NEW ZEALAND FAIR TRADING COALITION

SUBMISSION

TO THE

MINISTRY OF ECONOMIC DEVELOPMENT

REVIEW OF FRANCHISING REGULATION IN NEW ZEALAND

DISCUSSION PAPER

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21 NOVEMBER 2008

Level 2, 79 Taranaki Street, PO Box 9244, Wellington, NZ Tel: 04 385 8859, Fax: 04 385 9517
www.nzftc.org.nz

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New Zealand Fair Trading Coalition
C/- Motor Trade Association

PO Box 9244, Marion Square, Wellington 6141, New Zealand
Level 2, 79 Taranaki Street, Te Aro, Wellington 6011, New Zealand
Tel: +64 4 385 8859, Fax: +64 4 385 9517 **www.mta.org.nz**

21 November 2008

Review of Franchising Regulation
Ministry of Economic Development
PO Box 1473
WELLINGTON 6140

Dear Sir / Madam

Submission: Review of Franchising Regulation In New Zealand

This submission is from:

New Zealand Fair Trading Coalition
PO Box 9244
Marion Square
Wellington 6141

The contact person in respect of this submission is:

Name: Andy Cuming
Title: Communications Manager
Ph: (04) 381 8803
Fax: (04) 385 9517
Email: andy.cuming@mta.org.nz

Thank you for the opportunity for NZFTC to provide comment on the Discussion Document.

Yours sincerely

Andy Cuming
Communications Manager

REVIEW OF FRANCHISING REGULATION IN NEW ZEALAND

Executive Summary

1. This is a submission made by the New Zealand Fair Trading Coalition (referred to as "**NZFTC**" throughout this submission). The submission is divided into four sections:

   (a) Introductory comments about the NZFTC;

   (b) General submission regarding the nature of the franchising relationship and the current law in New Zealand defining this relationship;

   (c) An analysis of international best practice; and

   (d) Specific comments regarding proposed options for reform.

2. The NZFTC is supportive of the Ministry of Economic Development's Review of Franchising Regulations and the Minister's public statements in recognition of the importance of providing protection to franchisees and improving the legal framework around franchising in order to promote sector growth, development and innovation.

3. In our submission, there should be specific legislation aimed at the franchise relationship. This legislation should regulate the conduct of all participants in franchising relationships, and should not merely protect franchisees.

4. Such legislation should be modelled on the Australian franchising code and should include the following key elements to enable an effective and efficient franchising relationship, which will in turn lead to the perception of a more equitable and efficient franchising regulatory system:

   (a) full disclosure setting out material information so that an informed decision can be made by franchisees prior to entering into a franchise agreement;

   (b) a seven day cooling off period in which a franchisee can decide to terminate a franchise relationship;

   (c) an obligation on the franchisee to obtain independent advice from a legal adviser, business adviser or accountant, about proposed franchise agreements into which they intend to enter;

   (d) details of lease terms relating to the franchisee's premises;

   (e) the right of a franchisee to form an association, or associate with, other franchisees;

   (f) the requirement for ongoing disclosure by franchisors of material changes to circumstances that will affect the franchisee or franchise;

   (g) the right of a franchisee to request a current disclosure document from the franchisor every 12 months;

   (h) the right of a franchisee to obtain audited statements from the franchisor relating to payments made by franchisees to a marketing or other cooperative fund;

   (i) efficient, timely and low cost dispute resolution proceedings (including a mandatory mediation service);

(j) a requirement for the franchisee and franchisor to receive sufficient notice and adequate reasons in advance of any termination of the agreement;

(k) provisions to enable the franchisee to on-sell the business if certain requirements are met and the approval of the franchisor is given, such approval not to be unreasonably withheld; and

(l) negotiation and consultation procedures for the franchisor to meet with each franchisee or a representative of the franchisee, with regard to proposed promotions.

5. In our submission, these protections should be encapsulated in a standalone statute and enforced by the Commerce Commission. Currently, the Commerce Commission has no franchise specific code, but plays an integral enforcement role in other industry specific legislation such as the Electricity Industry Reform Act 1998, the Dairy Industry Restructuring Act 2001, the Telecommunications Act 2001 and the Credit Contracts and Consumer Finance Act 2003.

6. Penalties for breach of the legislation should be similar to those set out in the Australian context, in order to ensure compliance, including injunctions, damages, enforceable undertakings, corrective advertising and other orders where appropriate.

7. Benchmarking reforms against those of Australia presents additional benefits. First, many franchises operate across both sides of the Tasman. Second, legislation passed to regulate the franchise relationship (if formulated in the same way as the mandatory franchise code of practice which operates in Australia), would have the additional advantage of furthering the harmonisation of substantive trans-Tasman competition law - a stated aim of both governments.

Introduction

8. The NZFTC makes the following submission to the Ministry of Economic Development Discussion Paper on the Review of Franchising Regulation in New Zealand ("**discussion document**").

9. The Ministry of Economic Development has invited submissions in the form of answers to ten questions arising from the discussion document. The NZFTC specific answers to the ten questions posed are attached as Annexure 1. We note, however, it is difficult to encapsulate a detailed response within these answers. We have, therefore, developed a more detailed and focused submission which is set out below.

10. The NZFTC is an informal group of like-minded organisations across several industries promoting best business practice, sound business ethics and fair and rigorous competition. The members of the NZFTC are:

- Road Transport Forum New Zealand Inc;
- Horticulture New Zealand;
- New Zealand Contractors Federation Inc;
- MTA - Motor Trade Association of New Zealand;
- New Zealand Building Subcontractors Federation;
- Electrical Contractors Association of New Zealand Inc;
- New Zealand Taxi Federation Inc;
- Engine Reconditioners Association;
- Brake and Clutch Specialists Association;
- Bus and Coach Association (New Zealand) Inc;
- New Zealand Heavy Haulage Association;
- Forest Industry Contractors Association; and
- Refrigeration Air Conditioning Companies Association.

11. NZFTC believe that a key issue facing the New Zealand economy is the realisation of the full potential of all business to contribute to growth, and that small and medium enterprises ("**SMEs**") have a significant role to play in this. However, there are real obstacles to this, as the playing field is not level. There are substantial and unfair barriers that constrain SMEs. This can threaten the viability of SMEs, smother their vitality, and hinder their capacity to grow and contribute fully to our national economic growth. NZFTC promotes liberating the potential of SMEs through legislative reforms in a number of key target areas. Those target areas are: prohibiting unconscionable conduct, allowing codes of practice; granting SMEs the right of collective bargaining; franchise law; and enhancing the SME contribution to the economy. As such, the NZFTC embrace the government's assertion that:

> …the best way a government can ensure SMEs maximise their contribution to the economy is through maintaining solid economic and social foundations (institutional, legal and regulatory) and facilitating an environment conducive to entrepreneurial behaviour.[1]

12. Franchising is a key business structure in New Zealand. Most franchises are small businesses, and franchisees as a species of small business are particularly vulnerable to exploitation and therefore particularly worthy of special legislative protection. Currently the relationship between franchisors and franchisees is not governed effectively, with inadequate protection afforded by the common law.

13. We would welcome an opportunity to discuss this submission with you if you consider it would be useful or necessary.

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[1] The Government response to the Small and Medium Business Advisory Groups Second Report 2006

14. For further queries please contact:

Andy Cuming
NZFTC Communications Manager
C/- The Motor Trade Association
PO Box 9244, Marion Square
Wellington 6141
(04) 381 8803
andy.cuming@mta.org.nz

Stephen Matthews
Chairman
New Zealand Fair Trading Coalition
C/- The Motor Trade Association
PO Box 9244, Marion Square
Wellington 6141
(04) 381 8820
stephen.matthews@mta.org.nz

The Franchise Relationship

15. Franchising is a business model involving a licensing distribution agreement. Essentially, it is the grant of a right to deal in goods and services with which the grantor is in some way connected. The franchisor offers a brand, systems development and support, and purchasing and strategic issues; while the franchisee focuses on its individual business operations, customer service, staffing and day to day matters concerning running of the business.

16. The vast global success of franchising has been replicated in New Zealand where franchising has seen considerable growth in recent years. Traditionally, a distinction has been drawn between different franchising models. The "business format franchise" has been the most popular model, where a franchisee essentially buys a copy of the franchisors business system, with no scope for individualism. "Product franchising", where a distributor supplies the product of a manufacturer, usually accompanied by an exclusivity clause but with business relations otherwise operating at arms length, and "manufacturing franchising", where an ingredient or substance or technical information is supplied, are variants. However in our submission, the distinction between differing franchising arrangements is largely academic, with limited relevance to real world franchise relationships which defy these tidy academic definitions. By way of example, petrol station franchising is often seen as a product franchise type arrangement, but in many cases has evolved from concern merely with brand distribution, towards a business format mode built around the "convenience store" concept. Similarly, many of the motor vehicle dealership franchises do not lie easily within the product franchise definition - rather, there are systems, reporting requirements, business planning, marketing concepts, day-to-day integration of across-the network initiatives, promotions, special offers and monitoring of performance that clearly demonstrate that the franchisor and franchisee do not operate at “arm’s length” in the way envisaged by the traditional concept of a product franchise.

17. The franchise relationship is unique. While it is not a fiduciary relationship in nature, franchise agreements are not like standard sale and purchase agreements either, necessitating ongoing cooperation between the parties. This uniqueness has been acknowledged by the courts. In *Dymock* the Privy Council recognised that franchise agreements are:

> … not ordinary commercial contracts but contracts giving rise to long term mutual obligations in pursuance of what amounts in substance to a joint venture and therefore dependant upon co-ordinated action and co-operation.[2]

18. This relationship of mutual advantage and interdependence is an attractive business model. From the franchisor's point of view, the business is run by self-motivated owner-operators, which means the franchisor does not have to employ staff and make the level of capital investment otherwise required; and from the franchisee's perspective, they get a business with a known brand which has proven goodwill.

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[2] *Dymock Franchises Systems (NSW) Pty Limited v Todd* [2004] 1 NZLR 289, 311

19. In return for the advantages the franchisee receives, they dispense with some of the autonomy they would otherwise hold over the business, and accept that there must be controls imposed by the franchisor in order to regulate the quality of the goods and services provided. Inevitably, a franchisor wants to minimise the risk of an ineffectual franchisee, not just on that particular branch outlet, but on all franchisees and therefore the franchisor as well. The franchisor minimises this risk through the use of often stringent minimum standards and control systems.

20. The success of a franchise is underpinned by the ongoing success of the relationship between the franchisor and the franchisee. For instance, the actions of a single small business franchisee can impact on the reputation of the whole network, and the reputation of the franchise is built up by the goodwill created in large measure by individual franchisees.

21. Thus, the franchisee's business differs in several key respects from standard small business entities. First, small business owners are not ordinarily accountable for the running of their business. Nor are they subject to restrictions regarding the manner in which they operate their business. Second, operation manuals and franchise agreements mean that, in effect, a franchisee cannot regard a franchise as their own business in the ordinary sense. The constraints under which they operate effectively mean that they are mere licensees and in some instances can expect to forfeit their entire investment in the event of a franchisor ending the franchise agreement.

22. There are a number of disadvantages arising from the franchise relationship, including the ongoing obligation the franchisee owes the franchisor in respect of the proportion of the profits made, restrictions on the market freedom of the franchisee to make their own business decisions and the potential for the franchisor to implement policy decisions that may adversely affect the franchisee's profitability levels or result in other detriments.

23. It is essential therefore, that the franchise agreement defines the entire basis of the relationship at the beginning, so that both parties know their rights and obligations prior to entering into the agreement. The franchisee in particular can otherwise be in a precarious position.

24. Due to the disparity in bargaining power, the ongoing nature of the franchise relationship and the level of co-operation required between the franchisor and franchisee, there are specific issues surrounding the relationship between franchisors and franchisees that cause concern. These include:

    (a) **disclosure of information**, including at the negotiation stage prior to entering into the franchise relationship, and during the relationship;

    (b) the conditions contained in the agreement, particularly the lack of an appropriate **cooling off period** and provisions for associations of franchisees;

    (c) **termination of the agreement** without good reason or without appropriate notice, particularly where it is due to no fault on the part of the franchisee;

    (d) **resolution of disputes** - litigation can be expensive, drawn out and favour the better resourced franchisor, necessitating alternative dispute resolution;

    (e) the franchisor has the **full and ultimate right to veto the on-sale** of the business of the franchisee which can be onerous; and

    (f) the **imposition of mandatory promotions** on franchisees without any discussion or negotiation with the franchisee regarding the effect that this will have on their business.

25. The provision of prescriptive obligations and remedies which span across the whole franchise relationship - from the early stage of negotiations through to the renewal of the agreement, ensures that adequate protection is afforded to the franchisee, who is, more often than not, in a comparatively weak position.

Existing New Zealand franchise law

26. It is uncontroversial to point out that in New Zealand, most businesses are small. What is perhaps more surprising however, is that the framework of commercial law governing the operation of businesses in New Zealand does not generally differentiate between large and small business entities.

27. The New Zealand regime differs in this regard from that of Australia, where amendments were made in 1998 to the Trade Practices Act 1974 ("**TPA**") enhancing the protection afforded to small businesses. In particular, these amendments allowed for the making of regulations under the TPA pertaining to specific sectors. One area that benefited from this was franchising, which saw the introduction of a mandatory code of practice.

28. Currently, no legislation exists in New Zealand specific to franchising. Rather, franchise relationships are governed by general commercial law provisions. In addition to the general principles of contract law and trade practices law, the following acts are relevant to franchising and the structure of franchise agreements:

    (a) Commerce Act 1986;

    (b) Fair Trading Act 1986;

    (c) Consumer Guarantees Act 1993; and

    (d) Employment Relations Act 2000.

29. Restrictions on anti-competitive conduct and price fixing are relevant to the structure of franchise agreements, including that the franchisor and franchisee remain separate legal entities under the agreement. Thus, under the Commerce Act, price fixing will still constitute anti-competitive behaviour. In addition, the Commerce Act requires that franchising must be conducted in a manner that does not substantially lessen competition or allow either party to abuse their market power and this has implications for the nature of the relationship and the provisions contained in the agreement.

30. In respect of general sanctions against misleading and deceptive conduct, the Fair Trading Act may be relevant. The Act enforces the common law torts of passing off, breach of confidence and infringement of trademarks, and may be particularly relevant where there has been unfair exploitation of reputation and goodwill of a franchise system. The Act provides more accessible reliefs against a former franchisee since it does not require actual loss in order to pursue a claim.

31. Both the Employment Relations Act and the Consumer Guarantees Act set out numerous restrictions and obligations which must be adhered to throughout the franchise relationship. No franchise agreement in and of itself may breach either Act.

32. However, in our submission, consumer legislation has not extended protection to retailers or customers of suppliers. The House of Commons Report "All Party Parliamentary Small Shops Group - High St Britain: 2015"[3] was commissioned to raise awareness amongst Parliamentarians regarding issues relating to SMEs - such as crime, excessive insurance, planning reforms, red tape and environmental legislation.

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[3] www.nfsp.org.uk/uploads/pdfs/High%20Street%20Britain%202015%20report.pdf

The Report highlighted concerns of how wafer thin margins and unfair competition from supermarkets impact on SMEs who in turn impact on the fabric of rural and urban life in the UK. The NZFTC considers that this report stimulates discussion on whether similar concerns exist in the NZ context.

33. Hammond J in *Dymock* commented that:

> The application of the traditional law relating to private contracts to franchising can lead to very unhappy results. Franchisors can impose onerous terms, and … use flimsy pretexts to terminate, thereby depriving the franchisee of a justified expectation.[4]

34. While good franchisors will be unlikely to use their dominant bargaining position or the franchisees financial ties inequitably, it is the actions of rogue franchisors and the potential for same that the law should be enacted to control. Recently, high profile cases where franchisees have been aggrieved by this lack of protection have informed public opinion, and highlighted the need for a franchise-specific legislative regime. Although these cases are being investigated with a view to pursuing franchisors under existing legal remedies, the mere incidence of cases where franchisors have conducted themselves in an unfair and brinkmanship like manner, has highlighted the vulnerability of franchisees. This in turn has placed importance on creating a form of franchise-specific regulation to enhance current contractual arrangements.

35. Voluntary self regulation currently operates through the Franchise Association of New Zealand Inc ("**FANZ**"). FANZ has an established framework involving a Code of Practice, a Code of Ethics and a scrutineering process. Despite the virtue of the current code operated by FANZ, the voluntary nature of the regime means it is ineffective in targeting unscrupulous franchisors. Currently less than half those operating within a franchise system in New Zealand belong to FANZ, with those that do being overwhelmingly made up of franchisors. This results in a disparity between the standards of industry players, allows scope for unfairness, and perhaps more importantly, the perception of unfairness.

36. FANZ itself favours regulation of the sector through law rather than the voluntary code which it operates. FANZ has publicly stated that the impact of regulations on those that currently comply with the code is likely to be minimal. NZFTC finds this argument compelling. Those that it will impact on, are those that currently do not subscribe to the voluntary code of conduct operated by FANZ. Not only will this capture current rogues operating outside the voluntary code, it will also enhance perception of the viability of the industry and will promote the development of the franchise business model.

37. Further, in its *Review of Franchising Code of Conduct* in May 2000, the Australian Government Policy Council concluded that the benefits of franchise legislation outweighed the cost of compliance:

> Procedures imposed to regulate an industry invariably involve a cost. Regulation is beneficial if it reduces or combats what would otherwise be more costly developments, such as an increase in litigation or economic and social distortions caused by predatory business behaviour. There is a trade-off between costs associated with regulatory compliance and the benefits obtained from enhancing conduct and the image of the franchising industry.[5]

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[4] *Dymock Franchise Systems (NSW) Pty Limited v Bilgola Enterprises Limited* (1999) 8 TCLR 612, per Hammond J

[5] http:// Pandora.nla.gov.au/plan/31583/20021018-0000/www.industry.govt.au/library/content_library/ReviewofFCoc.pdf

38. There is no reason to suggest that the New Zealand franchising environment is materially different to that in Australia prior to its introduction of franchise-specific legislation. Regardless of how high-profile or not this problem appears to be, it is submitted that the Government should consider the Australian experience, and the rationales given for progressing legislation in that country to solve the issues outlined in our submission.

An international perspective

Australia

39. Before the introduction of franchise-specific regulation in Australia, franchise relationships operated under a similar system of self-regulation as currently operates as New Zealand's voluntary regime.

40. Australia implemented a Franchising Code of Practice in 1993. This was widely viewed as ineffective due to compliance remaining voluntary and that several key factors of the franchising industry chose not to be covered by that Code. This included motor vehicle dealerships and real estate franchises. Franchisors who rejected coverage by the Code gained a competitive advantage over those franchisors who did comply due to the compliance costs involved. It therefore became apparent that, to be effective, the Code needed to be mandatory for all industry players.

41. Part IV of the TPA implemented the Franchising Code of Conduct ("**Code**") in July 1998, which represents the watermark as the most prescriptive franchising regulations globally. The Code was primarily introduced to outline the rights and responsibilities of franchisors to franchisees, and includes particular requirements of disclosure of information, the provision of a cooling off period, and prohibitions against unconscionable conduct.

42. The Code provides that:

    (a) there must be a formal disclosure document in order to provide franchisees with the material information necessary to make an informed decision prior to entering a franchise agreement;

    (b) there must be ongoing disclosure on the part of franchisor of any material changes in circumstances affecting the franchisee

    (c) there must be a seven day cooling off period from the time of signing the agreement or the payment of money in which the franchisee can terminate the agreement;

    (d) franchisees must obtain independent advice from a legal or business advisor or an accountant and there must be a signed statement to this effect;

    (e) franchisors cannot prevent franchisees from forming associations with one another; and

    (f) in the event of disputes arising, the Code provides a dispute resolution process which must be adhered to. In particular, either party can require the other to attend mediation if the dispute cannot be resolved through any processes that may be set out in the franchise agreement itself. These provisions are aimed at making dispute resolution faster and more affordable and act as somewhat of a self-help mechanism for franchisees with concerns about a franchisor's conduct. The Franchising Australia 2004 Survey states that the Code has been effective in the area of dispute resolution with significantly more disputes being resolved through mediation rather than litigation.

43. Compliance with the Code in Australia is mandatory, although registration with a central body for "approval" is not required prior to the commencement of franchising. The Code has the force of law and contravention of the Code constitutes a breach of the TPA.

44. The Code has many features from its predecessor, the Code of Practice, maintained by the Franchise Association Australia and New Zealand, the predecessor body to the present Franchise Council of Australia (and FANZ). The main thrusts are therefore also the foundations for the Code of Practice in New Zealand, the key difference being that one is mandatory and the other only binds those who are voluntary members (being less than half the people involved in the franchising industry in New Zealand).

45. The Code is enforced by the Australian Competition and Consumer Commission ("**ACCC**"), and the penalties for breaching the Code include those available under the TPA and provides for such remedies as injunctions, corrective advertising, damages and the possibility of other orders that are necessary. Franchisors failing to meet the provisions of the Code may be liable for compensation and refunds as well as penalties of up to AUD200,000 for corporations and AUD40,000 for individuals.

46. The ACCC may also take representative actions on behalf of franchisees, and they have done so in a number of instances, particularly where the public interest is concerned. Where a franchisor has failed to comply with the Code or has used their strong bargaining position to the disadvantage of the franchisee, the ACCC will consider taking action on behalf of the franchisee. However, if the matter is a private dispute, private legal action will be recommended.

47. The Code has been hailed as a success in Australia and has addressed the majority of problems and perceived problems in relation to franchising relationships. Moreover it has succeeded in creating a more level playing field for small business franchisees in their negotiations with large organisations. These small business franchisees, as in New Zealand, make up the majority of franchisees in the Australian context. There appears also to have been a high level of acceptance of the Code within the franchising industry. Indeed, there has been an 8% increase per annum in franchising relationships showing a healthy growth in industry and therefore the economy.

48. The Code has not been without criticism. For instance, one of the perceived defects was bad definitional drafting. However, some regulatory changes were made to the Code in 2001, including the introduction of a short formal disclosure document involving fewer disclosure requirements for franchisors with a turnover of under AUD50,000 a year. There are, of course, some industry members who believe the Code has not gone far enough and that further reforms are necessary to further level the playing field in which the franchise industry operates to enhance fairness and efficiency.

United States

49. In the United States the offer and sale of franchises is regulated by federal law. This is administered by the Federal Trade Commission ("**FTC**"), where it has similar responsibilities to our Commerce Commission or the ACCC that operates in Australia.

50. The Trade Regulation Franchising Business Opportunity and Ventures requires sellers to disclose certain pre-sale financial and other information to prospective purchaser before they pay any money or sign an agreement. For a number of years Congress has been basing the need for a federal statute to govern other aspects that arise in the relationship between the franchisor and franchisee after sale and purchase. This is because a number of matters cannot be addressed within the scope of the current legislation or by the FTC. The need for such legislation is strongly advocated by the American Franchisee Association.

51. Many states have enacted additional statutes or regimes which vary in the degree of regulation they impose due to the perceived inadequacy of this federal law. Fifteen states have franchise investment laws, requiring franchisors to provide pre-sale disclosure. Thirteen of these states treat the sale of a franchise like the sale of security, whereby an offer for or sale of a franchise within their state was prohibited until a franchise offering circular has been filed on public record and registered by a designated state agency. Eight of them also give franchise purchasers legal rights such as the right to bring private law suits for violation of the state's disclosure requirements. The FTC itself does not require filings of franchise disclosure documents or offering circulars. The result is that some states are significantly more or less attractive than others as places in which to establish franchises.

52. Changes were adopted to federal regulations effective 1 July 2007, fully effective 1 July 2008, to make life a little easier. For example, the timing requirements as well as the content detail requirements regarding the provisions of disclosure documents were changed. These changes are considered to remove significant barriers which franchisors previously faced in expanding their businesses in the USA.

53. Gasoline and automobile dealers make up a large proportion of the revenue generated by franchising in the United States. They have specific franchise relationship protections dedicated to them in the form of the Automobile Dealers Day In Court Act and Petroleum Marketing Practices Act. These laws provide minimal standards for general good faith business practices.

Canada

54. The Canadian franchise system operates in a non-regulatory environment akin to the current New Zealand position. The Canadian Franchise Association ("**CFA**") is in fact very similar to FANZ. They have a code of ethics that all members are required to adhere to and have a disclosure document which describes the minimum level of disclosure required by members of the CFA. However, the CFA restricts its membership to only those franchisors who commit to adhering to its code of ethics and the mandatory disclosure requirements. In addition, prospective members are screened and must meet specified standards.

55. Some provinces, however, have introduced specific franchise legislation, such as Alberta and Ontario. As such, companies franchising within Ontario or Alberta must follow the legislative requirements in those provinces - being the Alberta Franchises Act 1995 and the Arthur Wishart Act (Franchise Disclosure) 2000 in Ontario. Both Acts provide for full disclosure of relevant facts and offer extra measures of protection to prospective franchisees. They also require a duty of fair dealing on each party to a franchise agreement and provide for actions and damages for misrepresentation and for failure to provide the required disclosure. Such actions can be brought against the franchisor and every person who signs the disclosure document. Lastly, there are sections to ensure franchisees have the right to associate freely and to form organisations among themselves.

European Union ("EU")

56. Members of the EU have divergent laws being a mixture of both individual national laws and overarching EU laws. Within the EU, franchising is governed by general laws relating to contracts and by Article 81(1) of the European Commission Treaty ("**EC Treaty**"), which contains restrictions applying to all franchise agreements, particularly restrictions regarding competition. However, a franchise agreement will not fall within the provisions of Article 81 of the EC Treaty if the agreement does not include restrictions on the liberty of the contracting parties which go beyond those that are necessary concomitants of a franchising system.

Furthermore, certain factors are inherent in the nature of the franchise agreement and are outside the scope of Article 81, such as:

(a) exclusive delivery and supply obligations, in so far as they are intended to ensure a standard selection of goods;

(b) uniform advertising and shop layouts; and

(c) a prohibition on selling goods supplied under the contract in other shops.

57. The European Court of Justice has held that the mere fact that a franchisor makes price recommendations to the franchisee will not constitute a restriction on competition, provided that there is no concerted practice between the franchisor and franchisee or between franchisees themselves for the actual application of such prices.

58. Franchise agreements are covered by the block exemption European Community Commission regulations 2790-99. The exemption applies to vertical agreements containing provisions that relate to the assignment to the buyer or use by the buyer of intellectual property rights, provided those provisions to not constitute the primary object of such agreements and are directly related to the use, sale or resale of goods or services by the buyer to its customers.

59. The European Franchise Federation encompasses 18 national franchise associations and promotes the European code of ethics for franchising.

60. An example discussed in *Lawtalk* 699 last year illustrates the idiosyncratic nature of EU law. This featured in the decision of the House of Lords in *Lonsdale v Howard and Hallams Limited* [2006] EWA civ 63. In *Lonsdale* an exporter using an agent within the EU with whom there was no written agreement was required to pay substantial compensation for terminating the agreement, a figure calculated on the notional capital value to what the agency might have to a hypothetical purchaser of the business at the time of termination, presumably assuming that it could not in fact be cancelled. Rights to the compensation accrued even when the termination was on expiry of an agreed term. Apparently a more formalised licensing or distribution or franchise agreement might have been effective in preventing the problem.

United Kingdom ("UK")

61. The UK does not have a specific regulatory scheme in relation to franchising, instead relying on a combination of generic legislation and self-regulation of the sector through voluntary membership of the British Franchising Association ("**BFA**").

62. The matter has been debated several times in the UK with successive governments reaching the conclusion that there is not enough evidence in the UK context that franchises are more risky than other forms of business to warrant special controls around them. Thus, in the UK context, regulation through the BFA is considered to be the most effective way of regulating franchising.

Unidroit

63. The International Institute for the Unification of Private Law ("**Unidroit**") is an independent intergovernmental organisation. Its purpose is to study needs and methods for modernising, harmonising and co-ordinating private and in particular commercial law as between States and groups of States. Unidroit's basic statutory objective is to prepare modern, and where appropriate, harmonised uniform rules of private law.

64. Membership of Unidroit is restricted to States acceding to the Unidroit Statute. Unidroit's 61 member States are drawn all around the world and represent a variety of different legal, economic and political systems as well as different cultural backgrounds. New Zealand is not a member State (note, however, that Australia, the United States, and the United Kingdom are).

65. In 2002 the Governing Council of Unidroit adopted a Model Franchise Disclosure Law ("**Model Law**"). The Model Law is not an international convention. Instead it is intended to be more flexible, to permit States to make changes they consider to be necessary to cater for the specific needs of the country. It is intended to provide national legislators who have decided that legislation specifically aimed at franchising should be introduced into their legal system with an instrument that they may consult and use as a model or blueprint should they deem it appropriate.

66. The Explanatory Report of the Model Law states that:

> The Model Law is intended to encourage the development of franchising as a vehicle for business. As a pro-commerce document, it recognises that franchising offers the potential of increased economic development, especially among countries seeking access to know-how.

67. The Model Law is a disclosure law, intended to create a secure legal environment between all the parties in a franchise arrangement. It ensures that prospective franchisees who intend to invest in franchising receive material information about franchise offerings, in order for them to make informed investment decisions. Unidroit decided that a disclosure law (limited to the regulation of the information that a franchiser should provide a prospective franchisee) was more appropriate than relationship laws (which regulate specific terms of the franchise relationship) because during its research it discovered that the experience of States with relationship laws had been negative, whereas experience with disclosure legislation had on the whole been positive.

68. The Model Law is limited to pre-contractual disclosure. It is intended to apply to both domestic and international franchising, and to different types of franchise agreement, such as traditional unit agreements, master franchise agreements and development agreements. It does not require disclosure on the part of the franchisee, only the franchisor, recognising the imbalance between the parties as regards experience and economic size.

Proposals for reform

69. For the most part, franchisees operating in the western developed world enjoy greater protection than they do in the New Zealand context. In our submission, the need for reform here is clear.

70. FANZ have recently made public statements in support of regulation. This is major recognition that voluntary regulation of the sector through the FANZ Code of Practice and Code of Ethics has significant limitations.

71. This is buffered by statistics indicating that less than half of those operating within the franchise industry in New Zealand have signed up to the self-regulatory model operated by FANZ.

72. In our submission, mere education of the sector affords insufficient protection. FANZ has a wide range of information on its website advising potential franchisees steps to take and matters to consider prior to entering into a franchise agreement. However, the problem remains that this education may not reach those most vulnerable and at risk, that it will fail to alter public perception and will fail to bring about any tangible change in respect of the current problems faced by those in, or looking to enter the franchising industry.

73. Different options include:

    (a) making membership of FANZ mandatory;

    (b) making the FANZ code mandatory; and/or

    (c) creating a statutory franchising body with membership from the franchising sector to oversee franchising arrangements.

74. While the first two options are preferable to the status quo, questions are raised regarding how this process would be funded and enforced.

75. In our submission, the Commerce Commission is best placed to enforce franchise-specific regulation, as with their Australian counter-part, the ACCC. The Commerce Commission has extensive experience monitoring information disclosure regimes and its Australian equivalent, the ACCC, has had success in specifically dealing with franchising. Use of the Commerce Commission to incorporate franchise-specific legislation into its current work stream would have the added benefit of reducing initial and ongoing costs of a regulatory regime for franchising.

76. Such legislation should be modelled on the Australian franchising code and should include the following key elements to enable an effective and efficient franchising relationship, which will in turn lead to the perception of a more equitable and efficient franchising regulatory system:

    (a) full disclosure setting out material information so that an informed decision can be made by franchisees prior to entering into a franchise agreement;

    (b) a seven day cooling off period in which a franchisee can decide to terminate a franchise relationship;

    (c) the obligation on the franchisee to obtain independent advice from a legal adviser, business adviser or accountant about proposed franchise agreements into which they intend to enter;

    (d) details of lease terms relating to the franchisee's premises;

    (e) the right of a franchisee to form an association or associate with other franchisees;

    (f) the requirement for ongoing disclosure by franchisors of material changes to circumstances that will affect the franchisee or franchise;

    (g) the right to request a current disclosure document from the franchisor every 12 months;

    (h) the right to obtain audited statements from the franchisor relating to payments made by franchisees to a marketing or other cooperative fund;

(i) efficient, timely and low cost dispute resolution proceedings (including a mandatory mediation service);

(j) a requirement for the franchisee to receive sufficient notice and adequate reasons in advance of any termination of the agreement by the franchisor;

(k) provisions to enable the franchisee to on-sell the business if certain requirements are met and the approval of the franchisor is given, such approval not to be unreasonably withheld; and

(l) negotiation and consultation procedures for the franchisor to meet with each franchisee or a representative of the franchisee with regard to proposed promotions.

Information disclosure

77. Adequate information disclosure is paramount in order to address inequities in the franchisor/franchisee relationship. Mandatory information disclosure would require franchisors to give specified information to potential franchisees prior to any agreement being entered into. This is essentially a due diligence requirement, ensuring that franchisees have the necessary information before entering into a franchise relationship. Information disclosure is a key aspect of the FANZ code and the mandatory code in Australia. It is also a key element of the Unidroit model.

78. The likely impact of mandatory information disclosure would be two-fold. First, it would help address the problem of information imbalance between franchisors and franchisees. Second, there would be likely flow on effects - for instance, reducing the number of contractual disputes that arise and the need for these disputes to be litigated.

79. In the Australian context, disclosure requirements have grown significantly from when the code was first introduced and there have been concerns expressed by franchisors that compliance costs have become onerous. However in the Department of Employment, Workplace Relations and Small Business *Review of the Franchising Code of Conduct* ("**Review**") it was reported that although a majority of franchisees interviewed claimed they had to alter their disclosure practices (including seeking external legal and accounting advice), a majority also claimed the Code did not have a significant impact on compliance costs, as a percentage of annual turnover.[6] Notably, the Review states that:

> It is encouraging to observe that the majority of survey respondents incurred either a compliance cost of less than one percent of turnover per annum, or no measurable costs. The few comments about costs from respondents indicate that costs are not a problem for franchisors. No actual dollar figures for costs were sought because a cost figure in isolation is meaningless unless it can be related to the overall turnover figure for the particular business. To this extent, some earlier indications from the industry of an occasional high cost figure may need to be re-examined.[7]

80. Arguably, once the initial information systems are set up it would be relatively simple to keep them up to date for release to other prospective franchisees. From a policy perspective, the importance of full disclosure of all necessary and relevant information trumps any small compliance costs to individual franchisors.

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[6] Department of Employment, Workplace Relations and Small Business, *Review of the Franchising Code of Conduct: Report of the Franchising Policy Council*, May 2000, p 80.
[7] Ibid, p 81.

81. A more complex set of disclosure requirements would, in our submission, be unlikely to deter overseas franchisors from entering into franchise relationships in New Zealand, particularly where we move to harmonise our laws with those of Australia, where there are an onerous set of disclosure requirements required prior to entering a franchise relationship and which continue throughout that franchise relationship.

82. Although there was a decline in the growth of the franchising sector in Australia initially after the introduction of the mandatory code, the industry quickly recovered and has in fact seen substantial growth of around 8% per annum. In our submission, this is because public confidence and a better working system have strengthened the franchising sector overall.

A seven day cooling off period and provision for associations of franchisees

83. The requirement to provide for a seven day cooling off period is a feature of the current FANZ code of practice and the mandatory code that operates in Australia. This mechanism would have the likely effect of preventing pressure sales. Some commentators have suggested that the requirement to provide for a seven day cooling off period could lead to unduly harsh trade restriction clauses following the termination of the agreement. In our submission, such clauses would be unlikely to be enforceable within wider contract law.

84. Freedom of association of franchisees is an important mechanism to provide a support base for what are usually small businesses, operating within a restricted framework.

Prohibition against the termination of the franchise agreement without good reason or without appropriate notice; the franchisor having the full and unlimited right to veto the on-sale of the business; and the imposition of mandatory promotions on franchisees.

85. The Franchise Council of Australia asserts:

> By nature the relationships in the franchise agreement will be imbalanced in favour of the franchisor, as the franchisor must at all times remain in control of a set of standards critical to the ongoing success of the business format.[8]

86. A corollary of the retention of control by franchisors is that rogue franchisors are able to take advantage of broad termination provisions to force franchisees to agree to concessions or accept changes to the franchise agreement or to act unfairly in a way which is detrimental to the franchisee and their business.

87. This potential exists irrespective of the specific industry in which the franchise operates. Whether in fact the franchisors who have tended to exhibit this right have mainly been sourced in particular industries is largely irrelevant to the potential scope of the problem and indeed, the perception of that problem.

88. Many franchisees face hefty start up expenditure including an initial franchise fee but also a requirement to purchase equipment and inventory or fit out their premises in order to commence business. For many small business owners/franchisees this will be a significant outlay. In a 2003 survey of franchising, the average total start up costs for franchisees in New Zealand was recorded as $132,000.

89. These start up costs make a franchisee particularly vulnerable where franchisors have a contractual right to unilaterally terminate the relationship without just cause and with minimal notice periods, to impose mandatory promotions and to veto the on sale of the franchise business to a third party.

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[8] See www.franchise.org.au.

Mandatory dispute resolution clause

90. Litigation can be expensive, drawn out and favour the better resourced franchisor. Moreover, litigation is counterintuitive to the interdependent nature of franchising relationships.

91. The provision for alternative dispute resolution, a feature of both the FANZ and the Australian codes, is a low cost alternative for disputes to be settled and proffers a successful ongoing relationship between the parties.

Conclusion

92. The importance of small business to the New Zealand economy cannot be overstated. For the continued success and expansion of one of its most charismatic integrants, franchising, legislation is required to prevent considerable scope for exploitation and unfairness (or even the perception of unfairness), that exists under the present common law regime.

93. In order to grow and increase in momentum, the New Zealand franchise industry is in need of specific regulatory control. In our submission, franchise-specific legislation should be passed to regulate the franchise relationship, modelled on the Australian code and administered by the Commerce Commission. As an alternative, a mandatory franchise code of practice could be implemented and enforced by a government department, to improve on the current situation.

94. In the absence of specific legislation, franchising disputes, such as those which have been prominent in the media recently, are likely to continue to tarnish the franchising industry. Franchisees are likely to be exposed to unnecessary risk, incorrect or misleading information, franchise failure and unconscionable conduct by rogue franchisors. Potential franchisees are likely to be deterred.

95. In our submission, the argument that a regulatory regime defining the rights and obligations of those engaged in franchise agreements would have a chilling effect on the growth of franchises is baseless. Extensive protection for franchisees in the US and Australia has not resulted in any decrease in the growth of franchise business, in fact, the converse has been true. The effect has been to create certainty and therefore promote growth.

96. The desirability of closer economic relations with Australia and the harmonisation of substantive trans-Tasman competition law further supports the adoption of franchise-specific legislation akin to Australia, particularly given that many existing franchises (and likely franchise operations) will operate at a trans-Tasman level.

ANNEXURE 1

Q1 Are there any particular features about franchise contracts that mean that potential and existing franchisees require further protection?

97. The franchise relationship is distinct from other business relationships. The relationship is one of mutual interdependence which necessitates an ongoing relationship, and is governed by relational contracts, much like a joint venture.

98. In practice, franchise agreement contracts tend to be very one sided, in favour of the franchisor. A typical franchise agreement excerpt shows the tenor of such agreements:

> The franchisor and related companies have developed a unique and integrated system…for the design and operation of retail stores specialising in the sale of books, magazines, stationery and other associated items…The Dymocks system is a comprehensive retail sales system. Its foundation and essence is the strict adherence by Franchisees to standards, specifications, procedures and policies of the Franchisor providing for the uniform operation and image of all Dymocks stores…
>
> The most important management and control device in the regulation of our franchise System is the Franchise Agreement…strict adherence by the Franchise owner to all the terms in the Agreement is absolutely essential as any deviation may have catastrophic effects on every Store in the chain…Uniformity within our whole Franchise System is the overriding objective and the Franchise Agreement has been written to protect this vital interest…Your rigid application of the terms of the Franchise Agreement will assist with the development of a mutually rewarding experience with Dymocks. Dymocks' role is to advise on and control the standards at every franchise and we will be uncompromising in doing so for the overall benefit of all franchise Owners as a whole.[9]

99. The very essence of the franchise relationship means that there is a systemic power imbalance between franchisor and franchisee, and it is this power imbalance that the law has an important role in protecting against, particularly in light of the potential excesses which franchisors may exercise.

100. Thus, franchisees warrant the laws protection through the provision of prescriptive obligations and remedies which span across the whole franchise relationship. The provision of such protective measures will in turn lead to the perception of a more equitable and efficient franchising regulatory system, promoting sector growth.

Q2 Have the problems been defined correctly? Are there other problems?

101. The discussion document has, in our submission, correctly identified and defined four particular problems with the current regulatory framework regarding franchising:

(a) information imbalance;

(b) barriers to resolving disputes;

(c) contractual power imbalance; and

(d) public perception.

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[9] The opening section of the Operations Manual of the Dymocks Bookshop franchise; reproduced in *Dymocks* (1999) 8 TCLR 612, 679, 689 quoted in Adhar, R. *The Franchise as a Cultural and Legal Phenomenon,*

102. However, in our submission, there are further problematic areas for concern. These include:

(a) the lack of an appropriate cooling off period in which a franchisee can decide to terminate a franchise relationship;

(b) the lack of provisions giving franchisees the right to form an association or associate with other franchisees;

(c) the imposition of mandatory promotions on franchisees without any discussion or negotiation with the franchisee regarding the effect that this will have on their business;

(d) no requirement for ongoing disclosure by franchisors of material changes to circumstances that will affect the franchisee or franchise;

(e) no right to regularly request a current disclosure document from the franchisor; and

(f) no right to obtain audited statements from the franchisor relating to payments made by franchisees to a marketing or other cooperative fund.

Q3 What is the magnitude of these problems? Do they apply to the franchising sector as a whole, or are they specific to particular types of franchising or particular industries?

103. In our submission, the problematic nature of franchise relationships is inherently systemic.

104. The Franchise Council of Australia asserts:

> By nature the relationships in the franchise agreement will be imbalanced in favour of the franchisor, as the franchisor must at all times remain in control of a set of standards critical to the ongoing success of the business format.[10]

105. A corollary of the retention of control by franchisors is that rogue franchisors are able to take advantage of broad termination provisions to force franchisees to agree to concessions or accept changes to the franchise agreement or to act unfairly in a way which is detrimental to the franchisee and their business.

106. This potential exists irrespective of the specific industry in which the franchise operates. Whether in fact the franchisors who have tended to exhibit this right have mainly been sourced in particular industries is largely irrelevant to the potential scope of the problem and indeed, the perception of that problem.

107. Many franchisees face hefty start up expenditure including an initial franchise fee but also a requirement to purchase equipment and inventory or fit out their premises in order to commence business. For many small business owners/franchisees this will be a significant outlay. In a 2003 survey of franchising, the average total start up costs for franchisees in New Zealand was recorded as $132,000.

108. These start up costs make a franchisee particularly vulnerable where franchisors have a contractual right to unilaterally terminate the relationship without just cause and with minimal notice periods, to impose mandatory promotions and to veto the on sale of the franchise business to a third party.

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[10] See www.franchise.org.au.

109. The discussion document suggests that it has been only product franchisees that have been affected by the unilateral cancelling of the franchise relationship without reason or sufficient notice. Putting aside the problematic nature of the definition of product franchise discussed earlier in the submission, the potential for abuse in this area relates to all franchising relationships. It is in fact possible because of the very nature of the power imbalance between franchisor and franchisee, and as such, all franchisees are vulnerable. This is particularly so where franchisees are small business owners with less business acumen, and have invested significant set up costs. In our submission, this is a power imbalance that warrants a form of franchise-specific regulation to enhance current contractual arrangements.

Q4 and Q5 Which of the options outlined do you favour? Why? Have all of the options (and sub-options) been identified or are there others that should be considered?

110. NZFTC favour Option 3 - the implementation of franchise-specific regulation. More specifically, NZFTC favour the following sub-options (giving further detail as regards these options where necessary):

(a) *Option 3.1 - Mandatory information disclosure*:

(i) Adequate information disclosure is paramount in order to address inequities in the franchisor/franchisee relationship. The likely impact of mandatory information disclosure would be two-fold. First, it would help address the problem of information imbalance between franchisors and franchisees. Second, there would be likely flow on effects - for instance, reducing the number of contractual disputes that arise and the need for these disputes to be litigated.

(b) *Option 3.2 - Mandatory professional advice*:

(i) The obligation on the franchisee to obtain independent advice from a legal adviser, business adviser or accountant about proposed franchise agreements into which they intend to enter should be included in all franchise agreements.

(c) *Option 3.3 - Cooling off period*:

(i) The requirement to provide for a seven day cooling off period is a feature of the current FANZ code of practice and the mandatory code that operates in Australia. This mechanism would have the likely effect of preventing pressure sales.

(ii) Some commentators have suggested that the requirement to provide for a seven day cooling off period could lead to unduly harsh trade restriction clauses following the termination of the agreement. In our submission, such clauses would be unlikely to be enforceable within wider contract law.

(d) *Option 3.4 - Enhanced dispute resolution*:

(i) This should be efficient, timely and low cost and include a mandatory mediation service.

(e) *Option 3.5 - Rules for franchising contracts*:

(i) These rules are necessary due to the power imbalance between franchisors and franchisees. Rules should include:

(aa) a prohibition against the termination of the franchise agreement without good reason or without appropriate notice;

(bb) a prohibition against the franchisor having the full and unlimited right to veto the on-sale of the business;

(cc) a prohibition against the imposition of mandatory promotions on franchisees, with negotiation and consultation procedures for the franchisor to meet with each franchisee or a representative of the franchisee with regard to proposed promotions;

(dd) details of lease terms relating to the franchisee's premises;

(ee) the right of a franchisee to form an association or associate with other franchisees, which is an important mechanism to provide a support base for what are usually small businesses, operating within a restricted framework;

(ff) an obligation on the franchisee to obtain independent professional advice; and

(gg) a dispute resolution clause.

(f) *Option 3.8 - The Commerce Commission taking responsibility for monitoring and enforcing franchise-specific regulation:*

(i) The Commerce Commission is best placed to enforce franchise-specific regulation, as with their Australian counter-part, the ACCC. The Commerce Commission has extensive experience monitoring information disclosure regimes and its Australian equivalent, the ACCC, has had success in specifically dealing with franchising.

(ii) Use of the Commerce Commission to incorporate franchise-specific legislation into its current work stream would have the added benefit of reducing initial and ongoing costs of a regulatory regime for franchising.

Q6 If information disclosure is to be introduced, which classes of information should be required to be disclosed?

111. Adequate information disclosure is paramount in order to address inequities in the franchisor/franchisee relationship. The following should be required:

(a) full disclosure setting out material information so that an informed decision can be made by franchisees prior to entering into a franchise agreement;

(b) the requirement for ongoing disclosure by franchisors of material changes to circumstances that will affect the franchisee or franchise;

(c) the right to request a current disclosure document from the franchisor every 12 months; and

(d) the right to obtain audited statements from the franchisor relating to payments made by franchisees to a marketing or other cooperative fund.

112. Mandatory information disclosure would require franchisors to give specified information to potential franchisees prior to any agreement being entered into. This is essentially a due diligence requirement, ensuring that franchisees have the necessary information before entering into a franchise relationship. Information disclosure is a key aspect of the FANZ code and the mandatory code in Australia. It is also a key element of the Unidroit model.

113. The likely impact of mandatory information disclosure would be two-fold. First, it would help address the problem of information imbalance between franchisors and franchisees. Second, there would be likely flow on effects - for instance, reducing the number of contractual disputes that arise and the need for these disputes to be litigated.

114. In the Australian context, disclosure requirements have grown significantly from when the code was first introduced and there have been concerns expressed by franchisors that compliance costs have become onerous. However, arguably, once the initial information systems are set up it would be relatively simple to keep them up to date for release to other prospective franchisees. The majority of Franchisors in the Australian context admitted that the Australia Franchising Code did not have a significant impact on compliance costs as a percentage of annual turnover. From a policy perspective, the importance of full disclosure of all necessary and relevant information trumps any small compliance costs to individual franchisors.

115. A more complex set of disclosure requirements would, in our submission, be unlikely to deter overseas franchisors from entering into franchise relationships in New Zealand, particularly where we move to harmonise our laws with those of Australia, where there are an onerous set of disclosure requirements required prior to entering a franchise relationship and which continue throughout that franchise relationship.

116. Although there was a decline in the growth of the franchising sector in Australia initially after the introduction of the mandatory code, the industry quickly recovered and has in fact seen substantial growth of around 8% per annum. In our submission, this is because public confidence and a better working system have strengthened the franchising sector overall.

Q7 and Q8 What are the benefits and cost and risks of each of the options (including any further options)?

Status quo - generic legislation and self-regulation

117. In our submission, the cost would be negligible, but the risk significant.

118. Voluntary self regulation currently operates through the FANZ. FANZ has an established framework involving a Code of Practice, a Code of Ethics and a scrutineering process. Despite the virtue of the current code operated by FANZ, the voluntary nature of the regime means it is ineffective in targeting unscrupulous franchisors. Currently less than half those operating within a franchise system in New Zealand belong to FANZ, which results in a disparity between the standards of industry players, allows scope for unfairness, and perhaps more importantly, the perception of unfairness.

119. Self regulation "…does not work…because it is expecting too much of human nature in light of the overwhelming influence of competitive forces."[11]

Education

120. In our submission, the cost would be limited, as would the likely success.

[11] Goode, R. *Commercial Law in the Next Millennium,* London, 1998, 48.

121. Mere education of the sector affords insufficient protection. FANZ has a wide range of information on its website advising potential franchisees steps to take and matters to consider prior to entering into a franchise agreement. However, the problem remains that this education may not reach those most vulnerable and at risk, that it will fail to alter public perception and will fail to bring about any tangible change in respect of the current problems faced by those in, or looking to enter the franchising industry.

Co-regulatory regime

122. In our submission, forced membership of FANZ is preferable to the status quo, as levels the playing field. However, enforceability may be an issue.

123. While either making membership of FANZ mandatory, making the FANZ code mandatory, an/or creating a statutory franchising body with membership from the franchising sector to oversee franchising arrangements is preferable to maintaining the status quo, these options raise questions regarding how such a regime would be funded or enforced. The NZFTC believe that the Commerce Commission is best placed to enforce the regime, as it has extensive experience with monitoring information disclosure regimes and incorporating franchise-specific legislation into its current work stream would reduce initial and ongoing costs of a regulatory regime for franchising.

A Regulatory Model administered by the Commerce Commission

124. NZTFC favours a mandatory statutory code of franchising, designed to address the systemic problems inherent in the franchising relationship.

125. Costs will be increased for those currently operating outside FANZ voluntary code, but benefits would be tangible in terms of the protection it affords to current franchisees, the certainty it creates for both franchisors and franchisees, the confidence it inspires in the industry, the likely flow on effects for both the franchise as a business medium and the economic effects of that confidence.

Q9 Can you give any estimates of the compliance costs associated with the options?

126. FANZ have stated that the costs to franchisors that currently accede to the voluntary code which they operate, would be likely to be minimal. The cost would obviously be greater or of more significance to those that currently operate outside the code.

127. In the Australian context, disclosure requirements have grown significantly from when the code was first introduced and there have been concerns expressed by franchisors that compliance costs have become onerous. However, arguably, once the initial information systems are set up it would be relatively simple to keep them up to date for release to other prospective franchisees. The majority of Franchisors in the Australian context admitted that the Australia Franchising Code did not have a significant impact on compliance costs as a percentage of annual turnover. From a policy perspective, the importance of full disclosure of all necessary and relevant information trumps any small compliance costs to individual franchisors.

128. In our submission, utilising the existing Commerce Commission not only makes practical, but also financial sense.

Q10 With any of the regulatory options discussed are there potential conflicts with any existing law, such as securities law or company law?

129. NZFTC have not identified any laws that would conflict with the enactment of a regime akin to Australia's Code.