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Franchising Review Secretariat Unit
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ALNA Submission to the Review of the Franchising Code of Conduct

The Australian Lottery and Newsagents Association (ALNA) is a not-for-profit organisation and is the peak industry body that provides advocacy and support services to our member newsagents, news distributors and lottery agents nationally.

ALNA represents one of the largest individual franchisee membership groups as we represent many lottery agents, who collectively make up one of the largest retail franchisee groups in the country with approximately 4000+ franchisees nationally.

As such ALNA has a strong interest in the efficient and equitable operation of franchising in Australia as a considerable number of our members are involved in multiple franchise systems including lotteries and marketing/banner groups, and we are pleased to have the opportunity to contribute to this important review.

The conduct and culture of franchising in our sector is generally exceptionally good and this demonstrated culture continues to improve over time, with the code playing an important and overarching role in moderating behaviours and improving guidance for all parties, which is helpful.

ALNA works closely with all the franchisors in our sector, and they continue to be very reliable and valued partners for our small business members. Our commentary for this review is based on members feedback on the issues that concern them with their franchises and it is directed at improvements to the operation of the code to make it more useful and effective for our members and other stakeholders. We want to ensure the Franchising Code continues to deliver a fairer and more equitable business environment, whilst enhancing its effectiveness and ability to adapt and change as the sector does. Our comments are informed by member feedback, previous reviews and outcomes, as well as considering edge cases and case studies that provide useful insights on how we can improve the whole sector with more win-win outcomes more often.

Whilst we acknowledge the importance of Franchising Code review consultations, the timing of this consultation and the relatively short window for submissions, is not particularly helpful for associations like ours who represent many franchisees and who have limited resources to apply to a range of important but competing issues.

This makes planning for these reviews, along with proper lead times critical for our ability to completely respond. As such we have included a section in this review, that if adopted, would deliver a

more strategic and planned approach to future reviews, which we believe would result in greater engagement and better outcomes.

In addition to this, we have focussed our attention on the questions we believe most impact our franchisee member base, for example, dispute resolution processes for matters not resolved at conciliation or mediation, digital migration, and network expansion strategies including non-exclusive franchisor territory policies.

We appreciate the government taking on board our views to inform the Review of the Franchising Code of Conduct which should result in positive changes to the Code. We also welcome the opportunity to meet with you to discuss our submission in more detail.

Yours sincerely,



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ALNA Submission to the Review of the Franchising Code of Conduct

ALNA has responded to only the most relevant questions for our membership in the consultation, as outlined below:

General Questions

1. *Are there any general observations you want to make about the regulatory framework?*

Franchising Code Review Mechanism

ALNA believes the new Franchising Code needs a Review Mechanism included for fixing a schedule of planned reviews to every 3-5 years. We believe this will deliver a more planned approach to future reviews and provide expectantly better outcomes.

Effective planning is critical and when you invest time and effort into planning something thoroughly, you are more likely to achieve your goals or objectives successfully.

Six weeks to respond to a request for review may seem like adequate time, but this is not necessarily the case when associations like ours who are not dissimilar to many small businesses themselves, have multiple competing requests for reviews, consultations, and submissions to prepare. Furthermore, to properly respond to this important review ALNA would normally consult our franchisee membership through multiple engagement models, which takes time to coordinate.

In addition to representing many lottery agents, who collectively make up one of the largest retail franchise groups in the country, we also represent a range of other retail channels including distributors, newsagents, convenience, tobacco, and chemists.

In the last year alone, ALNA has responded to the following reviews and consultations relating to lotteries plus more on other subjects, with some requiring multiple review stages, responding to hearings and follow up submissions.

- Federal Consultation Paper - Legislating to ban the use of credit cards for online wagering
- House of Representatives' Standing Committee on Social Policy and Legal Affairs inquiry and report on online gambling
- South Australia - Gambling Codes of Practice Consultation
- Review of gambling legislation in Western Australia
- AusPayNet – Consultation on the gaming industry's use of cheques
- Franchising Code review
- Lottery Licence – Commission Review Mechanism (National Review managed through Victorian Licence)

All of these reviews, consultations, and submissions appear to operate in a vacuum and do not consider the other priorities imposed on small business association stakeholders, often at the same time. This level of unplanned activity can affect our ability to prepare comprehensive and meaningful submissions, especially when they have tight timeframes to respond to.

We are not a single sector association, and we cover a broad spectrum of industries, which means we need to respond to a significant number of reviews and consultations every year with a limited budget and resources. As a not for profit, we do not have the ability to engage expensive lawyers and consultants to assist us with these reviews and submissions.

ALNA develops annual business and operational plans and longer term (3-5 year) strategic plans, but all of these reviews have to be managed on top of our planned activities as they are often thrust upon us without warning and with limited time to respond.

Ahead of this review and to help achieve better outcomes from the reviews, ALNA has been advocating for the adoption of a Review Mechanism for fixing a schedule of planned reviews of the Franchise Code with industry stakeholders, which to date has been met with positive responses.

This is supported by the Foreword comments in this review. *“Throughout its evolution, the franchising sector in Australia has encountered challenges that necessitate periodic reviews and adaptations of the regulatory landscape. The government’s commitment to fostering a competitive and fair business environment is reflected in regular reviews of the Franchising Code of Conduct, aimed at refining, and enhancing its effectiveness.”*

We strongly believe there are significant advantages and likely better outcomes to having fixed reviews including:

- Most reviews are forced on the industry, and they are either politically (change of government) or complaint or crisis driven and can catch stakeholders off-guard. Stakeholders can then become defensive, dissatisfied, and unsupportive and the review process can become counterproductive very quickly. When this occurs the most important stakeholders (franchisors & franchisees) can lose control of the outcomes and have unwanted regulations imposed on them with unintended consequences.
- Fixed reviews embedded in the new Franchising Code would allow for a more small business centric lens and ensure all stakeholders are not caught off guard and they could plan and prepare properly, and this should make the reviews more productive and more collaborative.
- The reviews would be more regular than the current political cycles and will put the process in the hands of the industry (where it belongs). This will likely limit the need for politicians to add this to their list of commitments when heading to an election.
- Recurring reviews would mean more regular reviews, and this is likely to result in a smaller suite of changes being sought and a faster process. That should make the process more efficient and more responsive to industry changes.
- It would allow key stakeholders the opportunity to work together in advance of the formal review to put together a list of outstanding or emerging franchising issues and recommended solutions based on compromised or agreed positions where possible.
 - Any predetermined review schedule and process should encourage stakeholders to work together prior to the next review, which will help guard against solutions being imposed on them.
 - In fact, the regulators (like ACCC) through their current Small Business and Franchising Consultative Committee could facilitate these consultations and help formulate recommendations to government for the next review.
 - Of course, where agreement could not be reached both parties (as they do now) could present their respective cases and note any areas of disagreement.
- Under the current ad-hoc review program, the issues to be reviewed are often imposed on stakeholders by the government of the day or regulators, whereas a planned approach might help the industry do some self-diagnosis and facilitate their identification of key issues in advance and allow them time to be prepared with remedies that all stakeholders could agree on.
- Currently the ad-hoc timetable for reviews and tight timeframes disadvantage the very people the Franchising Code is designed to protect, individual franchisees. A known schedule of reviews and greater lead times will help individual franchisees prepare submissions and consult their representative bodies if required.
- Short timeframes following release of the terms of reference means already busy stakeholders will prioritise and limit their responses based on their available time. For this very reason, ALNA has only commented on a small number of the issues raised in this review. Longer timeframes would result in greater engagement and input into the process.
- The Franchising Code review process should require all parties to act in good faith.

- Naturally, this review process would not limit the responsible Ministers ability to call a review out of cycle if urgent changes were required, or to include terms of reference they require but it is hoped this would not be as necessary.

As we have experienced in the past, reviews take quite some time from inception to completion. The last review was initiated in 2018 and there would have been a period of lobbying before the review was instigated. As a result, in 2019 the Parliamentary Joint Committee on Corporations and Financial Services published its Fairness in Franchising Report, which included over 70 recommendations designed to level the playing field between franchisors and franchisees in Australia. Following consultations, the Australian Government then released amendments to the Franchising Code on 1 June 2021, with some changes given more time to implement. It should not take this long to implement a review and changes.

We believe there is an opportunity on the expiration of the current Franchising Code and commencement of a new Code in April 2025 to embed a set number of reviews within the Franchising Code.

Case Study Example

As part of the Victorian Lottery Licence renewal process ALNA successfully argued that the Lottery Licence should include a mechanism to require the franchisor to complete a number of retailer commission reviews over the term of the Lottery Licence (10 years). A Commission Review Mechanism (CRM) was included in the Lottery Licence.

This fixed review process has been very successful. Following the first CRM the franchisor introduced the new Remuneration Program which has resulted in over \$20m in additional commissions being paid to franchisees annually and the opportunity to participate in the digital channel for the first time (online omni-channel commissions).

The second CRM resulted in a step change increase in lottery retailer revenue with a significant uplift in commissions occurring after this from 10.3% to 12.3% and doubling of online omni-channel commissions. These were great outcomes for franchisees and an increase unlike any seen before. These planned reviews have enabled key stakeholders to work together in a proactive, well planned, and constructive manner and this has delivered excellent results.

The CRM minimum requirements stipulate the commission reviews should:

- *Take place no less than three times during the term of the Licence;*
- *Be genuinely consultative and take into account the views of Distributors (Retailers/franchisees);*
- *Consider whether the commission reasonably rewards Distributors for their role in the conduct of Public Lotteries; and*
- *Be undertaken immediately before any application to the Minister for approval of the maximum commission rate.*

The CRM sets out the frequency of the formal reviews and requires the franchisor to conduct 4 commission reviews between 2018 and 2027 (one prior to the Licence commencement).

Formal reviews must be conducted by the franchisor prior to:

- *30 June 2018 with the review and consultation process with Distributors to commence no later than 1 January 2018 and then prior to 30 June 2021, 30 June 2024, and 30 June 2027.*

As part of the CRM, the consultation process must include meetings, representatives of and representations from the representative bodies such as ALNA. The CRM involves the franchisor inviting written submissions from ALNA, as a representative body, and from individual franchisees who are not members of a representative body.

The CRM requires the franchisor to genuinely consider whether rates of commission reasonably reward franchisees for their role in the Victorian lottery system. It does require the franchisor to have regard to a range of factors (13 of which are specified i.e., the performance of Distributors and importance of Authorised Public Lotteries to the viability of the business of Distributors and other business and economic factors), and to provide reasons for any decision to the relevant Minister.

The review process is required to be open and transparent such that representative bodies and individual franchisees should be able to form a view as to the conduct of the franchisor in making its review determinations.

Franchising Code Review Mechanism Implementation

ALNA believes there is a rare opportunity for the new Franchising Code to include a Review Mechanism that locks in a series of reviews (every 3-5 years) over the life of the regulation and set out the process to be undertaken for future reviews, the general terms of reference and range of factors that should be considered.

Historically Franchising Code reviews have included similar terms of reference including reviewing the scope of franchising regulation, the process for entering into a franchise agreement (FA) and disclosure, capital expenditure, end of term arrangements, termination or early exit of the FA, compliance, enforcement, and dispute resolution, etc.

These could be drafted into a suite of standard terms of reference for the future reviews, along with the timeframes, participants, and the process to be followed. This should not limit the ability of the government to limit future review scopes to part of the standard terms of reference or increase focus on some areas or add new areas. A more detailed and specific terms of reference can be determined and communicated closer to the set review. Like the current Franchising Code review the terms of reference do not limit the participants ability to comment on other issues that matter to them.

As mentioned above, the regulators (like ACCC) through their current Small Business and Franchising Consultative Committee could facilitate stakeholder consultations and help formulate recommendations to government for the next review.

There are examples of industry advisory bodies such as the Responsible Gambling Ministerial Advisory Council (RGMAC) in Victoria. The Victorian Government, through the Minister, seeks the council's advice on how to ensure the Victorian gambling industry operates responsibly and sustainably, in a way that minimises the harm from problem gambling, while creating an environment where those who gamble safely are permitted to do so.

Members are drawn mainly from industry, academia, local government, and community groups, and reflect a diverse range of skills, backgrounds, and expertise. Members are appointed based on their understanding of gambling and community issues, their understanding of public policy and their ability to contribute constructively to the work of the council.

The council's work is not necessarily about achieving consensus, but rather helping to inform decisions and to identify areas where members agree and those areas where agreement cannot be reached. These divergent views are recorded in the advice provided to the Minister but in most cases, it enables the Minister to adopt regulatory changes that will be more broadly accepted by all industry participants.

2. *Is the Franchising Code fit for purpose? Should it be retained? If so, should it be remade prior to sunseting?*

ALNA strongly believes the Franchising Code should be retained primarily in its current form, but there is an opportunity to make some changes to ensure it remains fit for purpose and to finish some work started in the last review that did not go far enough and did not fully level the playing field for franchisees e.g., dispute resolution for matters not resolved at conciliation or mediation. There are also some structural changes that can be made to facilitate more regular and planned reviews to ensure the Franchising Code continues to deliver a fairer and more equitable business environment, whilst enhancing its effectiveness and ability to adapt and change as the sector does.

3. *Are there any emerging trends, such as technology or cultural innovations, which would affect the operation of the Franchising Code?*

Digital Migration

Traditional retail franchise networks play a critical role in building customers trust in the franchisors brand and overall business growth both instore and digitally. Franchisees should always be fairly rewarded for their foundational and ongoing investment in capitalising the physical brand through their retail stores and customer service delivery.

With the rapid growth of retail channel sales in digital, which was supercharged through the pandemic, the Franchising Code may need to adapt and be expanded to deal with this sector change.

Ideally, the Franchise Code would prohibit franchisors from any activities that seek to exclude franchisees from digital opportunities or exploit them for themselves only. It should be incumbent on franchisors to always consider their franchisees by rewarding them for their contribution and helping them to successfully transition to the changing economic and digital environment.

Furthermore, consideration should be given to the Franchising Code setting best practice guidelines around how franchisors can equitably and fairly capitalise on these structural changes or growth opportunities by working in partnership with their franchisees.

This can be achieved by the code encouraging franchisors to develop genuine omni-channel model strategies, as we have positively seen occurring in the lotteries sector, which include and fairly reward their traditional and sometimes foundational retail franchisee channels for their ongoing contribution.

For example, franchisors should not be permitted to run exclusive digital sales channels without allowing franchisees the option to participate, or fairly rewarding them for their contribution to these channels and their growth. This may include developing suitable models that allow franchisees to sell the franchisors products digitally from their own websites and revenue sharing programs.

If this is not possible within the Franchising Code, at a minimum there should be a requirement for greater disclosure by franchisors about any exclusive activity and their forward plans. Critically, it should include information on the historical, current, and forecast sales performance of these channels and impacts on the franchisee channel e.g., sales migration and cannibalisation.

Questions – The scope of regulation

4. *Does the general scope of coverage of the Franchising Code remain appropriate? Is the scope of coverage flexible enough having regard to the diversity of the franchising industry?*

In general terms the coverage of the Franchising Code remains appropriate, however we believe the ACCC could have a more active role in assisting franchisees especially in dealing with disputes.

The Franchising Code review amendments included some changes relating to disputes, but we do not believe they went far enough, and they have not entirely levelled the playing field for franchisees, particularly for disputes that are not resolved at mediation. We believe it is appropriate to address these outstanding issues now and put in measures to ensure all parties act in good faith during disputes.

The Franchising Code provides a two-step process for resolving disputes, firstly internal dispute resolution (using the franchisor's established system) and secondly, Alternative Dispute Resolution (ADR) processes (an ADR process under the Code means conciliation or mediation). This process is normally facilitated by the Australian Small Business and Family Enterprise Ombudsman ASBFEO), or the various State based Small Business Commissioners offices where they exist.

Our aim is for the Franchising Code to provide greater guidance and support for disputes that are not resolved prior to or during the conciliation or mediation stage above. These are unresolved disputes.

Currently, for unresolved disputes at mediation under the ASBFEO franchising disputes process, if the parties agree in writing that arbitration can resolve the dispute or parts of the dispute, the ASBFEO will appoint an agreed arbitrator or independent arbitrator. Other than the arbitrator reporting back to the ASBFEO following the completed process and the parties being asked to complete a satisfaction survey, there does not appear to be any further assistance or support offered to the franchisees (no further advice or financial assistance).

ALNA will explore this further in the submission and provide some alternative dispute resolution models for unresolved disputes which lead to arbitration and an alternative model. We will also highlight where improvements can be made to existing arbitration models to ensure they are fit for purpose, should they be adopted by the Franchising Code.

Questions – Before entering into a franchise agreement.

8. *How effective are the requirements of the Franchising Code that ensure franchisors make information available to franchisees prior to entry into a franchise agreement? If possible, please comment on the effectiveness and content required for inclusion in each of the Franchise Disclosure Register, Information Statement, Key Facts Sheet and Disclosure Document.*

Franchise Disclosure Register

ALNA understands there will be a further opportunity to provide feedback on the operation of the Register in November this year, but we would like to provide some initial feedback now.

ALNA believes the current Franchise Disclosure Register can be improved significantly. The current Register gives prospective franchise buyers, current franchisees and professional advisers access to information that is important to know when making business decisions, but unfortunately, without measuring or ranking franchisors against any of the information provided or any other objective criteria, the information provided is deficient.

The Register has been established to increase franchisor transparency and provide access to disclosure information that can assist prospective franchise buyers to make an informed decision before entering a franchise agreement, but critically, it does not provide any real insights into how one franchise compares to another, or who would be considered the 'best franchisors' amongst their peers.

The Register should provide some insights, benchmarking or ranking based on collective feedback from existing franchisees in that system and against the information already disclosed in the Register. In addition, this could include a range of objective criteria, best

practice franchising standards and other performance measures that a potential franchisee could consider as a checklist against potential franchise models..

The website specifically states the Register or Government does not endorse any franchisor. Endorsement may not be necessary but some easily accessible assessment against some established criteria would be very helpful to prospective franchisees.

We believe the franchisor information on the Register is provided directly by franchisors without any form of filtering, review, or assessment for completeness (other than identifying information not provided) e.g., there is no assessment on whether the franchisors overall business model, especially relating to its treatment of franchisees is best practice or the Franchise Agreements are comparatively fair, or how they rank overall when compared to other franchise systems.

As mentioned above, the effectiveness of the Register would be improved markedly if it provided some analysis of the franchisor's performance across the already disclosed information (and some additional information) and other criteria developed to deliver some sort of ranking system.

It could be similar to the hospitality 5 Star rating system, but instead of just being based on customer feedback (in this case franchisees rating their franchisor) it could also include a range of assessment criteria.

For example, do they offer good support services such as training and development (in addition to induction training), or business development support and compliance assistance programs (employment relations advice including pay obligations), does the franchisor offer a marketing fund, do they offer exclusive territories, does it operate a genuine omni-channel sales and revenue share model to partner with franchisees, or have they been involved in a lot of disputes with franchisees and how many were resolved, etc.

Once established a rating or category system linked to the code would encourage franchisors to raise their standards and practices to ultimately improve their ranking and this would help prospective franchisees make a more informed decision.

ALNA would be happy to work with the government on the identification and establishment of the assessment criteria and scoring methodology to ensure it delivers meaningful and fair outcomes.

Non-Exclusive Territory Disclosure

ALNA has long advocated that all franchisors should provide franchisees with some surety over their substantial investments in the franchise (lease, franchise establishment costs, royalty fees, retail fit-out, etc.) by offering exclusive franchise territories like those provided by many retail franchisors.

These territories provide guarantees and protections to the franchisee by ensuring the franchisor will not establish another business, either itself or grant rights to a third party, in the exclusive zone as defined by the franchisor.

Non-exclusive franchise distribution models can undermine a franchisees revenue security, certainty, and confidence, and they are very powerful influencers of a retailer's perceptions about their franchisor and the system.

We believe that strategies and policies the franchisor adopts for the franchise system should be passed through the lens of protecting and enhancing the wellbeing of the existing network and not doing anything, including not creating any revenue traps that might harm an existing and loyal franchisees' business.

Expansion strategies are often adopted under the pretext of meeting customer demand and driving incremental sales revenue for the franchisor, but they do not always consider existing franchisees. These may be valid reasons, but we believe they should only be pursued when the strategy ensures no significant harm is done to existing franchisees or they are adequately protected or compensated as part of the strategy.

The Franchising Code expressly requires that during the term of a franchise agreement the franchisor must not require a franchisee to undertake significant capital expenditure unless it was disclosed to the franchisee in the Disclosure Document that they received before entering into, renewing, or extending their franchise agreement.

Amongst other important reasons this must be disclosed, is so prospective franchises can make an informed assessment on the expected returns on investment in the franchise business and its viability over time, etc. Capital expenditure can add to a franchisees' borrowing costs, impact cashflows and ultimately the profitability and viability of the business.

Things like capital expenditure that have a direct impact on a franchisee's revenue and viability, are not dissimilar to a franchisor doing something (creating a revenue trap) that could have unexpected and enduring detrimental impacts on a retailer's revenue and ultimately its viability, such as opening a new, or several new stores nearby.

We believe the Franchising Code needs to be expanded to address this matter in the same way disclosure is required for significant capital outlays. The Franchising Code may not be able to compel franchisors to offer exclusive territories, but it could require greater disclosure and suggest making them available is best practice franchising. In this submission we have talked about ranking franchisors through the Disclosure Register, and this should be a key criteria.

Generally speaking, franchisors will not disclose their network distribution growth strategies citing competitor concerns, however this reasoning can be both convenient and put franchisees at risk around a lack of suitable disclosure. Best practice examples should include providing a new outlet application process where existing franchisees are invited to lodge expressions of interest along with the open market for new site locations that have been identified for growth opportunities through transparent assessments, rather than accepting any application, and to comment on new site applications in their area before they are approved. Unfortunately, it is generally a one-way process for many franchisees now, they are not necessarily provided with the right to appeal or a fair hearing, because franchisees are often informed after the franchisor has decided to approve a new franchise application and it has advised and engaged contractually with the new franchisees. It is too late.

Often the advice provided by a franchisor that a new franchise within an existing franchisees trade area has been approved is very general and does not provide existing franchisees with any real insights into why the decision was made.

There is no disclosure about what the commercial analysis may have included, or what commercial criteria was used, or what being able to still obtain the benefit of their respective franchise agreements might mean, or what the likely impacts will be on the existing franchisees or whether this will be temporary or permanent impacts. This type of model makes broad assumptions about the impact and viability of the franchisees businesses without really knowing their financial circumstances and if they can sustain any loss of trade.

We have had rare examples where our members have had multiple new franchises approved in their trade area in succession without any understanding of the possible compounding impacts a second or third new franchise in addition to the first in the same trade area could have, and before the first is open and the financial impacts are realised. Even with the most sophisticated prediction models determining predictable impacts is impossible.

Each of these applications and subsequent approvals has widespread impacts on all of the affected franchisees in the area and this is an enormous distraction for worried franchisees, and it creates a wave of uncertainty over their business and its longer-term viability.

Over a long time, the franchising sector has faced scrutiny over fairness, most recently with the Parliamentary Joint Committee on Corporations and Financial Services (PJC) handing down its Fairness in Franchising report, which made 71 recommendations to improve the operation and the effectiveness of the franchising sector. In response the Australian Government has established an inter-agency Franchising Taskforce to implement a number of the committee's recommendations. The Government's actions are informed by the consultation and advice of the taskforce and are guided by seven core regulatory principles that strengthen protections for franchisees e.g. *"A healthy franchising model fosters mutually beneficial cooperation between the franchisor and the franchisee, with shared risk and reward, free from exploitation and conflicts of interest."*

It could be argued that not providing exclusive territories is not in accord with the new and evolving regulatory principles and is no longer a sustainable approach.

This is an example of a non-exclusive territory clause within a Franchise Agreement.

Territorial Rights Not Reserved

Under this Section, the permission given by the Franchisor to the Franchisee doesn't provide any unique rights to a specific region. On entering this Contract, the Franchisee recognises and concurs that the Franchisor retains the liberty to authorise others to function under the Franchise Model anywhere, irrespective of its nearness to the Outlet.

This Contract does not, in any manner, convey a commitment from the Franchisor to the Franchisee of any territorial exclusivity linked to the Outlet's location, be it in terms of area or duration. Additionally:

(a) The Franchisor, on its own or via a representative, can promote Products or different items online or through other channels they see fit; and (b) Beyond the stipulations of this Contract, the Franchisee won't be accorded any monetary benefits or compensation tied to transactions as mentioned in this Section.

These sorts of clauses allow franchisors to expand at will without having to justify why they are doing it or to consider or explain the possible detrimental financial the impacts on existing franchisees.

If franchisors do not offer exclusive territories, they should be required to disclose much more than just “*where the franchise is planning to expand*” which is usually answered in the Register with a general statement like *NSW, VIC*.

In addition to disclosing prominently the specific Non-Exclusive Territory clauses in their Franchise Agreement, franchisor disclosure should also include information about their specific distribution plans and the possible future financial impacts on the franchisee’s businesses.

If exclusive territories are not offered the required disclosure may include:

- Where is the franchisor planning to expand?
- What number of new franchises is the franchisor planning to open?
- Are there any specific areas the franchisor is planning to expand into e.g., growth corridors?
- Are there any new channels the franchisor is planning to expand into and how many sites are they contemplating and in what jurisdictions and sub regions?
- What is the franchisors net increase in franchises planned per annum or are they just maintaining current numbers?
- Typically, what have the sales cannibalisation impact ranges experienced by existing franchisees been when new franchisees are opened within existing trade areas and are they enduring?
- What is the commercial criteria for opening a new franchise?
- Does the franchisor use comprehensive new franchise prediction modelling tools based on existing franchisee data?
- Does the franchisor use financial modelling to ensure both the existing franchisees and new franchisees are able to obtain the benefit from their respective franchise agreements and what is the financial criteria e.g., what does the franchisor believe are acceptable rates of cannibalisation? Does the franchisor understand the typical % debt load and servicing arrangements of their franchisees.
- Does the franchisor offer any mechanism or processes to allow exiting franchisees to bid for or comment on new franchises before they are approved/opened?
- Does the franchisor offer any mechanisms for calculating and paying compensation if the detrimental impacts of a new franchise (or multiple new franchises) in a trade area exceeds their financial prediction modelling or assumptions i.e., their acceptable (and what should be disclosed) cannibalisation rates and longer-term impacts on existing franchisees?

This compensation could be a temporary reduction in franchise fees for as long as the loss is experienced by the existing franchisees and in extreme cases where the existing franchisees viability is threatened and they are forced to sell, the franchisor paying compensation for the lost good will and sale value of the business and the franchisor offering buyout options.

Questions – Enforcement and dispute resolution

Dispute resolution

12. Do the dispute resolution provisions in the Code provide an effective framework for the resolution of disputes? In particular, are you aware of whether 2021 reforms relating to multi-party dispute resolution and voluntary arbitration have been utilised by participants in the franchising sector? If not, why not?

Dispute Resolution

In 2019 the Parliamentary Joint Committee on Corporations and Financial Services published its Fairness in Franchising Report, which included over 70 recommendations designed to level the playing field between franchisors and franchisees in Australia. Following consultations, the Australian Government then released amendments to the Franchising Code of Conduct (Franchising Code) on 1 June 2021, with some changes given more time to implement.

The Franchising Code amendments included some changes relating to disputes, but we do not believe they went far enough, and they have not levelled the playing field for franchisees, particularly for disputes that are not resolved at mediation. The Franchising Code has not been reviewed since and we believe it is appropriate to address these outstanding issues in this review.

The Code provides a two-step process for resolving disputes, firstly internal dispute resolution (using the franchisor's established system) and secondly, Alternative Dispute Resolution (ADR) processes (an ADR process under the Code means conciliation or mediation).

Our main objective is to address disputes that are not resolved prior to or during the conciliation or mediation stage. These are unresolved disputes.

Supporting the procedures and requirements set out in the Franchising Code, we note the Australian Small Business and Family Enterprise Ombudsman (ASBFEO) office provides information on the dispute resolution process in the Code and assistance in resolving disputes. This includes free initial and pre-mediation assistance (to try and resolve the dispute) and alternative dispute resolution processes under the Franchising Code such as referrals where costs are shared e.g., provides access to an ADR practitioner or arbitrator. ASBFEO suggests, on average mediation costs around \$4,000 (\$2,000 per party for two parties to the dispute).

For unresolved disputes at mediation under the ASBFEO franchising disputes process, if the parties agree in writing that arbitration can resolve the dispute or parts of the dispute, ASBFEO will appoint agreed arbitrator or independent arbitrator. From that point the arbitrator will manage the process. Other than the arbitrator reporting back to the ASBFEO following the completed process and the parties being asked to complete a satisfaction survey, there does not appear to be any further assistance or support offered to the franchisees (no further advice or financial assistance).

In a recent dispute and mediation between a member and their franchisor facilitated through the ASBFEO, the total cost to the franchisee was closer to \$5000.00 (\$2,000 per

party, airfares, and accommodation) which is too much for a small business, especially as the dispute was not resolved.

In most States we refer members to their Small Business Commission first so they can benefit from the subsidised dispute resolution services. As a result, we believe most franchisees will use their Small Business Commission service and the number of cases actively managed relating to franchising through the ASBFEO is likely to be understated nationally. QLD, the ACT and NT do not offer subsidised dispute resolution services through a Small Business Commission service which makes alternative dispute resolution cost prohibitive there when compared to other States.

The subsidised State Small Business Commission services generally offer free preliminary help and free pre-mediation assistance, and subsidised low-cost mediation services e.g., for most commercial disputes in Victoria the Small Business Commission provide mediation services where each party pays \$195 for a half-day mediation session or \$390 for a whole-day session, making it a very low-cost alternative to litigation. If settlement is not achieved, mediation ends and either party might request a certificate to take the matter to the Victorian Civil and Administrative Tribunal (VCAT). Unfortunately, and just like the ASBFEO, the Small Business Commissions do not offer any further assistance beyond this point.

Most franchising disputes that are unresolved at mediation never go beyond this point because the cost of litigation and associated risks for the franchisee (lawyers and possible cost orders) are too great.

Franchisees have long called for dispute resolution processes that can assist them when they are unable to resolve a dispute at mediation i.e., a cost effective and fair arbitration process that levels the playing field for the franchisees. To our knowledge There has only been one example of this type of process implemented to date.

Following we will examine this arbitrated dispute resolution process, its failings and needed improvements before it was adopted nationally, and we will offer another option for the Franchising Code reviews consideration.

Case Study and Alternative Dispute Resolution Processes

In 2018 as part of the Victorian Lottery Licence awarding process ALNA advocated successfully for an arbitrated dispute resolution process to be included in the Lottery Licence.

ALNA argued that the Franchising Code did not adequately protect franchisees and did not provide an equitable process to progress disputes that were not resolved through mediation. Also, that there remained a significant power imbalance between a large corporation (franchisor) and individual small business (franchisee/distributor).

The State Government agreed, and the Public Lottery Licence granted to the Lottery Operator (franchisor) creates an obligation on the franchisor to ensure that the Dispute Resolution Process (DRP) described in Schedule 3 of the Licence is incorporated into the Franchise Agreement between the franchisor and its franchisees.

The benefits and objectives of the DRP process:

- The DRP helps address the significant power imbalance currently experienced between franchisors and franchisees.
- The DRP is in addition to the regime contained in the Franchising Code and includes an arbitration process.
- The DRP is more favourable to franchisees than the process provided for under the Franchising Code (for example, the process attributes some process costs to the franchisor and prevents it from initiating legal action – the Franchising Code does neither).
- The franchisee has absolute discretion as to which dispute resolution process it wishes to use (the Franchising Code or the DRP).
- Generally speaking, the franchisor must bear the costs associated with the dispute resolution process itself i.e., costs of mediator / arbitrator, etc. However, this does not include a Distributor's legal or industry representation and advice with respect to the dispute resolution process, and some other costs.
- The Franchise Agreement must continue to be performed during the dispute resolution process.
- The parties can agree to modify the dispute resolution process if it suits them to do so having regard to the nature of the dispute and the size of the franchisee's business.
- The franchisee can effectively choose whether or not to involve lawyers during mediation – if the franchisee is not legally represented at mediation, the franchisor must not be so represented.
- The process involves representative bodies such as ALNA to support franchisees.

In 2022 the DRP was tested by a franchisee over a dispute about new lottery outlets being opened nearby to their outlet. Analysis of this test case revealed that the process did not meet its intended purpose from the franchisees perspective, which resulted in them withdrawing from the DRP without the dispute being heard at arbitration or being resolved.

This test case exposed a number of shortcomings from the franchisee's perspective in the DRP which are summarised following.

- The process relies on both parties following the process and acting in good faith, and in the intended spirit or purpose of the DRP.

In this case, the actual dispute was never heard at arbitration. The process for arbitration does not prevent either party from engaging high-end lawyers to represent them. The franchisee could not match the same level of legal representation as the franchisor in this instance and when also faced with a situation where a cost order was not ruled out, decided to not proceed further.

- The process can also take a long time and allows either party to drag the process out if they choose.

The dispute process does not limit the time for the dispute to be heard and it was projected that it could take approximately 9 months.

The franchisee argued the lengthy timeframe which could have expanded costs was a significant contributing factor to their decision to discontinue with the process.

- The DRP process relies on, and the arbitrator is bound by the Commercial Arbitration Act 2011 (CAA), which opened up the franchisee to a cost ruling and too much risk.

The DRP deals with costs for the proceedings but does not completely protect against a cost order. In this case, the arbitrator could, or would not provide any guidance on the effect of the Lottery Licence on the process, especially around the awarding of costs.

- The CAA states *“Unless otherwise agreed by the parties, the costs of an arbitration (including the fees and expenses of the arbitrator or arbitrators) are to be in the discretion of the arbitral tribunal.”* It could be argued that the signing of the Franchise Agreement between the parties (which includes the Lottery Licence DRP), means costs have already been *“otherwise agreed by the parties”*. Of course, this would also need to be tested, and that would be difficult and costly.

In summary, while the Dispute Resolution Process (DRP) had good intent, escalating costs, potential cost orders and time meant the dispute was ended by the franchisee without resolution.

To resolve these issues there needs to be some changes made to the Victorian Lottery Licence DRP, but we are not convinced all of the issues experienced can be resolved if the process still relies on the Commercial Arbitration Act 2011 (CAA).

Even if changes to the Lottery Licence DRP were possible now to address all of these issues, this would not benefit franchisees more generally unless a similar and improved process was adopted nationally within the Franchising Code.

If the Franchising Code adopted this process (or similar), the issues experienced in this case would need to be resolved by the new process.

As part of this solution the ASBFEO’s responsibility could be expanded to include an arbitration role which may enable some of these issues to be addressed.

If a similar Arbitration process to the arbitrated Lottery Licence DRP was adopted in the Franchising Code, there are some key areas that would need to be addressed to improve the process:

1. **Intent of the Franchising Code Process and Breaches of the Process** – the process should set out why it has been included in the Franchising Code and what its key purpose or intents are i.e., to protect franchisees from the evident power imbalance in disputes and to level the playing field, and provide a non-litigious, time and cost-effective dispute resolution process, that allows independent and binding (enforceable) dispute rulings to be made.

This would help Governments, Regulators, and participants (franchisors & franchisees) understand why it exists and provide some context and expectations for the participants when the process is used.

If the process makes references and has requirements that the participants must act in good faith, these requirements should be more explicit and detail what conduct or

breaches of the terms of the process during a dispute would be considered as not acting in good faith and what the penalty or remedy would be.

2. **Time to resolve Disputes** - there would need to be some specific requirements limiting the time taken for a whole dispute to be processed and resolved to minimise costs, which includes the arbitration component. This may be problematic as the process relies on external Arbitrators and different complaints will have different levels of complexity.

As a minimum the Franchising Code process could state that either party must not deliberately use intimidatory, litigious, negligent, frivolous, or vexatious tactics to delay the process. It could also set out what would be a 'reasonable time' for a dispute to be resolved.

3. **Seeking a Costs Order** – the Franchising Code process would need an explicit statement prohibiting either party, from seeking a costs order at any time during or after a dispute is resolved or unresolved.

Again, this could be problematic because once the dispute moves to Arbitration it falls under the Commercial Arbitration Act 2011 (CAA). A solution could be that the Franchising Code process may need to require the participants to make a declaration to the Arbitrator (at the commencement) that there is an existing agreement between the parties that neither party will seek a costs order irrespective of the dispute outcome (i.e., it is otherwise agreed by the parties).

4. **Lawyer Representation** – the Franchising Code process including the arbitration component should both limit legal representation. If the franchisee elects not to have legal representation during the conciliation or mediation conducted, the franchisor agrees that it will not be accompanied by a legal representative at such mediation.

In regard to the proposed Arbitration process and circumstances where the franchisee needs to engage a lawyer, the franchisor should be permitted also, but this level of representation must have regard to the size and nature of the franchisees business and the dispute.

5. **The Commercial Arbitration Act 2011 (CAA)** – for a process that relies on the CAA to work, it is critical that the Franchising Code provides clear directives on what takes precedence, the Franchising Code, or the CAA. Ideally the Franchising Code.

As demonstrated above, the Lottery Licence arbitrated DRP process was well intended but, it has some unintended shortcomings and because it is tied to the CAA it is burdened with issues around precedence, uncertainties, and unacceptable risks to the franchisee.

If these cannot be satisfactorily resolved, ALNA believes an alternative process may need to be adopted.

ALNA also considered if a special agency could be established to handle franchise disputes or if the ACCC could take on this role, but we believe the establishment work involved would be too onerous and costly to maintain for just franchising disputes and the ACCC is a cross industry agency which is already overburdened and doing too much.

ALNA believes there is another proven model for resolving disputes that could be adopted or integrated into the current franchising resolution and support services available, “*The Australian Financial Complaints Authority (AFCA)*”.

To replicate AFCA and establish another Authority to resolve only franchising disputes would take considerable will and effort and may be considered too much to primarily resolve disputes that are not resolved through the existing Franchising Code ADR processes (conciliation and mediation), but is there a shared model that could work?

Could the solution be as simple as changing the authority to *The Australian Financial and Franchising Complaints Authority*?

If adopted, this expanded Authority could replace or supplement the existing Franchising Code ADR processes and services provided by the ASBFEO and State Small Business Commissions. If a shared model was chosen, it could be primarily used for disputes not resolved through the Codes ADR processes (i.e., conciliation or mediation).

The Franchising Code could make it a requirement that franchisors must maintain membership with the new AFFCA. This would eliminate the need to establish an arbitration process for franchising disputes and avoid the ensuing issues from it being reliant on the CAA.

ALNA believes the policies and processes used by AFCA could easily be expanded and modified to accommodate franchising disputes.

So how does AFCA operate?

AFCA is an external complaint resolution scheme established to resolve complaints by Complainants about Financial Firms. AFCA is operated by an independent not-for-profit company that has been authorised to do so by the responsible Minister under the Corporations Act.

The AFCA provides consumers and small businesses [and franchisees] with fair, free, and independent dispute resolution for financial [and franchising] complaints.

AFCA are industry funded by annual member registration fees, user charges and complaint fees received from member financial firms.

Many Australian financial services licensees, Australian credit licensees, authorised credit representatives and superannuation trustees are required to be a member of the Australian Financial Complaints Authority (AFCA) under their licence conditions. Other firms have joined AFCA voluntarily as part of a commitment to accountability in their dispute resolution.

The AFCA is governed by a set of Rules. These Rules are approved by ASIC, in accordance with the requirements of the Corporations Act 2001.

When determining complaints other than superannuation complaints, the AFCA decision maker must do what is fair in all the circumstances, and have regard to:

- legal principles
- applicable industry codes or guidance
- good industry practice
- previous relevant determinations of AFCA or predecessor schemes.

AFCA's governance, management structure, policies and procedures and decision-making are designed to ensure it meets its obligation to provide an independent service. Their Rules explicitly require complaints to be considered in an independent and impartial manner.

Their Board consists of an independent Chair and an equal number of consumer directors and industry directors. Decision panels are made up of an independent ombudsman, a consumer panel member, and an industry panel member.

AFCA provide an independent service through various means, including:

- through holding themselves to high standards of corporate governance, and transparency and accountability to the community
- through their Rules, which set out how they will ensure their process is fair and balanced for all parties
- by ensuring their leadership and decision makers are independent and free from material conflicts of interest
- by having an Independent Assessor to consider complaints about the standard of our service
- by having a Constitution and Rules that clearly and transparently set out how financial firms should interact with them, ensuring that they cannot unduly influence the outcome of any complaint.
- by requiring all members of AFCA to meet the costs of the service by paying a membership levy, along with fees for every complaint received about them. Payments have to be made whatever the outcome of the complaint.

All members pay a single annual registration fee plus additional user charge and complaint handling fees (if applicable). In FY22, this fee was \$375.55 for financial firm members and \$65.98 for Authorised Credit Representative (ACR) members. ACR's are charged an annual registration fee of \$65.98 as there is still a legislative requirement that they be members of an EDR scheme.

The Complaint fee schedule is designed to encourage early resolution of complaints. The first five (5) complaints closed in each financial year are not charged.

A determination is the final stage in their complaint resolution process, and other than by reference to the courts, it is not possible to appeal a determination.

A determination will be made in writing and will outline the reasons for the decision. Any remedy that AFCA award, whether it be monetary compensation, or some other remedy will also be included.

The financial firm [franchisor] is required to comply with AFCA's decision, if you the complainant [franchisee] chooses to accept it. The financial firm must provide any remedy in the determination within the timeframe AFCA have stated.

If a financial firm does not comply with a determination, AFCA are required to report this to ASIC.

<https://www.afca.org.au/media/1327/download>

<https://www.afca.org.au/media/1111/download>

ALNA would be happy to work with the government on the establishment of a much-needed arbitrated or alternative dispute resolution process within or supplementing the Franchising Code that levels the playing field for franchisees for disputes, especially those not resolved during conciliation and mediation.