

29 October 2021

Small and Family Business Division
Treasury
Langton Cres
PARKES ACT 2600

By email: franchisedisclosureregister@treasury.gov.au

Dear Sir/Madam,

Guide and Exposure Draft regulation relating to the establishment of the Franchise Disclosure Register

The Business Law Section (**BLS**) of the Law Council of Australia is pleased to have the opportunity to comment on the issues raised in in the Guide and Exposure Draft regulation relating to the establishment of the Franchise Disclosure Register.

Introductory Comments

The views expressed in this submission have come from the Competition & Consumer Committee (**CC Committee**) and the SME Business Law Committee (**SME Committee**) of the BLS. The SME Committee has as its primary focus the consideration of legal and commercial issues affecting small businesses and medium enterprises (**SMEs**) in the development of national legal policy in that domain. Its membership is comprised of legal practitioners who are extensively involved in legal issues affecting SMEs. The CC Committee is comprised of senior legal practitioners, including many senior franchise law specialists, who practise predominantly in the field of competition and consumer law. Where opinions on certain aspects of the matters under consideration in this submission may differ, that is a reflection on the different focus that is taken by the SME Committee.

As a general comment, members of the SME Committee are in favour of the introduction of the Franchise Disclosure Register, whereas members of the CC Committee do not believe that there is material additional benefit to be provided by the proposed Register, and in fact raise serious concerns as to the extent of the proposed disclosure to be included in the Register. The two viewpoints can be introduced as follows.

The SME Committee believes the proposed Register will provide small business franchisees with a more transparent, accessible and accountable source of information about various franchise opportunities. They note that many franchisors simply choose not to provide franchisees with any meaningful information about the likely financial performance of the franchise business, particularly if they are “greenfield” sites or territories. Rather, both franchisors and various franchising advice bodies encourage franchisees to speak to as many existing franchisees as possible to obtain information about the likely

financial performance of their franchise and the franchise system more generally. SME Committee members are concerned that advising prospective franchisees to speak to existing franchisees about issues such as likely financial performance may result in those existing franchisees becoming exposed to legal liability for misrepresentation or omission, albeit unintentional, which they have gratuitously provided to the prospective franchisee. Most existing franchisees who do provide information to prospective franchisees in this way may not appreciate that they may in fact be incurring potential legal liability.

On the other hand, it is not obvious to the CC Committee what material additional benefit will be provided by the proposed Register, given that prospective franchisees will already have access to the *same* information as part of the normal disclosure process set out in the Franchising Code of Conduct. The CC Committee believes the potential for abuse is a major concern, given it is proposed to provide to any person, located anywhere in the world, free and unfiltered access via the Franchise Disclosure Register to extensive information on an Australian business. Such an approach also seems contrary to policy underpinning other public registries, such as those applying to companies and incorporated associations, where only fairly limited information is provided. If the Government intends to proceed with the Franchise Disclosure Register, then it must allow franchisors to take reasonable steps to redact confidential or commercially sensitive information. The Government has rightly required the redaction of personal or confidential information relating to franchisees. The right of redaction should be extended in the manner set out in this submission.

The Committees' responses to the specific questions asked by the Government are set out below.

1. Are the amendments in the Exposure Draft likely to produce any unintended consequences?

The Committees assume that Treasury has already considered all reasonably foreseeable consequences, including the use which third parties who are not franchisees or prospective franchisees will make of the information contained in the disclosure documents uploaded onto the Register. Third parties would include competitors, suppliers, landlords, debtors, creditors, employees, consumers and the media. It seems unusual to provide free and unfettered access to such a wide variety of people if the sole expressed aim is to enhance transparency for prospective franchisees. It is also not clear whether the Government will actually track who has accessed the information, and what happens to that information. The Committees also assume that Treasury has considered the likelihood of prospective franchisees considering registration on the Franchising Disclosure Register as some form of imprimatur notwithstanding the disclaimers intended to form part of the inquiry process. The following comments are therefore limited to legal matters.

- **Clause 53B(2)(a)** seems somewhat narrow, and indeed the actual scenario provided quite unrealistic. Presumably the Secretary would need broader discretion to remove information, and should not have to rely on an unlikely request from a franchisor that has ceased to exist.
- **Clause 53B(3)** gives the Secretary the power to remove a disclosure document from the Register. It may be better to require the Secretary to issue a notice to the franchisor requiring the franchisor to show cause within, say, 14 days as to why the disclosure document should not be removed. In most cases this will

prompt the franchisor to either upload an updated disclosure document or provide the information under section 53F.

There also ought to be a fetter on the power of the Secretary, such that it will only be exercised where the show cause notice was not addressed.

- **Clause 53C(1)** - The unintended consequence is that a franchisor who is marketing franchises but may not have yet given a copy of its disclosure document to a franchisee or prospective franchisee, will not have to comply with section 53C. This would be easily rectified by adding the words “, or proposes to give,” after “the franchisor has given” in paragraph (a) of subsection 53C(1).
- **Clauses 53C(4) and 53D(4)** require that the franchisor must redact “any personal information that relates to an individual that is included in the document”. It would be useful if this section specified exactly what needed to be redacted, so there can be no ambiguity.
- **Clause 53C(5)(b)** should be amended to read “given to a franchisee under subclause 17(3)”. Otherwise the Secretary has the power to require a franchisor to include things on the Register that go well beyond the intended purpose of the Register such as:
 - a copy of a franchise agreement (as required under clause 9(1A)(a) of the Code);
 - a copy of the Code (as required under clause 9(1A)(d) of the Code);
 - specific leasing information (as required under clause 9(1A)(e) of the Code);
 - the information statement (as required under clause 11 of the Code);
 - leasing documents (as required under clause 13 of the Code);
 - other agreements (as required under clause 14 of the Code);
 - financial statements for marketing funds or other cooperative funds (as required under clause 15 of the Code);
 - end of term notifications (as required under clauses 18 and 47 of the Code).

Whilst one would expect that the Secretary will not request these types of documents to be included on the Register, the risk of this occurring can be alleviated by making the amendment suggested above.

The BLS is also concerned at the application of a pecuniary penalty of 600 penalty units to a breach of clauses 53C(2), 53D(2) and 53E(2) in circumstances where a franchisor is reliant on technology and systems outside the franchisor’s control. The BLS is similarly concerned at the application of a pecuniary penalty of 600 penalty units for breach of clause 53F.

These amounts are far in excess of the penalties applying to failure to lodge company documents under other legislation, such as the Corporations Act. The Code already provides for substantial pecuniary penalties for failure to prepare or update a disclosure document, being what many would consider to be substantive breaches of the Code. The penalties under clauses 53C, 53D, 53E and 53F are more analogous to penalties for failure to lodge documents, and arguably a duplication of the substantive penalties. This seems unreasonable.

2. Are there any consequential amendments to the Franchising Code which may be required which aren’t reflected in the Exposure Draft?

The SME Committee does not believe that any consequential amendments are required to the Franchising Code as a result of the Exposure Draft. However, the CC Committee suggests that this question be discussed with peak industry bodies such as the Franchise Council of Australia and the Federal Chamber of Automotive Industries. These bodies will be better placed to advise on consequential amendments.

3. Is the information to be included on the Register appropriate?

While a franchisor's disclosure document in particular provides franchisees with a significant amount of important information about a franchise which may be of considerable value when weighing up competing franchise opportunities, and hence is favoured by the SME Committee, the CC Committee considers that it is hard to see how requiring franchisors to upload their disclosure document will make any material contribution to achieving the intended purpose of assisting prospective franchisees to make an informed decision before entering into a franchise agreement. This purpose is far better served by the comprehensive and thoughtfully designed disclosure process set out under the Franchising Code. The primary concerns of the CC Committee are as follows:

1. Most disclosure documents are quite voluminous, and prospective franchisees are unlikely to wish to read disclosure documents online, let alone read and try to compare multiple different disclosure documents;
2. Search functionality appears to be quite limited, and not to include the ability to search and compare detail contained in the disclosure document itself using the search functionality;
3. A better alternative would have been to require lodgement of the Key Fact Sheet, and have search functionality directed to that more concise document.

The Key Fact Sheet is far shorter and contains pertinent information that will enable prospective franchisees to compare, and decide whether to go to the next stage in applying for the franchise and requesting the disclosure document. Less (perhaps no) information will need to be redacted from the Key Fact Sheet.

4. Are there other types of information, not within the existing scope of disclosure, that are important for prospective franchisees to compare?

It is not clear that prospective franchisees will often actually compare disclosure documents. Typically, by the time a prospective franchisee is looking for the information contained in a disclosure document they have reached an advanced stage of their process. As noted above, it would be far more useful (and easier and quicker) to compare the Key Fact Sheets of different franchise systems.

It is not so much that other types of information should be included; it is that there is so much detail in a disclosure document that efficient comparison is unlikely to be possible. However, there remains a deficiency in the current disclosure regime in relation to breach notices issued *or threatened to be issued* by franchisors to franchisees, which is a common method used by franchisors to keep franchisees compliant. This disclosure should be added to section 6.4 of Annexure 1 to the existing Code, as should the number of instances where a franchisee's request to terminate the franchise (or to de-brand) was refused, or where to have done so would have forfeited a significant proportion of the franchisee's investment.

5. Is the information to be redacted from franchisors' Disclosure Documents appropriate?

The CC Committee considers there should be more redaction. A franchisor should be entitled to redact confidential information beyond just the personal information of franchisees and details of rebate percentages under Item 10.1(k)(iii). As the register will be publicly available at no charge, there are other sensitive items that could be considered confidential. Redaction does not prejudice a prospective franchisee, as they can obtain the un-redacted information from the franchisor. However, it protects the franchisor and the

franchise system, including from use of the information to their detriment by third parties such as competitors, landlords, suppliers, the media and others.

The CC Committee considers that a franchisor should be able to redact information if it is confidential and commercially sensitive, provided the franchisor notes what has been redacted and provides reasoning for the redaction. See the table below for the specific examples of areas where disclosure of information without redaction could potentially be a problem.

Item	Information	Reasoning
8.1	Details of the franchisor's intellectual property, registration status, and details of any agreement that impacts the franchisor's right to use intellectual property.	For some franchise systems this information could be highly confidential. In the hands of competitors or the media the information would be open to abuse, to the detriment of the franchise system. This unfairly prejudices franchise systems that compete against non-franchised systems, often large corporations, as many do.
10.1(k)	Nature of rebates or financial benefits received from every supplier and the name of every supplier.	Highly confidential information that places franchise systems at a substantial competitive disadvantage to non-franchised networks.
10.1(m)	The method for working out how rebates are shared amongst members of a franchise network, and a description of each direct or indirect benefit received by the franchisee.	Competitors will have access to this information, which they can use to the disadvantage of franchise systems in negotiations with suppliers.
11	Restrictions on the goods or services franchisee may supply, to whom and whether they must supply the whole range.	This information is clearly relevant to a franchisee or prospective franchisee, but is available to a franchisee or prospective franchisee in un-redacted form as part of normal franchise disclosure. However, for some franchise systems the information could easily be used to the detriment of a franchisee by its competitors.
12	Details of online sales, including profit sharing with franchisees.	Non-franchised networks do not have to publicly disclose their online strategy, or the details of the arrangements that apply to those involved in online sales. Although this information is relevant to a franchisee or prospective franchisee, it is available to a franchisee or prospective franchisee in unredacted form as part of normal franchise disclosure.

14.3 – 14.10	Details of all establishment and operating costs, including real estate, equipment, inventory, security deposit and working capital in extensive detail.	This important information for prospective franchisees is highly confidential and market sensitive for most franchise systems. If redaction of sensitive information is not permitted there is concern that franchisors will reduce the quality of information provided to prospective franchisees, knowing it is likely to end up in the hands of competitors or others who can use it to the detriment of the franchise system. This cuts across the fundamental purpose of disclosure.
15	Marketing fund information.	In most cases franchisors can provide this information without major concern. However, a small number of franchise systems would regard this information as highly confidential. For example, some cooperatives and buying funds.
20	Earnings information.	There seems no justification for providing earnings information publicly. Noting the proposed amendments already allow some redaction, the right to redact should be extended to any earnings information that is confidential and commercially sensitive.
21.1	Solvency statement to be provided.	Providing an assurance of solvency in the context of the signing of a franchise agreement is one thing. However, it is quite another to require this to be done in a publicly available document, that can then potentially be misused by third parties or others who might claim to have relied upon it. This is an unreasonable extension of potential third party liability.
21.2	Financial reports for the franchisor for the past 2 years.	This cuts across reporting obligations of exempt proprietary companies under the Corporations Act, and provides highly sensitive information to the general public.

On the other hand, the SME Committee believes the proposed level of redaction from the franchisors' Disclosure Documents, as set out in the draft legislation, is appropriate. It agrees with the principle that only franchise-specific information should be redacted from the franchisors' Disclosure Documents. In this regard, the SME Committee disagrees with the proposals from the CC Committee set out above to significantly expand the amount of information redacted from the franchisors' Disclosure Documents

6. Are the transitional arrangements appropriate?

The transitional arrangements appear appropriate, although much depends on the appropriate development of the portal. The link to the MyGovID seems a critical component, yet the Committees understands only individual identification is currently available.

7. Is the proposed portal functionality fit-for-purpose?

The answer to this question will largely be determined by prospective franchisees. The Government should carefully monitor use and utility. As previously noted, the Franchise Disclosure Register is certain to be used by third parties such as competitors, suppliers, landlords, debtors, creditors, employees, consumers and the media, rather than just prospective franchisees. The Department should be prepared to issue step by step guidelines to franchisors to help them establish their profile and upload their documents. It will also be critical to widely promote the existence of the Franchise Disclosure Register. Otherwise, prospective franchisees are unlikely to know it exists.

8. Do you have any other suggestions on how to ensure franchisees and users of the portal understand that information on the Franchise Disclosure Register is not endorsed or checked by Government?

The obvious strategy to try to avoid this risk, though not one guaranteed to be successful, would be for the Portal to include clear and prominent disclaimers that the information on the Franchise Disclosure Register had not endorsed or checked by Government. It is also important for the Australian Competition and Consumer Commission (**ACCC**) to develop and implement a clear communications strategy consisting of online guides, videos and brochures which explain all aspects of the Franchise Disclosure Register including that information on the Register is not endorsed or checked by either the Government or the ACCC.

Notwithstanding such a strategy, it is reasonable to expect that some prospective franchisees will assume that information on the Franchise Disclosure Register is somehow endorsed and checked by Government, or that a franchisor which is registered on the Franchise Disclosure Register carries some form of implicit endorsement. This seems unavoidable given that the Franchise Disclosure Register is established by the Government, the Secretary of the relevant Government Department is responsible for the administration of the Franchise Disclosure Register, access is via a Government website and there is reference to the MyGovID as a core part of the process. The Government has also publicly commented that the Franchise Disclosure Register will enhance transparency – see for example the following comment in the Guide accompanying the Exposure Draft.

These features will motivate high quality of disclosure practices, improving the comparability and symmetry of franchising information, and enhancing the franchising industry's reputation through open publication of information while delivering on the Government's commitments in the context of the 2021-22 Budget to implement a Register.

The major risk for the Government appears to be its functionality and utility, and whether it can in fact deliver on the foregoing commitment.

Some requirement should exist for the Government to monitor use and access. It is important to ensure the Franchise Disclosure Register is actually being used by prospective franchisees for the intended purpose, as opposed to being used predominantly by competitors and other third parties for commercial purposes.

Conclusion and further contact

The BLS would be pleased to discuss any aspect of this submission.

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