

29 September 2023

Franchising Code Review Secretariat Unit

Small and Family Business Division

Department of the Treasury

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Dear Dr Schaper

Review of the Franchising Code of Conduct

The Australian Small Business and Family Enterprise Ombudsman (the ASBFEO) welcomes the review of the Franchising Code of Conduct (the Franchising Code). Effective codes of conduct are important in industries where market dysfunction impacts the welfare of businesses and consumers, and importantly, where self-regulation has not adequately addressed these issues.¹

Since its introduction, the Franchising Code has improved business conduct and addressed problems with some of the issues in commercial dealings between franchisees, master franchisees, and franchisors. Whilst dealings covered by the Franchising Code are commonly characterised as between small and family businesses and their large business counterparts, it is important to recognise that small businesses may be found on both sides of franchisee and franchisor relationships.

The ASBFEO recognises the way that the Franchising Code carefully balances regulatory safeguards and conduct expectations for franchisees and franchisors, whilst providing for incentives for businesses to invest, develop, take risks, uplift productivity, innovate and share success in franchise partnerships. The ASBFEO therefore supports the targeted and proportionate approaches of the Franchising Code that set behavioural and conduct minimums or floors, while encouraging ambitions for best practice approaches that far exceed the floor of the instrument.

Lamentably, the policy issue that underpins much of this submission is a franchising environment where small and family businesses are not provided with appropriate protections that they can themselves enforce and pursue under the Franchising Code and through the initiation of timely, and cost-effective determinative or legal action where required.

This submission presents policy solutions, under four themes, to strengthen the Franchising Code and regulatory landscape to improve the experience and productivity of small and family businesses in the franchising industry. The ASBFEO advocates for the Review to consider the proposals under these themes and help chart a path toward a more equitable and prosperous Australian franchising industry and improved capacity for parties to be able to rely on the Franchising Code.

¹ The Treasury, *Industry Codes of Conduct Policy Framework*, November 2017.

Our themes and key recommendations are:

1. *Promotion of good behaviour and shared success*

- Clarify the meaning of “good faith”.
- Use Franchising Code obligations as a ‘floor’ and encourage exemplar and best practice.
- Re-calibration of disclosure requirements and a requirement of reasonable opportunity for return on a franchisee’s investment.
- Adaptation of franchise models in executed franchise agreements should maintain a fair profit share.
- All types of franchise business models should be captured by the Franchising Code (even if labelled as a “licence” or like).

2. *Industry transparency, code navigation, and oversight*

- The Franchise Disclosure Register (FDR) should be modified to make data on the platform more readily accessible and easily comparable, including data on system dispute levels.
- Strengthen the effectiveness of multi-franchisee alternative dispute resolution (ADR) processes, including by specifically provide for multi-party notifications.
- Bolster Australian Competition and Consumer Commission (ACCC) enforcement.

3. *Improved routes to resolution and determination of disputes*

- Extension of the ASBFEO information gathering and ‘call out’ powers.
- Encourage use of arbitration, particularly where ADR has not resulted in a resolution, by notifying pre-agreement to arbitration on the FDR.
- Extend ‘super-complainant’ status to the ASBFEO and other credible dispute-resolution bodies.
- Establish a concierge service for trusted ADR advice, breach and termination processes that could be run by the ASBFEO in a way similar to its Small Business Tax Concierge service.
- Disputing parties could be provided with subsidised access to ADR processes coordinated by the ASBFEO.
- Address access to justice issues by introducing a Federal Small Business and Prescribed Codes List into the Federal Family and Circuit Court of Australia.

4. *Expanded access in the motor vehicle sales and service industries*

- It should be made clear that agency sales models are covered by the Franchising Code.
- The automotive schedule should be expanded to cover other ‘motor’ dealers, including truck, motorcycle and farm machinery dealerships.
- Agreements relating only to service and repair work should be covered by the Franchising Code protections.

1. Promotion of good behaviour and shared success

The regulatory framework governing franchising in Australia has undergone several major and minor revisions. As of 2022, the framework supported the health of an industry that contributes around \$172 billion yearly to the Australian economy.²

While the Franchising Code aims to balance the interests of franchisors and franchisees, challenges persist. Experience under the *Australian Small Business and Family Enterprise Ombudsman Act 2015* (the ASBFEO Act) and the dispute resolution mechanisms of the Franchising Code,³ the ASBFEO has observed a number of commonly shared issues and allegations made by franchisees and franchisors, namely:

- Payment disputes, including recoupment of debts accrued during the COVID-19 pandemic.
- Franchise system profitability (either in a specific region or across systems).
- Failure to act in good faith⁴, unconscionable conduct and unfair trading practices (UTP).
- Characterisation of arrangements as licenses or as franchises.
- Leasing issues with franchisor-led negotiation and non-renewal, and intersection of the Franchising Code with state-based retail leasing legislation.
- Issues with complaints handling and dispute resolution, including:
 - When obligations begin and whether procedures apply prior to the execution of a final agreement.
 - Reluctance of franchisees to access dispute procedures due to fears of retribution.⁵
 - Agreements reached in ADR not being honoured.
 - Failure of both parties to agree to the appointment of an arbitrator.

It is unfortunate that these challenges persist despite the introductions of robust dispute resolution, penalty, disclosure, and enforcement mechanisms in the past decade. Business owners regularly convey their sense of disappointment and disillusionment after holding faith in the Franchising Code to deliver enforceable safeguards, obligations and protections, only to arrive at an understanding that ACCC enforcement and direct litigation pathways are unachievable due to the gateways for Commission enforcement and the cost, risks and timeliness of direct legal action. However, this can be addressed through revisions to the operation of the Franchising Code and more generally addressing barriers to accessing justice. These revisions would also be supported through enhanced enforcement and improved resources and educative materials for industry participants.

² Franchise Council of Australia/Eden Exchange, *Unlocking Franchise Growth in Regional Australia*, 2023.

³ Competition and Consumer (Industry Codes—Franchising) Regulation 2014 (Cth), Part 4.

⁴ Competition and Consumer (Industry Codes—Franchising) Regulation 2014 (Cth), clause 6.

⁵ Competition and Consumer (Industry Codes—Franchising) Regulation 2014 (Cth), Division 3.



1.1. Obligations to act in good faith under the Franchising Code should be clarified and outline what ‘good faith’ means in practice

The Franchising Code does not specifically define good faith but relies on the definition of good faith in the ‘common law’.⁶ In its educative efforts, the ACCC provides information about good faith and examples of conduct. It should also be noted that subclause 6(6) of the Franchising Code provides that the obligation of good faith does not prevent parties to a franchising agreement, or a prospective agreement, acting in their legitimate commercial interests.

In our experience, small businesses frequently describe conduct that they maintain is not in good faith. The lack of a clear definition and actions that may be taken to accord with ‘legitimate commercial interests’ result in misunderstandings, uncertainty and frustration for business owners, most commonly franchisees.

Amending the Franchising Code by along the lines of subclause 11(4) of the Competition and Consumer (Industry Codes – Dairy) Regulations 2019, could help build confidence in and understanding of what ‘good faith’ means in practice. Clearly detailing behaviours that may be considered when determining whether a party has fulfilled its obligation to act in good faith, would help raise the standard of business conduct and promote more fruitful engagement in ADR processes.

1.2. The Franchising Code should outline the best practice standards of conduct for franchisees and franchisors

Legislation and prescribed codes of conduct provide the minimum standards for businesses in entering, operating and exiting of franchising arrangements. However, although industry codes may set a floor for behaviour, they should also encourage ‘best practice’ good behaviours that exceed the minimum standard that is set.

A mechanism to capture a ‘best practice’ intent, is found in the Statement of Guiding Principles under the industry-led (voluntary) Banking Code of Practice.⁷ The ASBFEO considers that there is merit in creating a similar framework in the Franchising Code. It could define principles-based behaviours that promote fairness, integrity, trust, transparency, and commitments to work together to achieve shared success.

Any guiding ‘best practice’ principles or framework should set targets that facilitate adoption of behaviours for ambitious franchise systems. Reaching these higher standards would support franchisors to be recognised as systems of choice by franchisees. These standards would set out the types of behaviour that best leverage sharing of system intellectual property, recognising the labour, organisation and contribution of franchisees. The focus would be to create the best likelihood for the parties to create and build valuable, prosperous businesses.

The Review might also wish to consider how parts of related prescribed codes of conduct, such as the Oil Code and business practices pursuant to it (such as the retailing of goods) can be aligned with the Franchising Code.

⁶ ACCC, *Acting in good faith under the franchising code*, accessed 20 September 2023.

⁷ Australian Banking Association, *Banking Code of Practice*, October 2021.



1.3. The Franchising Code should carefully calibrate disclosure requirements and provide information relevant to franchisees

The focus of the Franchising Code on addressing information asymmetry and encouraging fairness for prospective franchisees has been a significant step forward for the industry. However, there needs to be careful calibration of required disclosure. While new franchisees should be supported with information to assist them to exercise due diligence, it may not be in the interests of either franchisees or franchisors to produce and maintain increasingly wide-ranging and complex documents. The depth of detail in disclosure documentation can impede good decision-making by prospective franchisees by obscuring relevant detail and making the task of considering that detail simply too hard.

One area of disclosure that could be refined is the requirement for financial information about a franchise system.⁸ While the approach of a *Key Facts Sheet* has been an effective step in the right direction, a more standardised approach to presenting the financial data across the industry would help enhance comparison of systems and simplify the evaluation process for prospective franchisees and their trusted advisors. A key element would be to include a metric that compares the level of system fees and levies with profit share in the system, as well including data on site turnover. We raise this due to ongoing requests for assistance related to disputes arising in franchise systems that might be considered to demonstrate high levels of churning and burning.⁹

We further note that prospective franchisees are warned that the Franchising Code (and associated laws applicable to franchising) do not reduce the commercial or business risks of buying a franchise.¹⁰ However, there is more that can be done for prospective franchisees to alert them that when assessing investment risk of franchise systems that attention should be directed to determining whether system profit may rely on the clawback and sale of existing, or the sale of new and untested sites that may have poor prospects of commercial return. This may be addressed in part by mirroring clause 46B that applies to new vehicle dealerships and require that franchise agreements should provide a reasonable opportunity for return on the franchisee's investment.

The review should also consider whether the disclosure documents adequately convey the assumptions underpinning the prospective profitability of a franchise unit. This may include surfacing whether the franchise opportunity is tested and proven, or a newer, conceptual model; declare if the model requires a minimum amount of time in the business by the franchisee; and canvass the financial implications of multi-unit ownership.

1.4. Adaptation of franchise models in executed franchise agreements (made in response to changing markets or innovations should maintain a fair profit share

In recent years, several emerging trends have significantly impacted the operation of the Franchising Code. These trends reflect the evolving nature of the economy, consumer choices, and the franchising landscape. They also highlight the requirement for consistent and ongoing reviews of regulatory frameworks to address contemporary and future franchising challenges.

A key area where the ASBFE Ombudsman has seen issues includes technological innovations and the digital transformation of business operations. Franchisors and franchisees are grappling with issues

⁸ Australian Government, *Information statement for prospective franchisees*, page 2, 2023.

⁹ Australian Competition and Consumer Commission, *About Franchising*, accessed 20 September 2023.

¹⁰ Australian Competition and Consumer Commission, *About Franchising*, accessed 20 September 2023.



related to online sales, e-commerce platforms, third-party delivery service platforms, and digital marketing service providers. These types of change in franchise systems raise issues relating to how royalties are calculated, how internal systems are built and paid for, and ultimately may impact the profitability of operations and the profit shares of franchisors and franchisees.

For example, the ASBFEO has supported franchisees in relation to disputes involving royalty fees applied to third-party delivery service commission fees. This was an adaptation to trends in delivery services that altered the profit share between the franchisor and franchisee. With franchisees claiming that commissions added to profitless, ‘pass-through’ charges resulted in an increased share of revenue with the franchisor.

1.5. Franchising Code definitions should capture all types of franchise business model

There is an increasing trend where business operators establish systems that engage small and family businesses to provide the labour and coordination of operations across regions. In our dispute support experience, we have observed numerous agreements that, while not being explicitly drafted as ‘franchise agreements’, demonstrate business relationships with the hallmarks of franchisee-franchisor interdependent dynamics. These arrangements typically include a high degree of control and direction by the “franchisor”, who assigns the rights to use intellectual property, uniforms, branded products, as well as specifying pricing and how the business markets and sells its products and services.

While the ASBFEO supports legal commercial relationships between businesses, there is a sense that choices, with or without legal advisors, are being intentionally made to seek to evade the operation of the Franchising Code. With requirements of the Franchising Code not being fulfilled on entry, during the term or on exit of the arrangements, we have seen increasing numbers of dispute where businesses, and their legal advisors, seek to mount arguments as to why the Franchise Code does not apply. One egregious example was a fast-food business advertising “franchisee opportunities” on its website but then denying that a franchise relationship existed and seeking to deny access to the complaints handling procedures of the Franchising Code.

We are concerned that franchises may exploit low perceptions of enforcement risk and are making commercial decisions to operate outside of the remit of the Franchising Code, at the cost of prospective franchisees. This would be addressed in part by the Franchising Code more explicitly covering arrangements that exhibit the hallmarks of a franchise despite being labelled a “licence” or other term.

2. Industry transparency, code navigation, and oversight

2.1 The Franchise Disclosure Register should be modified to make data on the platform more readily accessible and easily comparable

Introduced to the Franchising Code via legislative amendment in April 2022, the Franchise Disclosure Register (FDR) provides prospective franchise buyers, current franchisees and professional advisers access to information to inform commercial decision making.¹¹

All franchisors and non-exempt master franchisors were required to have published a profile on the FDR by 14 November 2022, before its public launch on 15 November 2022. We understand that

¹¹ Australian Government, *Franchise Disclosure Register*, accessed 20 September 2023.

this review seeks to satisfy section 53J of the Franchising Code, to review and report to the Minister on the operation of the FDR.

Through our dispute support experience and consultations with the public and industry stakeholders about the FDR, the ASBFEO identified several key themes, including:

- Views that, although the FDR contains desired information, it is not as user-friendly, standardised, comparable and clear as envisaged, particularly to prospective franchisees.
- Concerns that disputes under the Franchising Code have not been disclosed appropriately and a desire for overall disputation, including notification of ADR processes managed internally, be published to the FDR.
- Complaints from franchisors that the current obligations are too onerous.
- Challenges encountered when creating a public profile for businesses without a *MyGovID*.
- A number of franchise systems not being on the FDR and other non-compliance by franchise systems.

A key improvement to the Franchising Code would be to require all franchisors to provide statistical information related to levels of disputation within their franchise system. Under Section 4A of the Franchising Code, the ASBFEO is required to report statistical data related to disputes that follow the complaints handling procedures under both the Franchising Code, and the terms of a franchise agreement that are in accordance with the Franchising Code.¹²

While the ASBFEO reports on requests for assistance raised with our Office, as well as any reports made to our Office by systems or alternative dispute practitioners, the ASBFEO does not have visibility over internal complaint experience and resolution, and over ADR processes where parties can agree to a practitioner and process without third-party assistance.

The ASBFEO is encouraged by all franchise participants who seek to use the complaints handling procedures under the Franchising Code to resolve disputes and return to business – whether or not they access our services. However, it is of utmost importance in understanding the effectiveness of the Franchising Code to monitor the health and true levels of disputation within the industry, including the effective use of internal dispute/grievance resolution mechanisms. The introduction of an obligation to upload data yearly to the FDR on levels of disputation (internally resolved or externally facilitated) is a vital and valuable amendment for prospective, current, and renewing franchisees.

2.2 Strengthen the effectiveness of multi-franchisee ADR processes

While the ASBFEO welcomes the changes to introduce franchisees to request and participate in multi-franchisee ADR, it is our experience that uptake of these processes has been limited. The ASBFEO has assisted with multi-franchisee matters that have proceeded to mediation, but the success of mediation has also been limited in producing agreed settlements of all issues in dispute. Having said that, multi-party mediation has still provided opportunities to have disputes addressed (that may not otherwise have been addressed), improve understandings, and clarify the issues for the parties due to the ability to share process costs.

A key learning from the ASBFEO's involvement in multi-franchisee ADR, is that participating franchisees have a misunderstanding about the ASBFEO's role. The ASBFEO's role is to assist in the

¹² Competition and Consumer (Industry Codes—Franchising) Regulation 2014 (Cth), section 4A.



appointment and passing carriage of matters to an ADR practitioner, however franchisees often want the ASBFEO to also gauge willingness and coordinate prospective participants, including identifying 'lead' complainants/spokespersons.

Although the Franchising Code details the ability of franchisees to discuss disputes with each other for the purposes of determining whether multi-franchisee action is suitable, the ASBFEO has seen several instances where franchise systems appear to have actively inhibited or threatened franchisees seeking to discuss issues across the system. The fear of commercial retribution or legal escalation will dissuade some franchisees from seeking resolution of their disputes. The Franchising Code could directly reference and address franchisor behaviours that appear to disrupt or discourage franchisees from engaging in multi-franchisee ADR. This may include coverage of this issue in any changes made to good faith requirements under the Franchising Code. The importance of access to multi-party ADR could also be supported by direct reference to multi-franchisee notification in clauses 40A and 40B.

A key role that the ASBFEO provides with multi-franchisee ADR, is to assist with the appointment and passing carriage of matters to an ADR practitioner with the franchisees being ready to engage appropriately in the process. We are providing guidance on navigating multi-franchisee ADR, including standardising party details wherever possible, and demonstrated awareness of the franchise system of the dispute and confirmation of its engagement.

2.3 Bolster ACCC activity to ensure that both franchisees and franchisors sense genuine prospects of compliance and enforcement activity

All sectors of the franchising industry, including small businesses, legal advisors, industry groups and government agencies, recognise that enforcement activity by the ACCC is necessarily limited by available resources. The ASBFEO has previously noted this picture of the ACCC's role as the regulator tasked with enforcement but constrained due to resources as akin to 'a hunting dog that won't leave the porch'.¹³

We recognise the responsibility, challenges, and successes of the ACCC in ensuring that businesses comply with the Franchising Code through the prosecution of wilful, egregious and systemic breaches by businesses. We also acknowledge the ACCC's work in engaging via targeted education, reminders and warnings prior to public notices, enforceable undertakings and prosecution. Alongside this important work, funding of additional enforcement activity would be seen as support of the franchise industry through increased action by the ACCC to improve the integrity of the franchising industry. It would also assist in the jurisprudence around key Code concepts and guiding reasonable expectations as to the utility of provisions. Further support in this regard would then be added through improving the ability of franchisees and franchisors to access justice through the Federal Circuit Court (see 3.6 below).

¹³ ASBFEO, submission on *Treasury Laws Amendment (Competition and Consumer Reforms No. 1) Bill 2022*, August 2023.



3. Improved routes to resolution and determination of disputes

3.1 Extension of ASBFEO information gathering and ‘call out’ powers

The ASBFEO recommends introducing information and document gathering provisions, as well as ‘call out’ provisions, in relation to ADR processes under the Franchising Code.

Previous amendments have introduced and enhanced penalties in relation to compliance with the Complaints Handling Procedures under the Franchising Code. However, an environment where concepts have not been clarified, penalties are not regularly enforced, and fines for summary offences, or similar, are unavailable persists. An additional mechanism could be introduced to incentivise both franchisees and franchisors to follow their obligations to act in good faith throughout the complaints handling and ADR processes under the Franchising Code.

By adding a call-out power, agencies assisting with disputes under the Franchising code, and in particular the ASBFEO, could publicise non-attendance at ADR, failure to act in good faith at ADR, an unwillingness to implement mediated resolutions and any general lack of good faith, or similar compliance issues.

If the ASBFEO could publicise these issues, including on the FDR, both franchisees and franchisors would be encouraged to try to resolve disputes and implement agreed resolutions in a meaningful and productive way and avoid litigation. This could be further supported by extended existing ASBFEO powers to call for information and documents to disputes handled directly under the Franchising Code. The information gathering powers could be utilised where franchisees or franchisors seek to withhold key information relating to disputes, or large power-asymmetries prevent any real prospects of successful ADR processes. We note that we currently use these mechanisms sparingly and with careful consideration. The mere presence of these powers also encourages industry participants to engage early and well with our Office.

3.2 Encourage an improvement in business practices by franchisors, and the use of arbitration to avoid the costs and stresses associated with currently available formal legal action, particularly in instances where ADR has not resulted in a resolution.

The ASBFEO had welcomed the ability of franchisee and franchisors to agree to voluntary binding arbitration (VBA) for disputes following the *Fairness in Franchising* amendments to the Franchising Code taking effect in 2021.¹⁴ However, since its introduction, there have been no appointments of an arbitrator by the ASBFEO under the Franchising Code, nor are we aware of any agreed VBA engagements external to our Office. This is despite the ASBFEO supporting parties in disputes to seek agreement of other parties to arbitrate.

Arbitration offers opportunities for franchisees and franchisors to resolve disputes more quickly and at a lower cost than court processes. It particularly suits resolution of disputes in ongoing franchise relationships. To increase the uptake of VBA, the ASBFEO suggests a ‘soft’ approach, in which franchisors would self-elect willingness to use VBA and what type of disputes they would be willing to resolve by VBA by making an appropriate disclosure in pre-entry documents, as well as on the FDR. This would allow franchise systems to demonstrate their willingness to resolve disputes in their system in a timely and cost-effective way. Early adopters could also benefit as they distinguish their systems in this way.

¹⁴ Australian Government, *Explanatory Statement – Competition and Consumer (Industry Codes – Franchising) Amendment (Fairness in Franchising) Regulations 2021*.



Like the approach agreed for the Motor Vehicle Industry, a standard VBA clause could be developed, its uptake encouraged and its adoption appropriately recognised. A simple note on FDR would communicate a franchise system's precommitment to agree to voluntary arbitration.

An alternative, more insistent approach would be to include an undertaking to agree to VBA or similar declaration during the FDR disclosure process that would see a franchise system pre-commit to use binding arbitration where mediation or conciliation is unsuccessful and VBA is a 'given' next step for ASBFEO dispute resolution facilitation as a condition of entry onto the FDR.

3.3 Extend 'super-complainant' status to the ASBFEO and other credible dispute-resolution bodies

The ASBFEO welcomed the 2023-24 Budget announcement that the ACCC will establish the first phase of a complainant mechanism for designated consumer and small business advocacy groups to raise systemic issues under consumer law. The super-complainant mechanism is a key pathway to facilitate the escalation of small business complaints to the ACCC and other relevant regulators, and facilitate enforcement action that is timely and minimises small business victims of illegal conduct.

We acknowledge that at the time of writing, the ACCC is exploring how the mechanism will work, and the ASBFEO looks forward to working with the ACCC as a super-complainant once the approach is launched in July 2024.

3.4 Establish a concierge service for trusted ADR advice, breach and termination processes

In the ASBFEO's experience, small business franchisees often enter disputation at points in their business journeys where their capital, resources, and mental wellbeing have been stretched. These observations are most common in the entry and establishment and exit phases of a franchise system.

When disputation occurs, franchisees turn to the Franchising Code complaints handling procedures as a mechanism to resolve their issues through structured processes that give weight to all parties in dispute. However, the ASBFEO has observed that when franchisees in these difficult situations access ADR, reaching an agreed settlement can be difficult. Franchisees often cannot separate their perceptions of how the other party has acted under the Franchising Code and at law from their personal disappointment of seeing their hopes and expectations of their investment unfulfilled. Also, disputes may fail to settle due to the imbalance between parties and an inability of franchisees to mount persuasive arguments in ADR processes that are based in legal obligations. For successful ADR, it is imperative that both parties are open to options and have the ability to advance convincing and persuasive arguments based on specific facts of the matter and that are based in legal fairness and equity.¹⁵

The ASBFEO therefore advocates for a concierge service to support franchisees to seek advice, including on their prospects and support from a trusted legal and professional advisor before formally entering an ADR, breach or termination process. Such a service could operate similarly to the Small Business Tax Concierge (SBTC) administered by the ASBFEO. The SBTC service provides one or two hours of subsidised legal advice that affords small businesses an opportunity to hear from an independent third party before they decide whether to appeal an ATO decision to the Administrative Appeals Tribunal. A franchise system version could provide small business

¹⁵ The Hon Michael McHugh AC KC, *Mediation & negotiation in legal disputes*, 2021.



franchisees who have requested assistance from the ASBFEO to access subsidised legal advice in order to help them understand the relative strength of their legal position, the risks of not resolving their case at ADR and assistance with preparation for ADR. This would increase the likelihood of resolution at ADR and reduce the likelihood that parties remain aggrieved about the outcome of a dispute.

3.5 Disputing parties could be provided with subsidised access to ADR processes coordinated by the ASBFEO, ensuring equity of access to ADR for all participants, including those who are in hardship or otherwise vulnerable

State governments, such as Victoria and New South Wales, have chosen to enact legislation and funding mechanisms to support subsidised ADR through their small business commissioner services. However, the Government has not done this for the Franchising Code at a federal level.

By the time a small business franchisee arrives at the need or decision to engage with ADR, they frequently find themselves with a combination of a lack of resources, withholding of moneys by franchise systems, and reductions or cessations in the supply of leads, goods and services. These franchisees may choose not to engage in ADR simply because they cannot afford it.

Providing subsidised ADR for small business involved in franchising disputes would allow all parties to access to ADR in a timely fashion. It would also help avoid parties remaining in dispute for prolonged periods as entrenched positions increase and underutilised productivity and hampered growth persist.

The Review may also consider turning its mind to the ongoing existence of South Australian legislation and the extent to which it impacts on a nationally consistent approach to franchising regulation in Australia.

3.6 Address access to justice issues for franchisees and franchisors by introducing a Federal Small Business and Prescribed Codes List into the Federal Family and Circuit Court of Australia

It is well established that small and family businesses, both as franchisees and franchisors, can face significant power imbalances and information asymmetries when engaging within the franchising industry, particularly with large business counterparts. These imbalances and asymmetries are accompanied and compounded by breaches of the Franchising Code, use of unfair contract terms (UCTs) and unfair business (trading) practices (UTPs). Ultimately, these behaviours reduce competition, efficiency, and confidence in the economy.

The Government is currently consulting on ways to address the consumer and small business harms of UTPs, and the ASBFEO supports stronger policy action to establish frameworks that will reduce harm to small and family businesses.¹⁶ However, in the context of this review and the relationship between franchisees and franchisors, the wider legislative and judicial environment remains. The problem is that small businesses currently have little hope of defending their economic interests where ADR has been unsuccessful, primarily due to the costs, delays and risks of formal legal action to access the current court system. This is despite increased penalties under the Franchising Code, since they still lack the genuine prospect of formal dispute resolution due to a lack of individual accessibility to justice in their particular circumstances.

¹⁶ The Treasury, *Protecting consumers from unfair trading practices*, August 2023.



Introducing a Federal Small Business and Codes List into the Federal Family and Circuit Court of Australia would provide a low-cost alternative for small businesses and regulators to seek redress and cost-effective and timely enforcement action. Disputes appearing on the list would be capped at \$1 million (award or fine) and delivered via online hearings, significantly reducing the time and cost burden on a small business. Critically, the list would:

- Operate as a ‘no costs’ jurisdiction.
- Include a reduced of capped ‘court book’ evidentiary entitlement.
- Provide a guaranteed turnaround time.
- Include compulsory pre-hearing ADR and Court-appointed ‘experts’.
- Exercise discretion in dismissing frivolous or vexatious claims.

This reform would reduce barriers to justice for franchisees and franchisors by supporting them in protecting their own commercial interests in a way that is affordable, timely, and able to deliver appropriate sanctions, interventions and recompense from parties engaging in unlawful, anti-competitive, or unfair conduct. Such a reform would also support the development of jurisprudence, address perception of Code and law ineffectiveness due to a lack of enforcement, support regulators focusing on materially-significant matters to the economy and systemic failures and guard against further over regulation aimed at abating ongoing harm that actually arises from a lack of enforcement of current regulation rather than a need for more.

4. Expanded access in the motor vehicle sales and service industries

There remains a power imbalance between multinational car manufacturers and Australian dealers, most recently demonstrated through the Hon Justice Jonathan Beach’s dismissal of 38 dealers’ \$650 million compensation claim against Mercedes-Benz. In the context of Justice Beach’s remark, ‘it may be that further consideration needs to be given to the terms of the Franchising Code and possible modifications’, we make the below recommendations.

The full impact of the 2021 changes in the Franchising Code is not yet known in relation to return on investment for new vehicle dealership agreements, the obligation to act in good faith in relation to new car dealerships and compensation for early termination of new vehicle dealership agreements. The ASBFEO’s submission to the 2021 *Automotive Franchising Discussion Paper* provided that the then recent changes to the Franchising Code needed time to take effect before considering further changes. The majority of dealers remain trading under old dealer agreements and, for those that have transitioned onto new agreements during the last 15 months, those dealers will generally not experience the need to engage in or test these reforms until renegotiating the entirety of their agreements from July 2026 (with standard dealer agreements having 5-year durations).

The Automotive Franchising Memorandum of Understanding (MoU) also came into effect on 1 July 2022 only to complement the Franchising Code with an additional pathway for manufacturers and dealerships to settle their disputes through Voluntary Binding Arbitration (VBA). Parties to the MoU (Federal Chamber of Automotive Industries (FCAI), Australian Automotive Dealer Association (AADA) and Motor Trades Association of Australia (MTAA)) jointly agreed to a best practice pathway

for to settle their disputes via arbitration in the event of early termination of an agreement by a manufacturer.

Noting that the MoU is subject to review every 2 years to determine its effectiveness and identify potential areas of improvement and with its first review coinciding with the review of the Franchising Code, the ASBFEO provides the following observations:

- The parties attest that they have worked closely together in good faith.
- The relevant provisions have not been fully tested because the MoU has been part of the industry-led regulatory framework from 1 July 2021 only.
- No dispute cases have been lodged to test VBA under the MoU, with the parties believing that education of OEMs and dealer councils have aided in minimising potential disputes.
- The MoU between industry representatives does not mandate compliance by their members and limits the influence of the representatives largely to educative approaches.

4.1. It should be made clear that agency sales models are covered by the Franchising Code

We have previously proposed amendments to the Franchising Code to clarify the breadth of automotive dealer models and agency models that are captured, for example where a separate agency agreement is created for the parts or services functions. The agency model has been adopted by at least 2 original equipment manufacturers (OEMs), namely Tesla and Hyundai, and it is assumed that these agency models are appropriately captured under Part 5 of the Franchising Code.

4.2. The automotive schedule should be expanded to cover other ‘motive’ dealers, including truck, motorcycle and farm machinery dealerships

The common element across franchising in automotive markets is the power imbalance between much larger manufacturers and their dealers. New car franchise agreements typically involve engaging with large multinational manufacturers, high upfront capital investments with specific and expensive fit outs, geographically limited territories, and long term after-sales interactions with customers.

Through previous automotive franchising consultation processes, industry stakeholders have supported the expansion of the automotive schedule to cover commercial vehicle, motorcycle, farm, and industrial machinery franchise dealers, so that they are afforded the same legislative protections as new car dealers.¹⁷ Industry’s position remains relevant in the current environment, and the ASBFEO supports dealerships in other automotive sectors that face similar power imbalances, high capital investments and longer term after-sales interactions, benefitting from the protections available to new car vehicle dealership agreements.

¹⁷ Motor Trades Association of Australia, *Submission - Automotive Franchising Discussion Paper*, September 2021; Federal Chamber of Automotive Industries, Australian Automotive Dealer Association, *Response to the Automotive Franchising Discussion Paper*, September 2021; Victorian Automotive Dealer Association, *Response to The Treasury’s Automotive Franchising: Discussion Paper*, August 2021.



4.3. Agreements between automotive manufacturers and dealerships that relate only to service and repair work should be considered as franchise agreements and be covered by the Franchising Code protections

The ASBFEO has previously recommended that the Government consider including emerging automotive markets under the Franchising Code.¹⁸ This would ensure that segmented agency models, such as where a separate agency agreement is created for the parts or services functions, are captured.

Dealerships engaged in service and repair work face similar challenges regarding contract terms, access to necessary resources, and potential disputes with manufacturers. Bringing these service-oriented agreements under the Franchising Code's umbrella helps ensure a consistent and equitable regulatory framework across the automotive industry.

If you require any further information or have any questions regarding our submission, please contact Mr Keiran Stroh, Policy Analyst, on 02 5114 6113 or via email to advocacy@asbfeo.gov.au

Yours sincerely

The Hon. Bruce Billson

Australian Small Business and Family Enterprise Ombudsman

¹⁸ ASBFEO, 15 September 2012, Submission to the 2021 Automotive Franchising Discussion Paper.