



***FRANCHISE COUNCIL OF AUSTRALIA
ADELAIDE CONFERENCE
23rd OCTOBER 2001***

***“THE HEALTH OF
FRANCHISING FROM THE VIEWPOINT
OF ITS REGULATOR”***

***Presented by
Commissioner John Martin
Australian Competition & Consumer Commission***

Introduction

My colleague Brendan Bailey and I welcome the opportunity to participate with you all in this highly professional forum. Brendan will be known to many of you as the guru on franchising matters at the ACCC.

This conference has given us much to think about in terms of the directions for franchising in Australia.

The franchising sector's significance to the economy is demonstrated by its annual turnover estimated at \$81 billion and its extensive coverage of business types including specialist retailing, courier services, domestic cleaning and other services, lawn-mowing, real estate, lottery agents, auto parts and services, motor vehicle dealers, fast food, printing and petrol outlets.

Operation of the Franchising Code

The Australian Competition and Consumer Commission plays an active role in administering and enforcing the Franchising Code of Conduct through its powers under the *Trade Practices Act*. The mandatory Code was introduced in July 1998 and became fully operational in October 1998.

Overall the impression is the Code is working effectively and the health of the franchising industry appears generally sound. There is always room for improvement but the initial teething problems that followed the introduction of the Code seem to have been addressed.

An important part of my role in the Commission is to present the small business perspective. As we know, franchisees and the majority of franchisors are technically, small businesses. In the interests of the Australian economy our objective is to encourage small businesses to grow and prosper.

The Commission receives, on average, over 2000 inquiries and complaints each quarter from small business. They cover the full range of matters dealt with under the Trade Practices Act.

Each quarter we receive over 150 inquiries and complaints about franchising.

Leaving aside GST matters, the three main areas of franchising inquiry or complaint are:

- whether the Code applies to a particular business relationship;
- obligations in the disclosure document and representations made by the franchisor; and
- the operation of the Code, particularly in the area of resolution of disputes.

Legal Action

Since the Code began in 1998 only four Code-related matters have resulted in a decision by the Commission to initiate formal litigation.¹ While all these matters are Code-related they can also include allegations of other breaches of the Trade Practices Act. A franchisor in its business dealings must also comply with the other provisions of the Trade Practices Act including, not engaging in restrictive trade practices and not misleading or deceiving ordinary consumers.

Some have argued that the Commission has been over zealous in looking at franchising when seeking to clarify the statutory provisions on breaches of the Code and unconscionable conduct in business transactions. However the Commission has not singled out franchising and its actions have only responded to complaints which were well investigated before action was taken. In the area of unconscionable conduct the Commission has also run significant cases on retail tenancy and, in the financial sector, has taken action against a major bank. A fourth major area of complaint currently under investigation is the dealings between primary producers and larger players further down the supply chain.

ACCC Processes

Given the misinformation surrounding some of the franchising court cases, it may be useful to explain procedures the Commission has in place before deciding to take legal action.

The first step is to hold discussions with both the franchisees and the franchisor to encourage them to resolve problems amicably. The Commission makes it clear that its initial role is to hear both sides of the issues involved.

It is reassuring that most parties tend to reach an understanding. When this is not possible the Commission steps aside to allow the parties to go to mediation. Only where there is no other option will the Commission take further action such as seeking a court enforceable undertaking from an offending party or in extreme cases go to litigation.

The decision on litigation is not taken lightly. The Commission has a formal process for considering each matter through its Enforcement Committee process.

It would be a serious mistake to assume that the Commission only sees matters through the eyes of the franchisees. That is not the case and it has never been. The ACCC role is to apply regulatory measures without fear or favour consistent with common sense and proper commercial practices.

¹ The Commission has successfully concluded litigation in *ACCC v Simply No-Knead (Franchising) Pty Ltd* (2000) and *ACCC v Cheap As Chips Franchising Pty Ltd* (2001), and the recently initiated (but not concluded) proceedings in *ACCC v Suffolk Parke Pty Ltd* (2001) and *ACCC v 4WD Systems Pty Ltd* (2001).

Coverage and Compliance Issues

The Commission notes the development of case law on franchising in Australia and overseas. These developments have helped clarify the law. We now await, with interest, judicial findings arising from private actions that will further clarify of the definition a franchise agreement under the Code.² The Commission promotes a broad view of the Code because it encourages better standards in business conduct – a goal that benefits franchisors, franchisees and ultimately the reputation of the sector with consumers.

The ACCC was also mindful of the decision in the private action *Timic v Hammock* in the Federal Court of Australia in the Victorian Division in February 2001. The court found that an arbitration clause, as distinct from mediation under the Code, could ultimately result in the removal of the matter to the home jurisdiction of the franchisor – which in that case was Connecticut in the United States. The decision in the *Timic* case resulted in a recent amendment to the Code to make it clear that mediation, at least, must be conducted in Australia.³

I would point out that the Commission's role is not to decide the legal meaning of the provisions of the Trade Practices Act. That is the function of the courts. The courts in this country consistently deliver well-reasoned decisions. There was a positive outcome recently in the United States March 2001 decision of *Bolter v Superior Court*⁴ in which the California Court of Appeal held that an arbitration forum selection clause in a franchise agreement was unconscionable and unenforceable. In that particular case, the franchisee in dispute was facing relocation of an arbitration hearing from California to Utah with all the attendant additional costs.

While the Commission is responsible for the administration of the Franchising Code of Conduct it does not determine policy. That role belongs to the Minister for Small Business supported by the Department of Employment, Workplace Relations and Small Business. The Commission does, however, become involved in how the Code is applied in a practical sense. We welcomed the recent set of amendments to the Code, effective from 1 October 2001, offering greater flexibility and streamlining of obligations under the Code.

² See, for example, the decisions in *Agro Holdings Ltd v Flexi-Coil (Australia) Pty Ltd* [1999] and *Subway Systems Australia Pty Ltd v Michael John Thorpe* [2000].

³ See amendment number 34 in Statutory Rules: Trade Practices (Industry Codes – Franchising) Amendment Regulations 2001 (No. 1) 2001 No. 165.

⁴ *Bolter v Superior Court* 104 Cal Rptr. 2d 888 (Mar. 9, 2001).

Assisting Compliance

The Commission is mindful of the cost of compliance and seeks to work with the industry and the FCA in particular to improve understanding and compliance with the Code.

The ACCC puts a lot of effort into consultation, participation in industry events such as expos and development of user friendly written material. Our publications include:

- The Franchisee Guide which focuses on franchisee obligations and rights under the Code.
- The Franchising Compliance Manual which assists small to medium size franchisors in particular.

We aim for these products to complement the practical guides produced by the FCA. Both these ACCC publications have been revised recently and updated versions are expected to be released soon. They will be available on the ACCC website (www.accc.gov.au) as is the latest version of the Franchising Code.

Assessing Performance

The Franchising Code of Conduct is seen by other business groups as an example of what could apply to them. There have been approaches to the Commission and Government from the private sector asking about a similar mechanism to foster better business practices and investor confidence. As you know the preference of the present government is to support self regulatory Codes and only to default to mandatory Codes if the self regulation approach is not working.

In its involvement with Codes, the Commission recently reviewed the voluntary Cinema Code. We are also actively involved in raising awareness across Australia of the voluntary Retail Grocery Industry Code of Conduct, particularly its application to the supply of fresh produce to processors and the major retail chains. The Commission also recently has been made aware of suggestions for a national uniform retail tenancy Code.

In a way it can be said the franchising sector leads the game. You have a Code that is working and you have a good industry image.

Due to the cooperation and common sense displayed by your industry in supporting the Code you have made the regulator's role more constructive in assisting investors and the industry as a whole.

Conclusion

Franchising remains the major pipeline for successful and growing small business.

The peripheral “dodgy” operators are coming under increasing pressure and steadily being weeded out.

My own experience has revealed franchisors who are in the main professional, innovative, proud of their achievements and highly supportive of their franchisees. This is a great recipe for continued success.

The ACCC looks forward to continuing to work constructively with the franchising sector.