series of bulletins in 2017 outlining what Franchisors must do to comply with their end of financial year obligations under the Franchising Code.

The ACCC also has a general small business subscription network with over 7 200 subscribers. In 2017, the ACCC sent 38 emails to this network.

Since 2010, the ACCC has funded an online franchising pre-entry education program. The free program is delivered by FranchiseED³⁷ and consists of five modules covering a range of topics, including:

- advantages and disadvantages of franchising
- the disclosure document
- fees and royalties
- site selection
- intellectual property, and
- questions to ask a Franchisor.

The program assists prospective Franchisees to better understand the due diligence process and supports the ACCC's objective of encouraging compliance with the law. To date, over 16 000 people have enrolled in the program and feedback from participants has been overwhelmingly positive.

Liaison activities

The ACCC has staff in all capital cities and Townsville, who participate in events and engagement activities to disseminate key information to Franchisees, Franchisors, other small business operators and their professional advisors. For example, the ACCC has attended:

- Franchising and business opportunities expo³⁸
- CPA Australia's 2018 small business roadshow
- Legalwise's 2017 'Franchising: developments, debates and disputes' seminar
- Franchising Council of Australia's annual franchising legal symposium.

The ACCC has a Small Business and Franchising Consultative Committee, which meets at least twice a year to discuss competition and consumer law concerns related to the small

³⁷ Up until February 2018, the program was delivered by Griffith University's Asia-Pacific Centre for Franchising Excellence.

³⁸ In 2018, the ACCC will participate in events in Sydney and Melbourne. In previous years, the ACCC has also participated in events in Brisbane and Perth.

business and franchising sectors, emerging issues or market developments and relevant activities undertaken by the ACCC. The Committee is made up of 17 industry associations, five academics, four business advisers and three legal advisers.

The ACCC has encouraged Committee members to make submissions to this inquiry. Matters relevant to the inquiry were discussed at the Committee meeting on 27 April 2018.

At the meeting, a number of Committee members raised concerns about:

- Prospective Franchisees not undertaking due diligence activities, including obtaining professional advice
- Quality of information provided to prospective Franchisees
- Insufficient detail provided to Franchisees about how marketing fees are used and
- Franchise models where the margin is likely to be insufficient for the business to be profitable.

The ACCC meets regularly with the ASBFEO, state Small Business Commissioners from Western Australia, South Australia, New South Wales and Victoria, as well as the Queensland Small Business Champion, to discuss contacts received, franchising matters, and new or proposed laws that will impact on small businesses.

Attachment B – Scope of the Codes

Franchising Code

The Franchising Code imposes one set of obligations on all franchise agreements entered into, renewed, extended or transferred on or after 1 October 1998. A small number of Franchising Code provisions do not apply to franchise agreements entered into prior to 1 January 2015, the date on which the updated Franchising Code came into effect. However, franchise agreements entered into before 1 January 2015 become subject to the entire Franchising Code if they are renewed, transferred or varied in any way on or after this date.

An agreement (either written, verbal or implied) is a **franchise agreement** for the purposes of the Franchising Code if it meets the following conditions:

- one party (Franchisor) has granted to another (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);
- the operation of the business is substantially or materially associated with a trademark, advertising or commercial symbol that is owned, used, licensed or specified by the Franchisor (or its associate), and;
- the Franchisee is required to pay, or has agreed to pay, a fee to the Franchisor (or its associate) before starting or continuing the business, which may be:
 - an initial capital investment fee
 - a payment for goods or services
 - a fee based on a percentage of gross or net income; or
 - a training fee or training school fee.³⁹

The Franchising Code does not apply to a franchise agreement where another industry code, such as the Oil Code, applies.

Oil Code

The Oil Code applies to fuel re-selling agreements, whether they be new agreements or transfers, extensions or renewals.

The definition of a **fuel re-selling agreement** in the Oil Code largely mirrors the definition of a franchise agreement under the Franchising Code. However, some fuel re-selling agreements, for example, some commission agent agreements, do not satisfy the criteria of a franchise agreement under the Franchising Code.

³⁹ Clause 5(1)(d)(v) – (viii) of the Franchising Code sets out a number of payments that are excluded when determining whether an agreement is a 'franchise agreement'.

Attachment C - Key obligations under the Codes

Key obligations under the Codes are set out in the table below. A detailed comparison of the Codes is on the following pages.

| | Franchising Code | Oil Code |
|---|---|--|
| Pre-entry disclosure | <ul style="list-style-type: none"> ✓ information statement ✓ disclosure document ✓ copy of the Franchising Code ✓ copy of the franchise agreement in its final form | <ul style="list-style-type: none"> ✓ disclosure document (long form or short form, depending on duration of the agreement) ✓ copy of the Oil Code |
| Minimum duration for franchise agreement | No | Yes – 5 years (subject to exceptions) |
| Cooling-off period | Yes | Yes |
| General obligation for parties to act in good faith | Yes | No - Obligation of good faith limited to 1) mediating a dispute and 2) making changes to the terms and conditions of a renewed franchise agreement |
| Record keeping obligation | Yes | No |
| Prohibition against significant capital expenditure | Yes | No |
| Prohibition on general release from liability | Yes | Yes |
| Prohibition against waivers clause | Yes | No |
| Marketing fund provisions | Yes - Annual financial statement must be prepared within <i>four months</i> of end of financial year. Copy must be provided to Franchisees <i>within 30 days of preparation</i> | Yes - Annual financial statement must be prepared within <i>three months</i> of end of financial year. Copy only has to be provided to a Franchisee <i>if they request it</i> (once requested, Franchisor has 30 days to comply) |
| Requirement to audit annual financial statement | Yes – unless 75% of contributing Franchisees vote not to within <i>three months</i> of end of financial year | Yes – unless 75% of contributing Franchisees vote not to (no timeframe specified for vote to be conducted) |
| Availability of mediation | Yes - mediation can be initiated if dispute remains unresolved after three weeks | Yes - mediation can be initiated at any time |
| Parties must pay own mediation costs | Yes | Yes |
| Franchisor required to pay proportion of costs relation to termination | No | Yes - for agreed terminations |
| Financial penalties available for breaches | Yes – 24 civil pecuniary penalty provisions (Attachment E) | No |

Obligations common to both of the Codes

Pre-entry rights - disclosure and cooling off

Both Codes require Franchisors to disclose certain information, and provide specific documents to prospective Franchisees and current Franchisees that propose to renew or extend an agreement. This information is intended to assist the Franchisee or prospective Franchisee to make an informed decision about whether to enter, renew or extend an agreement.

A Franchisor's disclosure obligations vary depending on whether the Franchisee is entering into an agreement for the first time, or renewing or extending an existing agreement.

The documents that must be provided to prospective Franchisees differ between the Codes. Under the Franchising Code, a Franchisor must provide:

- an information statement on the risks and rewards of franchising⁴⁰
- copy of the Franchising Code⁴¹
- a disclosure document⁴² and
- a copy of the franchise agreement in its final form.⁴³

By contrast, the Oil Code only requires the Franchisor to provide the disclosure document and a copy of the Oil Code.⁴⁴

A prospective Franchisee is entitled to a cooling-off period of seven days after entering into a new agreement or making any payment under the agreement, whichever occurs earlier.⁴⁵ The seven day cooling-off period does not apply to transfers, renewals or extensions of an existing agreement.⁴⁶

If a Franchisee terminates the agreement within the cooling-off period, a Franchisor must fully refund all payments made by the Franchisee under the agreement within 14 days.⁴⁷ The Franchisor may deduct reasonable expenses from the amount to be refunded if the expenses or their method of calculation have been set out in the agreement.⁴⁸

Rights and obligations during the agreement

Marketing fund financial statements

If an agreement requires a Franchisee to pay money into a marketing or cooperative fund, the Franchisor must prepare an annual financial statement for the fund.⁴⁹ The annual financial statement must set out meaningful information about sources of income and items of expenditure.⁵⁰

The annual financial statement must be audited by a registered company auditor, unless 75 per cent of the Franchisees in Australia that contribute to the fund vote not to audit the

⁴⁰ Clause 11 Franchising Code

⁴¹ Clause 9(1)(a) and 9(2) Franchising Code

⁴² Clause 9(1)(b) and 9(2) Franchising Code

⁴³ Clause 9(1)(c) and 9(2) Franchising Code

⁴⁴ Clause 19 Oil Code

⁴⁵ Clause 26(1) Franchising Code, Clause 24(1) Oil Code

⁴⁶ Clause 26(2) Franchising Code, Clause 24(2) Oil Code

⁴⁷ Clause 26(3) Franchising Code, Clause 24(3) Oil Code

⁴⁸ Clause 26(4) Franchising Code, Clause 24(4) Oil Code

⁴⁹ Clause 15(1)(a) Franchising Code, Clause 28(1)(a) Oil Code

⁵⁰ Clause 15(1)(a) and (b) Franchising Code, Clause 28(1)(a) Oil Code

statement.⁵¹ Under the Franchising Code, the agreement not to audit must be made annually within three months of the end of the financial year.⁵² No such time period is specified in the Oil Code.

The annual financial statement and auditor's report (if one is required) must be prepared within four months of the end of the financial year under the Franchising Code⁵³ and within three months of the end of the financial year under the Oil Code.⁵⁴

While both Codes require Franchisors to prepare these documents, the Codes impose different obligations as to what a Franchisor must do with them. Under the Oil Code, a Franchisor must give a copy of the annual financial statement to a Franchisee within 30 days of a Franchisee requesting it.⁵⁵ There is no obligation to provide a copy of the auditor's report. By contrast, the Franchising Code states that the annual financial statement and auditor's report must be provided to Franchisees within 30 days of their preparation.⁵⁶

General releases

An agreement must not require a Franchisee to sign a general release of the Franchisor from liability towards the Franchisee.⁵⁷

Transfer

Both Codes require a Franchisee that wants to transfer an agreement to request the Franchisor's consent to the transfer in writing.⁵⁸ A Franchisor must not unreasonably withhold their consent.⁵⁹

Both Codes provide a non-exhaustive list of circumstances in which it would be reasonable for a Franchisor to withhold consent to a transfer.⁶⁰ These include a range of issues with the proposed transferee, the Franchisee owing monies to the Franchisor and the Franchisee being in breach of the agreement and failing to remedy the breach.

Consent is assumed to be given by the Franchisor after 42 days unless the Franchisor advises the Franchisee, in writing, that they do not consent.⁶¹

Termination of the agreement

The Codes provide processes for a Franchisor to follow if they propose to terminate an agreement where:

- there is a breach of the agreement by the Franchisee⁶²
- the Franchisee is not in breach of the agreement⁶³ or
- certain special circumstances apply.⁶⁴

⁵¹ Clause 15(2)(a) Franchising Code, Clause 28(2) Oil Code

⁵² Clause 15(2)(a) Franchising Code

⁵³ Clause 15(1)(a) Franchising Code

⁵⁴ Clause 28(1)(a) Oil Code

⁵⁵ Clause 28(1)(c) Oil Code

⁵⁶ Clause 15(1)(d) Franchising Code

⁵⁷ Clause 20(1)(a) Franchising Code, Clause 27(1) Oil Code

⁵⁸ Clause 24(1) Franchising Code, Clause 34(1) Oil Code

⁵⁹ Clause 24(2) Franchising Code, Clause 34(2) Oil Code

⁶⁰ Clause 25(3) Franchising Code, Clause 34(3) Oil Code

⁶¹ Clause 25(4) Franchising Code, Clause 34(4) Oil Code

⁶² Clause 27 Franchising Code, Clause 35 Oil Code

⁶³ Clause 28 Franchising Code, Clauses 37 and 38 Oil Code

⁶⁴ Clause 29 Franchising Code, Clause 36 Oil Code

Dispute resolution mechanisms

Both Codes are intended to promote the cost-effective and timely resolution of disputes. They both provide for mediation as the primary code-mandated process for resolving disputes. There are many similar provisions governing how mediation must be conducted under both Codes.

The procedures set out in the Codes require parties to first try to resolve the dispute between themselves.⁶⁵ Where the dispute cannot be resolved (within three weeks under the Franchising Code⁶⁶ or at any time under the Oil Code⁶⁷), either the Franchisor or Franchisee may refer the matter to a mediator or dispute resolution adviser. If mediation is initiated, both parties must attend and try to resolve the dispute.⁶⁸

There is also an obligation for both parties to act in good faith during the dispute resolution process.⁶⁹

Parties must pay for their own costs of attending mediation under the respective Codes.⁷⁰ Unless they have agreed otherwise, both parties are equally liable for the other costs of mediation specified under the codes.

Any action taken under the Codes to try to resolve a dispute does not affect parties' rights to commence legal action.⁷¹

The Codes each contain additional provisions regarding dispute resolution that are distinct to that Code.

The Franchising Code imposes an additional requirement on Franchisors to develop their own internal complaint-handling procedures to deal with disputes. This internal procedure must be set out in the franchise agreement and must broadly follow the same steps as the dispute resolution procedure set out in the Franchising Code.⁷² Where a dispute arises, a party can either seek to resolve the matter using the Franchisor's complaint-handling procedure or the procedure set out in the Franchising Code.⁷³

The Oil Code mandates a specific dispute resolution process for disputes that arise when a Franchisor fails to supply a declared petroleum product to a Franchisee.⁷⁴ If a dispute of this nature arises the complainant will need to notify the respondent, in writing, of the details of the dispute.⁷⁵ The complainant may also notify the dispute resolution adviser and ask the adviser to attempt to resolve the dispute.⁷⁶

Under the Oil Code, the dispute resolution adviser also has the power to make a non-binding determination in relation to a dispute.⁷⁷

⁶⁵ Clause 40(1)&(2) Franchising Code, Clause 44(1) Oil Code

⁶⁶ Clause 40(3) Franchising Code

⁶⁷ Clause 44(2)(a) Oil Code

⁶⁸ Clause 41(3) and (5) Franchising Code, Clause 44(4)&(5) Oil Code

⁶⁹ Clause 6 Franchising Code, Clause 45(1) Oil Code

⁷⁰ Clause 43(1) Franchising Code, Clause 47(2) Oil Code

⁷¹ Clause 37 Franchising Code, Clause 47(1) Oil Code

⁷² Clause 34 Franchising Code

⁷³ Clause 35 Franchising Code

⁷⁴ Clause 43 Oil Code

⁷⁵ Clause 43(2) Oil Code

⁷⁶ Clause 43(3) Oil Code

⁷⁷ Clause 43(7) Oil Code

Obligations specific to the Franchising Code

General obligation to act in good faith

The Franchising Code contains an obligation for all parties to a franchise agreement to act in good faith towards each other in respect of any matter relating to their agreement or the Franchising Code.⁷⁸ This means they must act honestly and not arbitrarily towards each other.⁷⁹ This obligation cannot be limited in any way by a franchise agreement.⁸⁰

The obligation to act in good faith also applies to parties who propose to enter into a franchise agreement.⁸¹

Information statement

The Franchising Code requires Franchisors to provide an information statement to prospective Franchisees.⁸² The information statement is a generic statement that highlights the risks and rewards of franchising. It must be provided to prospective Franchisees as soon as practicable after they express an interest in buying into the franchise.

Waivers

The Franchising Code provides that an agreement must not contain, or require a Franchisee to sign a waiver of any verbal or written representation the Franchisor has made to the Franchisee.⁸³

Rights and obligations during the agreement

Restraint of trade

A restraint a trade clause in a franchise agreement will have no effect in certain circumstances. If the Franchisee has sought, in writing, to extend their agreement and the Franchisor does not grant the extension, a restraint of trade clause in the agreement will have no effect if the Franchisee:

- had sought to extend the agreement on substantially the same terms as those contained in the Franchisor's current franchise agreement that applies to other franchisees or would apply to a prospective Franchisee and
- was not in breach of their agreement or any related agreement and
- had not infringed the intellectual property of the Franchisor or breached any confidentiality agreements and
- received only nominal, and not genuine, compensation for goodwill or
- the agreement provided no avenue by which to claim compensation in the event it was not extended.⁸⁴

Settling disputes

A franchise agreement must not require mediation to be conducted, or actions or proceedings to be brought outside of the State or Territory of the Franchisee, or any jurisdiction outside Australia.⁸⁵

⁷⁸ Clause 6(1) Franchising Code

⁷⁹ Clause 6(3) Franchising Code

⁸⁰ Clause 6(4) Franchising Code

⁸¹ Clause 6(2) Franchising Code

⁸² Clause 11 Franchising Code

⁸³ Clause 20(1)(b) Franchising Code

⁸⁴ Clause 23 Franchising Code

⁸⁵ Clause 21(2)(b) Franchising Code

A franchise agreement must not contain a clause that requires a Franchisee to pay the Franchisor's costs to settle a dispute under the agreement.⁸⁶

If a franchise agreement contains such clauses, those clauses are of no effect.⁸⁷

Former franchisees' details

A Franchisor must not engage in conduct with the intention of influencing a former Franchisees' decision to request, or not request, that their details be withheld from prospective Franchisees.⁸⁸

Dealing with marketing and advertising fees

If the Franchisor operates a marketing fund, the Franchising Code imposes certain restrictions on how the Franchisor can deal with the marketing and advertising fees contributed to that fund.

The Franchisor must maintain a separate bank account for marketing and advertising fees and contribute to the fund on the same basis as other Franchisees for each company-owned store that a Franchisor operates.⁸⁹ Marketing and advertising fees may only be used to meet certain expenses.⁹⁰

Significant capital expenditure

During the term of a franchise agreement a Franchisor must not require a Franchisee to undertake significant capital expenditure.⁹¹ The Franchising Code does not define what 'significant capital expenditure' means.

However, a Franchisor can require Franchisees to incur expenses where the expenditure:⁹²

- was disclosed to the Franchisee in the disclosure document that they received before entering into, renewing, or extending their franchise agreement or
- will be incurred by a majority of Franchisees and a majority of those Franchisees approve the expense or
- is necessary to comply with legislative obligations or
- has been agreed to by the franchisee or
- is considered necessary by the Franchisor as a capital investment in the franchised business, justified by a statement which sets out the:
 - rationale for making the investment
 - amount of capital expenditure required
 - anticipated outcomes and benefits
 - expected risks associated with the investment.

Record-keeping⁹³

If the Franchising Code requires, or allows, a Franchisee or prospective Franchisee to give something to a Franchisor in writing, the Franchisor is required to keep this type of document or a copy of it. This includes any documents provided electronically.⁹⁴

⁸⁶ Clause 22 Franchising Code

⁸⁷ Clause 21(3) and Clause 22 Franchising Code

⁸⁸ Clause 32(3) Franchising Code

⁸⁹ Clause 31 Franchising Code

⁹⁰ Clause 31(3) Franchising Code

⁹¹ Clause 30(1) (Franchising Code)

⁹² Clause 30(2) (Franchising Code)

⁹³ Clause 19 Franchising Code

⁹⁴ Clause 19(1) Franchising Code

If a Franchisor makes any statements or claims in the disclosure document which rely on another document to support the statement or claim, they must keep that document.⁹⁵ The Franchisor must keep these documents for six years after they were created.⁹⁶

Penalties for breaches of the Franchising Code

Since 1 January 2015, the ACCC has had the power to seek pecuniary penalties and issue infringement notices for breaches of certain provisions of the Franchising Code.

Both Franchisors and Franchisees may be liable for pecuniary penalties of up to 300 penalty units⁹⁷ (currently \$63 000⁹⁸) if they breach certain sections of the Franchising Code. A complete list of the pecuniary penalty provisions is provided at **Attachment E**.

The ACCC can also issue an infringement notice where the ACCC has reasonable grounds to believe that a person has breached a pecuniary penalty provision of the Franchising Code.⁹⁹ Infringement notices provide a timely and cost-effective way of resolving concerns and avoiding legal proceedings. The current value of an infringement notice is 50 penalty units for a body corporate (\$10 500 as of 1 July 2017).¹⁰⁰

The ACCC can issue an infringement notice within 12 months of the alleged breach. Each notice is limited to a breach of a single penalty provision but multiple notices may be issued if there are alleged breaches of multiple provisions.¹⁰¹

Whilst there is no obligation to pay an infringement notice, non-payment may expose a party to the prospect of legal proceedings initiated by the ACCC.¹⁰²

Obligations specific to the Oil Code

Pre-entry rights - disclosure and cooling off

The Oil Code requires Franchisors to maintain two disclosure documents; a long form and a short form. The long form document is used for agreements longer than five years¹⁰³ and the short form document is used for agreements of a lesser duration.¹⁰⁴ However, a Franchisee whose agreement is for less than five years may request a long form document.¹⁰⁵

The short form disclosure document differs from the long form in that it doesn't need to contain information about: the Franchisor's business experience, payments to agents, existing agreements, requirements for the supply of goods to and from the Franchisee, site information, financing, summary of other conditions (including end of term arrangements), obligations to sign related agreements, earnings information, materially relevant facts and other relevant details.¹⁰⁶

⁹⁵ Clause 19(2) Franchising Code

⁹⁶ Clause 19(3) Franchising Code

⁹⁷ Section 51AE(2) of the CCA

⁹⁸ The calculation of the monetary amount of a penalty is dependent on 'penalty units' that are set out in the *Crimes Act 1914*. From 1 July 2017 the value of the penalty unit is \$210.

⁹⁹ Section 51ACD of the CCA

¹⁰⁰ Section 51ACF of the CCA

¹⁰¹ Section 51ACD(2) of the CCA

¹⁰² Section 51ACH of the CCA

¹⁰³ Clause 16(1) Oil Code

¹⁰⁴ Clause 16(2) Oil Code

¹⁰⁵ Clause 17(1)&(2) Oil Code

¹⁰⁶ Refer to the requirements listed in Annexure 1 and 2 of the Oil Code

Rights and obligations during the agreement

The Oil Code sets out a minimum duration for agreements entered into after 1 March 2007. Any agreement entered into after that date must be for at least five years.¹⁰⁷

However, the minimum tenure period is extended if the agreement requires the Franchisee to buy fuel from the Franchisor (or gives the Franchisor the entitlement to sell it to the Franchisee) and the Franchisor owns or leases the retail site. In this case, agreements must be for at least five years and provide for a minimum of at least one four year option to renew.¹⁰⁸ The Franchisor cannot refuse the renewal unless they lease the site for another purpose, dispose of the site or operate it for another purpose.¹⁰⁹

The Oil Code provides for some exemptions to the minimum tenure requirement.¹¹⁰ These are largely related to the duration of the lease on the site (sites with leases of shorter terms that meet the criteria set out in clause 32(11) may negate the minimum term requirement) but also include situations where the total initial non-refundable amount paid by the Franchisee is less than \$20 000.¹¹¹

Termination of the agreement

The Oil Code sets out processes that a Franchisor must follow if they propose to:

- Terminate where the total initial non-refundable amount paid by the Franchisee is less than \$20 000 and the agreement itself does not specify a minimum term¹¹²
- Mutually agree with the Franchisee to the early termination of the agreement.¹¹³

In order to terminate in the former scenario, the Franchisor must give the Franchisee 30 days' notice of their intention to terminate¹¹⁴ and offer to buy, or find a buyer for the Franchisee's fuel stocks, merchandise and equipment.¹¹⁵ The purchase price for these items must be determined by either an agreement between the Franchisor and Franchisee or if they are unable to agree, by a valuer.¹¹⁶

In the instance of a mutual agreement to terminate, the Franchisor must notify the Franchisee that they have rights under the agreement, that the Franchisor will negotiate with them to terminate those rights and that they should seek financial and legal advice about any offer made by the Franchisor.¹¹⁷

The Franchisor must also offer to pay the costs relating to the termination, including a proportional refund for the remaining period of the agreement.¹¹⁸ Further, the Franchisor must offer to buy, or find a buyer for the Franchisee's fuel stocks, merchandise and equipment.¹¹⁹ The purchase price for these items must be determined by either an agreement between the franchisor and franchisee or if they are unable to agree, by a valuer.¹²⁰

¹⁰⁷ Clause 32(5) Oil Code

¹⁰⁸ Clause 32(5) Oil Code

¹⁰⁹ Clause 32(6) Oil Code

¹¹⁰ Clause 32(11) Oil Code

¹¹¹ Clause 32(11)(c) Oil Code

¹¹² Clause 37 Oil Code

¹¹³ Clause 38(1) Oil Code

¹¹⁴ Clause 37(2)(a) Oil Code

¹¹⁵ See clauses 37(2)(b)(c)(d) Oil Code

¹¹⁶ *ibid*

¹¹⁷ Clause 38(2)(a) Oil Code

¹¹⁸ Clause 38 (2)(b) Oil Code

¹¹⁹ See clauses 38(2)(c)(d)(e) Oil Code

¹²⁰ *ibid*

Dispute resolution

The Oil Code mandates a specific dispute resolution process for disputes that arise when a Franchisor fails to supply a declared petroleum product to a Franchisee.¹²¹

If a dispute of this nature arises the complainant will need to notify the respondent, in writing, of the details of the dispute.¹²² The complainant may also notify the dispute resolution adviser and ask the adviser to attempt to resolve the dispute.¹²³ The dispute resolution adviser has the power to make a non-binding determination in these circumstances.¹²⁴

Terminal gate price (TGP) and related arrangements

The Oil Code contains a Part dedicated to setting out the requirements for TGP agreements. This section, which sets out what a Franchisor may charge a Franchisee,¹²⁵ governs:

- when an option may be offered under a TGP agreement¹²⁶
- arrangements for when a Franchisee seeks to purchase petrol from a Franchisor outside of a term contract¹²⁷
- when prices must be identified¹²⁸
- how prices must be disclosed¹²⁹
- the documentation that must be provided in relation to the sale of petrol, when these documents must be provided and the information that they must contain¹³⁰
- when the Franchisor is and is not required to supply petrol products to the Franchisee¹³¹
- health and safety requirements.¹³²

¹²¹ Clause 43 Oil Code

¹²² Clause 43(2) Oil Code

¹²³ Clause 43(3) Oil Code

¹²⁴ Clause 43(7) Oil Code

¹²⁵ Clause 7(1)&(2) Oil Code

¹²⁶ Clause 7(3) Oil Code

¹²⁷ Clause 7(4) Oil Code. 'Term contract' means a contract between a customer and a wholesale supplier that sets out the price at which, and the conditions under which, the customer will purchase a declared petroleum product for a fixed period.

¹²⁸ Clause 8 Oil Code

¹²⁹ Clause 9 Oil Code

¹³⁰ Clause 10 Oil Code

¹³¹ Clause 11 Oil Code

¹³² Clause 12 Oil Code

Attachment D - Application of the CCA to franchise agreements

The Franchising and Oil Codes operate alongside a business' obligations and protections under the CCA, including the ACL. Franchisors and Franchisees must comply with both the obligations set out in the Codes and the obligations set out in the CCA and ACL.

The CCA provides protections beyond those expressly provided for in the Franchising and Oil Codes. In particular, the ACL:

- prohibits false representations and misleading or deceptive conduct (ss18 and 29),
- prohibits unconscionable conduct (s21) and
- provides a means of challenging unfair contract terms in standard form small business contracts (s23), which can include franchise agreements.

The CCA also imposes a number of additional obligations on the Franchisor and Franchisee. In particular, the CCA:

- prohibits the Franchisor from requiring the Franchisee to acquire goods and services from particular suppliers if doing so has the purpose, effect or likely effect of substantially lessening competition (s47)
- prohibits the Franchisor from providing the Franchisee with an exclusive territory if doing so has the purpose, effect or likely effect of substantially lessening competition (s45) and
- prohibits the Franchisor and Franchisee from agreeing to minimum prices for the sale of the Franchisee's goods or services (s48).

The above anti-competitive conduct can be authorised by the ACCC where the public benefits of engaging in the conduct outweigh the public detriments.

Further information about the additional protections and obligations imposed by the CCA and ACL are set out below.

Key ACL issues

Misleading or deceptive conduct

The ACL prohibits a person from engaging in conduct, in trade and commerce, that is misleading or deceptive or likely to mislead or deceive. Where the conduct of concern falls under one of the specific prohibitions in s29 of the ACL, the conduct is subject to a civil pecuniary penalty.

Relevantly, the disclosure obligations under the Codes are strengthened by the prohibitions against false representations and misleading or deceptive conduct under the ACL. If a Franchisor meets their disclosure obligations under one of the Codes, but does so in a way that is misleading or deceptive, then the ACCC and/or the affected party can take enforcement action.

The ACL does not generally create a positive obligation to disclose information in this manner, except where the failure to provide the information is itself misleading or deceptive. For example, a failure to disclose certain court proceedings (ongoing or historical) against a Franchisor may not be misleading or deceptive. However, it would be a breach of the Codes.

When the ACCC investigates alleged breaches of one of the Codes, there is often associated alleged misleading or deceptive conduct. This was the case in both the *Ultra Tune* and *Geowash* litigation discussed in Attachment A.

Unconscionable conduct

Section 21 of the ACL prohibits conduct in connection with the supply or acquisition of goods and services that is, in all the circumstances, unconscionable. In some instances, where a party is in breach of the Codes, they may also be in breach of s21. For example, where a Franchisor has deliberately failed to disclose upfront costs in the franchise agreement and then sought payments not provided for under the agreement, it is likely that the Franchisor may have breached s21. The ACCC alleges that this was the case in the *Geowash* matter discussed in Attachment A. This litigation is ongoing.

Unfair contract terms

Under s23 of the ACL, a term of a consumer or 'small business contract' is void if the term is unfair and the contract is a standard form contract. A contract is a 'small business contract' if:

- the contract is for the supply of goods or services or the sale or grant of an interest in land; and
- at least one party to the contract is a business that employs fewer than 20 people¹³³ and
- either the upfront price payable under the contract does not exceed \$300 000 or, if the contract is for a duration of more than 12 months, the upfront price payable does not exceed \$1 million.

The meaning of 'unfair' is contained in s24 of the ACL and includes circumstances where:

- it would cause a significant imbalance in the parties' rights and obligations arising under the contract
- it is not reasonably necessary to protect the legitimate interests of the party who would be advantaged by the terms
- it would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on.

Under the unfair contract terms regime, it is not illegal for a standard form contract to contain an unfair contract term.

However, a party to the contract or an ACL regulator can apply to the court to have declared unfair and void – this means the term in question is not binding on the parties. The rest of the contract will continue to bind the parties to the extent it is capable of operating without the unfair term. It is only illegal for a contract to contain an unfair term where the specific term has been declared unfair by the court, and a party subsequently seeks to apply or rely upon that unfair term. In these circumstances, a court can:

- grant an injunction preventing the party from acting upon the term
- make an order to provide redress to non-party small businesses or
- make any other orders it considers appropriate.

¹³³ Including casual employees that are employed on a regular and systematic basis, see sub-s23(5).

Key competition issues

Franchisors and Franchisees are also required to comply the anti-competitive conduct prohibitions in the CCA. There are three issues that commonly arise in the franchising sector that may give rise to competition concerns: third line forcing, exclusive territories and setting prices for goods sold by the franchise.

Third line forcing

A common competition issue that can arise in franchising arrangements is third line forcing, which is a type of exclusive dealing prohibited under section 47 of the CCA.

Third line forcing occurs when a business will only supply goods or services, or give a particular price or discount, on the condition that the purchaser buys goods or services from a particular third party. If the buyer refuses to comply with this condition, the business will refuse to supply them with goods or services. Third line forcing will only break the law if it has the purpose, effect or likely effect of substantially lessening competition in the relevant market.

An assessment of whether third line forcing is likely to result in a substantial lessening of competition is complex, but is likely to include consideration of factors such as:

- whether there has been a real effect on the competition in the overall market for a particular product and its substitutes;
- whether the refusal to supply would substantially restrict the availability of that type of product to consumers; and
- whether consumers are severely restricted in their ability to buy a product or its substitutes because the business has imposed territorial restrictions as a condition of supply.

In the context of franchising, third line forcing arises when a Franchisor refuses to enter into a franchise agreement with a Franchisee (or provide services under a franchise agreement) unless the Franchisee agrees to purchase goods or services from a particular supplier. Often this includes key inputs for the business such as a specific supplier of drinks to be sold in the franchise or a particular type of equipment (such as a steam cleaner) to be used in the business.

In the ACCC's experience, third line forcing arrangements in the franchising sector are unlikely to substantially lessen competition where the franchise itself and the supplier both compete with a number of other businesses to supply the same or similar products.

There are a number of reasons why a Franchisor may require Franchisees to use a particular product or type of equipment. Often this is a means of ensuring quality of goods and consistency of service between franchises. This, in turn, may help to protect the brand of the franchise. In some cases, the Franchisor may receive a rebate or some other kind of benefit from suppliers. The Franchising Code requires Franchisors to disclose which suppliers they receive a rebate or benefit from.

One way to ensure that franchise agreements do not breach third line forcing provisions in the CCA is to offer Franchisees a choice of suppliers. This allows Franchisors to maintain consistency between the businesses, but also gives Franchisees the capacity to seek out the best price for goods or choose the supplier that are more convenient for them.

If a Franchise agreement contains terms that amount to third line forcing and a Franchisor is concerned that the third line forcing may substantially lessen competition, the Franchisor can seek authorisation from the ACCC or notify the ACCC of the conduct. In both cases the

ACCC will assess whether, in all the circumstances, the conduct result in a likely public benefit which would outweigh the likely public detriment. If the ACCC finds that the benefits outweigh the detriment the Franchisor will be allowed to continue to engage in the third line forcing conduct.

Exclusive Territories

In the ACCC's experience, Franchisees may seek some assurance from Franchisors that the Franchisee will have exclusive access to a particular territory, or that the Franchisor will not establish a Franchise within a particular geographic area. Franchise agreements that provide exclusive access to territories may raise concerns under section 45 of the CCA if they have the purpose, effect, or likely effect of substantially lessening competition.

As outlined above, the test of substantially lessening competition needs to be applied on a case by case basis. The ACCC takes a range of issues into account when assessing the competition impact of particular agreements, however, in the franchising context, the length of the agreement is often a key factor. The shorter the term of the agreement less likely they are to substantially lessen competition.

As with third line forcing, elements of franchise agreements that raise concerns under section 45 of the CCA can be authorised by the ACCC, where the public benefits outweigh the public detriment.

Setting prices

A Franchisor generally has detailed knowledge of the running costs of a franchise business and is well placed to recommend a price point for the products or services that the franchise sells. It is permissible for a Franchisor to set a maximum price for the goods or services sold in a franchised business, and / or circulate a recommended price list. However, a Franchisor cannot specify a minimum retail price that Franchisee must charge for their goods or services. For example, if a Franchisor withheld marketing support for a particular Franchisee because they sold products below a specified price, this would amount to retail price maintenance and is likely to breach section 48 of the CCA.

It is also important that where a Franchisor chooses to provide a recommended price list, it is simply a recommendation and there is no agreement between the Franchisor and Franchisees to charge those particular prices. If there was an agreement, there is a risk that the Franchisor and Franchisees could be engaging in price fixing which is prohibited under the CCA.

Attachment E – Current civil pecuniary penalty provisions under the Franchising Code

| Obligation | Relevant clause |
|---|--------------------------|
| Failure to act in good faith | subclause 6(1) |
| Failure to create a Code compliant disclosure document | subclause 8(1) |
| Failure to update the disclosure document within 4 months after the end of each financial year | subclause 8(6) |
| Failure to update the disclosure document to reflect the position of the franchise as at the end of the last financial year in circumstances where the Franchisor was not required to update but a Franchisee has requested a disclosure document | subclause 8(8) |
| Failure to provide pre-entry disclosure documents as required by the Code | subclauses 9(1) and (2) |
| Failure to provide lease documents where Franchisee leases premises from the Franchisor or its associate or failure to do so within one month | subclauses 13(1) and (2) |
| Failure to provide lease information where Franchisee occupies premises without a lease or failure to do so within the specified time | subclauses 13(3) and (4) |
| Failure to provide certain agreements to the Franchisee | subclause 14(1) |
| Failure to comply with reporting obligations for marketing or cooperative funds | subclause 15(1) |
| Failure to provide a copy of the disclosure document to a Franchisee within specified time (after receiving a written request) | subclause 16(1) |
| Failure to disclose a materially relevant fact | subclauses 17(1) and (2) |
| Failure to provide notice of end of term arrangements | subclauses 18(2) |
| Failure to inform a Franchisee that they may request a disclosure document when providing notice of end of term arrangements | subclause 18(3) |
| Failure to repay all payments (whether of money or of other valuable consideration) made by the Franchisee to the Franchisor within the specified time after the Franchisee has exercised their cooling off rights | subclause 26(3) |
| Failure to provide reasonable written notice of proposed termination for breach | subclause 27(2) |
| Failure to provide reasonable written notice of proposed termination, and the reasons for it, where the Franchisee is not in breach | subclause 28(3) |

| | |
|---|-----------------|
| Franchisor influencing, or attempting to influence a former Franchisee to request that their details not be disclosed | subclause 32(3) |
| Franchisor restricting or impairing the freedom or ability of Franchisees or prospective Franchisees to form an association | clause 33 |
| Failure to attend mediation under the internal complaint-handling procedure | subclause 39(3) |
| Failure to attend mediation under the code complaint-handling procedure | subclause 41(3) |



AUSTRALIAN COMPETITION
& CONSUMER COMMISSION

Small business in focus

Small business, franchising & agriculture news—Report no. 15

July—December 2017



In the last six months



737 000

page views of our small business resources



\$2.47m

reported small business scam losses



24

compliance checks (franchising, horticulture + food & grocery codes)



6

ongoing inquiries



4

new court actions for matters affecting small business



Changes to competition laws introduced

A profile of the typical business contacting the ACCC¹



At least 1 out of 3 that contact us are established businesses aged 10+ years

Majority are micro sized businesses with 0-4 staff (63% of contacts)



Most commonly report misleading or deceptive conduct (21% of contacts)

Coming up this year

- New food labelling requirements mandatory from 1 July 2018
- Review of the Food & Grocery Code
- Horticulture Code transition period ends 1 April 2018

¹ ACCC data of contacts where business size and age was stated (excludes scam reports).

Who's contacting us²

| Contact type | Small business ³ | | Franchising | | Agriculture | |
|--------------|-----------------------------|---------------|---------------|---------------|---------------|---------------|
| | July-Dec 2017 | Jan-June 2017 | July-Dec 2017 | Jan-June 2017 | July-Dec 2017 | Jan-June 2017 |
| Reports | 2590 | 2199 | 185 | 192 | 161 | 138 |
| Enquiries | 2356 | 1503 | 94 | 127 | 94 | 66 |
| Total | 4946 | 3702 | 279 | 319 | 255 | 204 |

Reports by key issue⁴

| Issues | Small business | | Franchising | | Agriculture | |
|--|----------------|---------------|---------------|---------------|---------------|---------------|
| | July-Dec 2017 | Jan-June 2017 | July-Dec 2017 | Jan-June 2017 | July-Dec 2017 | Jan-June 2017 |
| Consumer law related issues | | | | | | |
| Misleading conduct/false representations | 1057 | 696 | 49 | 32 | 77 | 59 |
| Consumer guarantees | 464 | 317 | 2 | 1 | 22 | 13 |
| Product safety | 36 | 34 | 1 | - | 1 | 5 |
| Unconscionable conduct | 40 | 39 | 9 | 8 | 4 | 3 |
| Wrongly accepting payment | 196 | 132 | 1 | - | 10 | 5 |
| Unsolicited goods and services | 34 | 13 | - | 1 | - | - |
| Other Australian Consumer Law (ACL) issues | 237 | 128 | 8 | 3 | 12 | 7 |
| Competition related issues | | | | | | |
| Misuse of market power | 123 | 90 | - | - | 6 | 10 |
| Exclusive dealing | 87 | 78 | 8 | 15 | 4 | 5 |
| Other competition issues | 79 | 58 | 4 | 4 | 5 | 4 |
| Franchising Code related issues | | | | | | |
| Inadequate disclosure | - | - | 29 | 26 | - | - |
| Not acting in good faith | - | - | 20 | 27 | - | - |
| Improper termination of agreement | - | - | 11 | 6 | - | - |

Enforcing the law

In the last six months, we've worked to protect small businesses through our enforcement action, including:

- Court action and penalties totalling \$150 000 against Pastacup franchisor **Morild Pty Ltd** and the company's co-founder and former director for [failing to provide a disclosure document](#) to prospective franchisees which complied with the Franchising Code.
- Issuing an Infringement Notice of \$9000 to **West Aust Couriers Pty Ltd trading as Fastway Couriers (Perth)** for [allegedly breaching the Franchising Code](#) by providing a disclosure document to a prospective franchisee that didn't include details of former franchisees that had terminated or transferred their courier franchises.
- Starting court action against **Domain Name Corp Pty Ltd and Domain Name Agency Pty Ltd trading as Domain Name Register** for [alleged misleading or deceptive conduct](#) and making false or misleading representations to Australian businesses about the domain name services they offered.
- [Starting court action](#) against **Servcorp Ltd** and two of its subsidiaries, alleging that a number of terms in Servcorp's standard form contracts with small business are unfair and should be declared void.
- [Court action and orders](#) declaring, by consent, that eight terms in the small business standard form contract used by **JJ Richards & Sons Pty Ltd** were unfair and therefore void.

² 'Reports' are contacts about potential misconduct, and 'enquiries' are contacts seeking advice or information about competition or consumer issues. Further investigations of reports may not reveal a legislative breach. Data should be used as general guidance only and care should be taken when drawing any conclusions.

³ This publication applies a different methodology to previous SBIF publications and excludes data on scam contacts to the ACCC, which has resulted in a lower number of contacts.

⁴ Some reports are categorised as having more than one issue. Excludes reports not within the remit of the ACCC.

Agriculture

In November, we released our [interim report](#) on the competitiveness of prices, trading practices and the supply chain in the Australian **dairy industry**. The final report will be submitted to the Treasurer by 30 April 2018.

We also held our 4th **Agriculture Consultative Committee** meeting in November. A review of the Committee's membership for 2018 and 2019 is underway.

Have you heard about our new **online tool for anonymous agricultural complaints**? We encourage you to [report](#)⁵ potential misconduct in the agriculture industry using our online tool.

Horticulture Code

The transition period for the revised [Horticulture Code](#) ends on 1 April 2018. We have been working with industry organisations to educate growers and traders of horticulture produce about their rights and obligations. We are now shifting focus to enforcing the Code. During this period we issued 15 compliance check notices to horticulture traders across the wholesale central markets.

Changes to competition laws

On 6 November 2017, Australia's competition laws were amended by Parliament following a [comprehensive review](#). Changes relating to small business include:

- New 'purpose or effects test' in misuse of market power provisions—corporations with substantial market power are now prohibited from engaging in conduct that has the purpose, effect or likely effect of substantially lessening competition.
- New concerted practices prohibition—introduction of a new prohibition against concerted practices that have the purpose, effect or likely effect of substantially lessening competition. A concerted practice involves some form of cooperation between businesses that is less than an 'agreement'.
- Changes to the [collective bargaining notification process](#) now make it easier and more flexible for small businesses to lodge a notification to obtain legal protection to collectively bargain with a customer or supplier.

The ACCC has developed interim guidelines setting out how we propose to interpret the new [misuse of market power](#) and [concerted practices](#) provisions, which are available on our website.

Consumer guarantee reports increase

In 2017, reports to the ACCC about consumer guarantee issues increased for both consumers and small businesses. A review of the online policies of several large Australian clothing retailers found that some may be misleading consumers about their rights under the ACL's consumer guarantees.

To make sure you know when you have to give a refund, and when you're entitled to one, check out our recently updated guide, [Small business and the Competition and Consumer Act](#) on our website.

Business scams

The ACCC reminds you to beware of scams targeting businesses, particularly false billing scams which can include:

- **Fake directories and advertising scams** in which you receive an invoice for a listing or advertisement that you didn't authorise or request, resulting in subsequent demands for payment.
- **Domain name renewal scams** involving an unsolicited invoice or email from a domain name supplier trying to trick you into signing up to their service or a scammer trying to make you pay for a fake domain name registration.

For further information visit www.scamwatch.gov.au and [sign up for radar alerts](#).

Exemptions

Sometimes conduct that breaches Australia's competition laws can still have some wider public benefits. In those cases businesses can lodge an authorisation or notification asking for an exemption from us to engage in the conduct. For example, during the last six months, we allowed:

- **Licensed Post Office Group** to collectively negotiate with Australia Post on behalf of itself and current and future members for the provision of postal and distribution services.
- **SA Baiada Growers Group** to collectively bargain on behalf of current and future members who provide chicken growing services to Baiada.
- **Australian Medical Association (NSW)** to collectively negotiate on behalf of visiting medical officers in NSW with Healthscope Operations Pty Ltd regarding the terms and conditions (including remuneration) of visiting medical officer contracts at the Northern Beaches Hospital.

We have developed [draft guidelines](#) on small business collective bargaining to assist businesses, including farmers, to engage in and understand the processes for obtaining ACCC approval for collective bargaining or boycott activity.

New car retailing market study—final report

In December, we released our [final report](#) which recommended that:

1. A **mandatory scheme** be introduced to give independent repairers the same level of access to technical information as dealers and preferred repairer networks (subject to the appropriate safeguards).
2. Manufacturers **update their complaints handling systems** and commercial arrangements with dealers to ensure that they properly consider customers' ACL consumer guarantee rights.

The ACCC will now work to implement the study's actions and recommendations, including taking enforcement action where we see potential breaches of the ACL.

⁵ <https://app.whispli.com/accc-report-an-agricultural-issue-anonymously>

Retail Electricity Pricing Inquiry

The ACCC is continuing its inquiry into the **competitiveness of retail electricity markets** in the National Electricity Market. In October, we released our [preliminary report](#) which found that retail electricity prices for small businesses and households have increased by 80 to 90 per cent over the past decade (when taking into account estimated price rises in July 2017).

The remainder of the inquiry will focus on identifying practical and meaningful measures that will ease the pressures on electricity prices for Australians. A final report will be provided to the Treasurer by 30 June 2018.

Country of origin food labelling

From 1 July 2018, most food offered or suitable for retail sale in stores, markets, online or from vending machines must be labelled according to the *Country of Origin Food Labelling Information Standard 2016*.

To assist businesses who produce or supply dairy products in Australia to comply with the Standard, we released a [Country of origin labelling and the dairy industry](#) guide. The guide sets out our views on the application and interpretation of the new labelling rules for dairy-based foods e.g. cheese and yoghurt.

Unfair contract terms

The ACCC continues to educate businesses and take action to ensure they receive the protections of the new unfair contract terms law. In addition to our court action against **JJ Richards & Sons** and **Servcorp**, we have also liaised with other businesses about potentially unfair contract terms. In response to concerns raised by us about certain terms, **Australia Post** is proposing some amendments to its Licensed Post Office Agreement. It plans to consult with its licensees on the proposed changes.

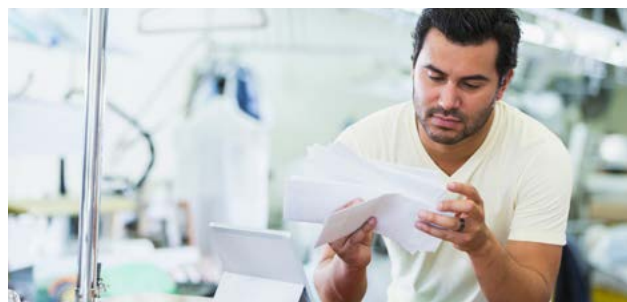
Small Business & Franchising Consultative Committee—New members

Our SBFCC keeps us updated on issues affecting the small business and franchising sectors. We recently appointed new members after reviewing our membership for 2018–19, which now consists of 17 industry associations, five academics, four business advisors and three legal advisors.

Excessive payment surcharging

The ban on excessive surcharges, which already applied to large businesses, was extended to small businesses on 1 September 2017. This ban restricts the amount a business can charge customers for using EFTPOS (debit and prepaid), MasterCard (credit, debit and prepaid), Visa (credit, debit and prepaid) and American Express cards issued by Australian banks.

Red Balloon Pty Ltd, recently paid a [\\$43 200 penalty](#) after we issued four infringement notices for allegedly charging four customers' excessive surcharges when they made either credit or debit card payments.



Dr Michael Schaper

In May 2018, the ACCC will farewell Dr Michael Schaper who was first appointed as Deputy Chair of the Commission in July 2008.

For nearly 10 years, Michael has led our engagement with small businesses, franchisors and franchisees, industry associations and other regulators with an interest in business liaison. Michael has made a significant contribution in building and maintaining these relationships and ensuring small business is considered on the government agenda.

Online programs

How well do you and your staff know your rights and obligations under Australia's competition and consumer laws? Find out now by checking out our free small business education program www.accc.gov.au/ccaeducation

Since its launch in 2013, the small business program, together with a similar program for tertiary students, has been accessed by over 78 000 users.

Current in-depth inquiries

[Dairy inquiry](#)

[Digital platforms inquiry](#)

[Electricity supply & prices inquiry](#)

[Gas inquiry 2017–2020](#)

[Northern Australia insurance inquiry](#)

[Residential mortgage products price inquiry](#)

Publications and fact sheets

[Small business and the Competition and Consumer Act \(updated\)](#)

[Country of origin claims and the Australian Consumer Law](#)

[Country of origin labelling and the dairy industry](#)

[Payment surcharges—only charge what it costs you](#)

[Unfair contract terms: New protection for small businesses](#)

[How the Horticulture Code Helps You & Enforcement of the Horticulture Code of conduct](#)

[Gas inquiry December 2017 interim report](#)

[Business scams](#)

Contact us

ACCC Small Business Helpline: 1300 302 021

ACCC website: www.accc.gov.au/smallbusiness

Email updates: Keep up-to-date on the latest news and events by signing up to one of our **free newsletters** for small businesses, franchises, agriculture sector and educators. Subscribe online on [our website](#).