

## Changes to the Franchise Code

Following the release of the Fairness in Franchising Report and industry consultation, the Australian government has made some changes to the Franchise Code of Conduct (**the Franchise Code**) which will be implemented from 1 July 2021. This article will step you through the most significant of these changes, including changes to:

1. Cooling-off periods;
2. Good faith termination;
3. Disclosure obligations
4. Lease and occupancy rights;
5. Passing on legal costs;
6. Dispute resolution mechanisms;
7. Capital expenditure; and
8. General terms.

### Cooling-off Periods

Under the new Franchise Code, the standard cooling-off period has been increased from within 7 to 14 days of entering into the agreement.

Franchisors should also be mindful that the cooling-off period restarts when a franchisee assigns or transfers their interest under the franchise agreement to a new franchisee. In these circumstances, the new franchisee will have 14 days from either becoming the franchisee or taking possession and control (whichever is earliest) to:

1. Cease to be the franchisee;
2. If the old franchisee can become the franchisee for those purposes again - cause the old franchisee to do so; or
3. If there was a transfer agreement in place between the new and old franchisees - terminate that agreement.

If the new franchisee ceases to be a franchisee, the franchisor must refund all payments, made by the new franchiser, less reasonably incurred expenses - which may be something to keep in mind when spending money in anticipation of a new franchisee coming on board.

## Good Faith Termination

Good faith obligations have taken on new significance in the updated Franchise Code as the franchisee is now entitled to propose to terminate the franchise agreement at any time. If given such a proposal, the franchisor must respond in good faith to the written proposal within 28 days by either agreeing to the termination or providing written reasons for their refusal. Although the Franchise Code stipulates that the obligation to act in good faith does not prevent a party from acting in their legitimate commercial interests, in practice the obligation to act in good faith may limit the circumstances in which a franchisor is entitled to reject a termination proposal.

## Lease and Occupancy Rights

Where the franchisor or an associate of the franchisor proposes to lease or licence the premises to the franchisee, the franchisee now has further termination rights. In these circumstances, the franchisee will have the right to terminate within 14 days of:

1. Receiving the first document setting out the terms of the proposed lease or occupancy right;
2. Receiving any further documents setting out the terms which are not substantially identical to the terms of the first document (provided the changes were not requested by the franchisee); or
3. Entering into the lease, if they were not provided a document setting out the terms of the proposed lease or occupancy right which are substantially identical to the actual agreement.

In light of this new termination right, it is particularly important that franchisors who intend to lease or license premises to the franchisee fully comply with their disclosure obligations.

## Disclosure Obligations

Before providing any substantive disclosure, a franchisor must provide prospective franchisees with a copy of the Information Statement Relating to Franchising, which that is [published on the Commission's website](#).

The updated Franchise Code has introduced two new disclosure requirements, meaning that franchisors will now also need to disclose:

1. The Key Fact Sheet, which franchisors will be able to generate using a template which will be published on the ACCC website; and
2. If the franchisor or their associate plans on leasing premises to the franchisee, a copy of the lease for the premises or a summary of the commercial terms of the lease.

Disclosure may now be made in printed or electronic form, depending on which form the franchisee requests.

## Passing On Legal Costs

Under the new Franchise Code, the general rule is that franchisors must not require the franchisee or their associate to pay the legal costs associated with entering into a franchise agreement. However, a franchisor can pass on some of these legal costs if they include in the franchise agreement:

1. The fixed sum payment for legal costs;
2. A statement that the payment is for the franchisor's costs of legal services relating to preparing, negotiating or executing the agreement; and
3. A statement that the sum does not include any amount for the franchisor's costs of legal services that will or may be provided, after the franchise agreement is entered into, in relation to preparing, negotiating or executing other documents.

Alternatively, franchisors may wish to increase the overall franchise fee to incorporate legal costs.

## Dispute Resolution Process

Under the new Franchise Code, the options available to parties to a dispute are:

Options	Process	Available under the Franchise Code?
<b>Mediation</b>	The parties meet with an impartial third party who helps facilitate a resolution to the dispute	Yes - ADR Process
<b>Conciliation</b>	The parties meet with an impartial third party who facilitates discussion and draws upon their expertise to suggest solutions to the dispute	Yes - ADR Process
<b>Arbitration</b>	The parties present their perspectives on the dispute and the arbitrator imposes a final resolution to the dispute which is contractually binding on the parties	Only available if the parties have entered into a written agreement stipulating arbitration as the dispute resolution mechanism

The Franchise Code now also specifies that ADR can be conducted using virtual attendance technology, which will hopefully improve convenience for parties and minimise disruption due to COVID-19.

## Capital Expenditure

The rules surrounding capital expenditure have also changed, with franchisors no longer able to require capital expenditure on the basis that franchisor believes the expenditure is reasonably necessary and has justified it with a written statement. In practice, this means that if a franchisor wants their franchisees to incur a capital expense they will need to seek consent from franchisees or ensure the expense is disclosed prior to the signing of a new or extended franchise agreement.

Relatedly, to enhance accountability franchisors who collect funds from franchisees for marketing and advertising purposes will now need to prepare an audited financial statement annually unless 75% of the franchisees vote to waive the auditing requirements.

## General Terms

Restraint of trade clauses will now be construed more narrowly under the Franchise Code as restraints will now only be effective if the franchisee was in serious breach immediately prior to the expiry of the franchise agreement. The Franchise Code has not defined 'serious' as this may vary from industry to industry, but has specified that this change is intended to ensure that franchisees who have committed minor, procedural breaches are not hampered with restraints of trade.

## Key Takeaways

It is impossible to assess the full affects that the updates to the Franchise Code will have at this early stage. However, in the meantime we recommend that franchisors be mindful of the following:

1. In light of the changes to cooling-off periods, franchisors should be vigilant regarding their expenditure prior to and during this period as they may be required to refund franchisee fees upon termination;
2. Good faith obligations may affect the grounds on which franchisors can refuse to accept a termination proposal by a franchisee;
3. Disclosure is vitally important and may affect the franchisee's right to terminate, particularly in circumstances where the franchisor or their associate plan to lease or license premises to the franchisee;
4. If franchisors want prospective franchisees to cover part of the legal costs associated with entering into the franchise agreement, they will either need to specify a fixed sum in the franchise agreement or incorporate the costs into their overall franchise fee; and
5. Parties can now opt-in to the arbitration process through their franchise agreements.

The information contained in this article is general in nature only. Please contact Rouse Lawyers if you wish discuss in more detail.