



Law Council
OF AUSTRALIA

Business Law Section

Franchising Code Review Secretariat
Department of Industry, Innovation, Science, Research and Tertiary Education
Small Business Division
GPO Box 9839
Canberra ACT 2601
Via email: franchisingcodereview@innovation.gov.au

22 February 2013

Attention: Mr Alan Wein

Dear Mr Wein,

2013 Review of the Franchising Code of Conduct

I have pleasure in enclosing a submission which has been prepared by the Competition and Consumer Committee of the Business Law Section of the Law Council of Australia.

Under separate cover, I will also be providing you with a copy of a supplementary submission prepared by the Section's SME Business Law Committee.

Yours sincerely,

Frank O'Loughlin
Section Chairman

Enc.

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Law Council
OF AUSTRALIA

Business Law Section

Review of the Franchising Code of Conduct

Submission by the Competition and Consumer
Committee of the Business Law Section of the Law
Council of Australia

22 February 2013

1 Introduction

- 1.1 The Competition and Consumer Committee of the Business Law Section of the Law Council of Australia (Committee) appreciates the opportunity to make the following submissions concerning the issues covered by the terms of reference for the Review of the Franchising Code of Conduct (Code) for consideration by Mr Alan Wein, who has been appointed to conduct the review and to report to the Minister for Small Business.

2 Executive summary

- 2.1 The Committee's submission focuses on three key themes relevant to the Review:

- (a) good faith in franchising;
- (b) enforcement of the Code, in particular the proposal to introduce civil penalties for breaches of the Code; and
- (c) the need for consistent and uniform national regulation.

- 2.2 The following submissions outline and consider:

- (a) the extent of an obligation to act in good faith in contractual arrangements generally;
- (b) the implications of importing an express obligation to act in good faith into franchise agreements;
- (c) the extent to which the existing common law and provisions of the *Competition and Consumer Act 2010* (Cth) (**CCA**) and *Australian Consumer Law* (**ACL**) already provide appropriate remedies to address any instances of unfairness between franchisors and franchisees;
- (d) the efficacy of introducing civil penalties as a means of enforcing the code, particularly given the nature of the Code and the existing ability to impose civil penalties for unconscionable conduct; and
- (e) the need for consistent and uniform national regulation of franchising and to avoid overlapping State and Federal regulation and enforcement.

- 2.3 For the reasons outlined, the Committee considers that the existing legal framework provides adequate protection for franchisees and franchisors in relation to misleading, deceptive or unconscionable conduct while balancing the rights of each party to a franchise arrangement to act in their own interests – as in any commercial arrangement.

- 2.4 If any amendments are to be made to the Code for the purpose of introducing an obligation to act in good faith, such amendments should not attempt to define good faith or contain any prescriptive requirement to act in good faith as defined. Any implication of a duty to act in good faith should be left to the courts to determine each case on its own particular facts and circumstances.
- 2.5 There are two objections to introducing a civil penalties regime:
- (a) first the number of complaints made about breaches of the Code do not warrant the imposition of a civil penalty regime for breach of the Code; and
 - (b) second, and more fundamentally, in the Committee's view, it is not appropriate to introduce civil penalties for breaches of the Code. Civil penalties are generally concerned with serious conduct and cases where the impugned conduct causes some public harm, not merely damage to a particular individual or individuals. Further, civil penalties are already available for other breaches of the CCA and ACL most likely to arise as between franchisee and franchisor, including unconscionable conduct.
- 2.6 It is fundamental that the Review highlights the importance of ensuring a consistent and uniform national approach to the regulation and enforcement of franchising. This is critical for business certainty and to limit administrative and financial costs to business (for both franchisors and franchisees). Increased costs of business will inevitably be passed on to consumers.

3 Good faith in franchising

- 3.1 Generally speaking, an explicit doctrine of good faith in contract law is not part of the common law tradition. This is not true in many other legal traditions. General duties of good faith are part of the contract law in many other jurisdictions, including Germany, China and in the United States. Principles which support long-term cooperative contracts - including rules about good faith, hardship, and undisclosed agency - are also found in the UNIDROIT Principles of International Commercial Contracts.
- 3.2 In Australia, consistent with common law tradition, there is no general doctrine of good faith in contract law. Rather, an obligation to act in good faith can arise in contracts in three ways.¹

¹ Terms can also be implied by custom or usage, or through sufficiently long course of dealings between the parties – these additional foundations for implication are ignored.

- 3.3 The first way is that an obligation to act in good faith can arise in contracts through express terms agreed between the parties to the contract.
- 3.4 The second way the obligation can arise in contracts is as a necessary implication arising out of judicial construction of the contract during litigation, for the purpose of giving business efficacy to the contract.
- 3.5 The third way that an obligation to act in good faith can arise in contracts is where an implied term of good faith is automatically recognised and found by the courts for particular kinds of contracts unless the contracting parties have expressly stipulated otherwise. This is the closest thing to a legal doctrine of good faith in Australian contract law. Labour contracts are one such category of contract. It is an open question whether franchise contracts are another such category of contract (see below).
- 3.6 The last reform to the Code (in 2010) rejected the reform of including an explicit requirement for parties to a franchise agreement to act in good faith in the Code. It instead inserted section 23A, which states that nothing in the Code limits any obligation imposed by the common law on the parties to a franchise agreement to act in good faith. The importance of this is that in some States there has been judicial development (see below) requiring the legal implication of good faith into franchise agreements as a specific contractual category. The 2010 reform of the Code ensured that the Code would not interfere with this development.
- 3.7 The current review of the Code has once again opened up consideration of whether the Code should contain an overarching obligation to act in good faith and, if so, how it should be included (see questions 15 to 22 on page 23 of the Discussion Paper).

Extent of any existing duty of good faith

- 3.8 In Australian common law, companies are assumed to know and act in their own interests. Obligations of good faith in contractual relations arise only if the parties to the contract have explicitly included them, or else when they arise as a necessary implication to the construction of the contract, to give it business efficacy. Generally, express or (factually) implied terms of good faith are only found in long-term contracts (called in legal academia 'relational' contracts²), or contracts which give effect to a strong cooperative commercial purpose, such as joint ventures or partnerships.³ The content of the obligation of good faith

² Eisenberg, *Why is there no law of relational contract*, (2000) Northwestern University Law Review, Vol 94(3).

³ *Hospital Products Ltd v United States Surgical Corporation*, [1984] 156 CLR 41 (though of course this case dealt with fiduciary duties within such types of contract rather than good faith).

will depend on the construction of each contract, but could entail an obligation on the parties to:⁴

- (a) cooperate in achieving the contractual objects;
- (b) comply with honest standards of conduct; and/or
- (c) comply with standards of conduct which are reasonable, having regard to the interests of the parties.

Legal implication of good faith in franchise contracts

- 3.9 For some categories of contract, good faith is implied as a matter of law. In some Australian states, there is authority to the effect that franchise agreements are one of those categories. This is because franchise agreements are 'relational' in nature, involving long-term cooperative relationships between the franchisor and franchisee in pursuit of a joint purpose and joint profit, and so are an obvious candidate for such legal implication.⁵
- 3.10 The High Court has never explicitly considered the issue of good faith in contracting, either in the context of franchising or generally.⁶ The foundation at the state level for a legally implied duty of good faith in commercial contracts *in general* is *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234. That case remains controversial. Some cases which have found a legally implied duty in franchise agreements (as a category of contract) include: *Far Horizons v McDonalds Australia* [2000] VSC 310 and *Gary Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* (1999) ATPR and *Burger King Corp v Hungry Jack's Pty Ltd* [2001] NSWCA 187.
- 3.11 To give an example of the content of such an implied duty, in *JF Keir Pty Ltd v Priority Management Systems Pty Ltd* [2007] NSWSC 789 it was held that:

"a franchisor is required to act reasonably and honestly (to an objective standard), not to act for an ulterior motive, to recognise and have regard to the legitimate interest of both parties in the enjoyment of the fruits of the contract, and to avoid rendering the franchisee's interest under the agreement nugatory or worthless or seriously undermining it."

- 3.12 It should be noted that, to the extent that there is an implied obligation of good faith in franchise contracting, it is near the attenuated end of the scale of possible content for such an obligation, since the cases are clear that it requires merely that parties to the contract

⁴ See Mason, *Contract, Good Faith and Equitable Standards in Dealing* (2000) 116 Law Quarterly Review 66.

⁵ Blair and Lafontaine (2005) *The Economics of Franchising*, Cambridge University Press.

⁶ The High Court explicitly declined to do so in *Royal Botanic Gardens and Domain Trust v South Sydney City Council* (2002) 240 CLR 45.

act reasonably for the furtherance of the joint purpose of the contract (namely, the franchise relationship). It does not involve obliging any party to a franchise agreement to act against its own best interests.⁷

Should an obligation to act in good faith be included in the Code?

3.13 The question arises whether the duty – however attenuated – adumbrated in the cases in some state jurisdictions should be explicitly included in the Code. As mentioned, the Code currently does not interfere (in clause 23A) with any common law duty of good faith found by the courts, and so, to the extent that there is a common law duty, it would be unnecessary to include it in the Code.

3.14 Nonetheless, the benefits of inclusion would be:

- (a) to create certainty about the existence and content of the obligation (to the extent that there is still uncertainty about the existence or content of such a duty); and
- (b) to universalise the obligation across all Australian states. This would have the advantage of everyone knowing where they stand.

3.15 However, this should only be done if it is thought that the emergent but still uncertain duty currently found in some state jurisdictions is a good idea. If it is not considered a good idea, then it should not be hard-wired into the Code.

3.16 If it is to be hard-wired in the Code, then it is the Committee's view that it should be expressly confined to specific categories of conduct under the franchise agreement itself, rather than extending to the broader dealings between franchisor and franchisee (see below).

New definition or importation

3.17 If the Code is amended for the purpose of introducing an obligation to act in good faith, that amendment should not attempt an independent or distinct statutory definition of good faith partnered with a prescriptive requirement to act in good faith as defined. Rather, the amendment should, in as simple terms as possible, impose a duty or obligation to act in good faith without definition and allow the courts to determine, in accordance with the existing and evolving law (referred to in other legislation as the unwritten law), whether that duty has been breached in the circumstances of each case.

⁷ See for example *Far Horizons Pty Ltd v McDonalds Australia Ltd* [2000] VSC 310; *Garry Rogers Motors (Aus) Pty Ltd v Subaru (Aust) Pty Ltd* (1999) ATPR 41-703 and *Meridian Retail Pty Ltd v Australian Unity Retail Network Pty Ltd* [2006] VSC 222.

3.18 Section 20(1) of the ACL illustrates one legislative approach to importing a pre-existing unwritten (common) law concept (unconscionable conduct). It provides:

"A person must not, in trade or commerce, engage in conduct that is unconscionable, within the meaning of the unwritten law from time to time."

3.19 If a similarly styled duty of good faith is to be imported into the Code, the Committee believes it must be more confined than the legislative approach taken in relation to unconscionable conduct. Unlike unconscionable conduct, which proscribes conduct only if the circumstances require it, if a duty of good faith is imposed it immediately imports a positive duty.

3.20 In the Committee's view, if the Code is to import a duty of good faith within the meaning of the unwritten law or otherwise, it should be specific as to the aspects of the franchise relationship to which that duty should apply. For example, it might limit the duty to specific instances of conduct, such as:

- (a) the performance by either party of their obligations under the terms of the franchise agreement; and
- (b) the exercise of any right or power by a party under the terms of the franchise agreement.

3.21 The Committee considers that any attempt to define and apply a new definition of good faith in the Code is likely to create inconsistency between the evolving unwritten law and the Code. A new definition increases the risk of creating a divergent line of jurisprudence, which would add complexity to the law and increase compliance costs for franchisees and franchisors.

3.22 The process of codification creates an inherent problem of parallelism and divergence. As Lord Scarman, arguing in favour of codification, pointed out:

"However carefully drafted, into whatever detail it goes, a code is likely in places to fall into the error of ambiguity and is bound to contain some omissions. If it be ambiguous, yet the judge's decision must be certain; if it fail to cover the case under consideration, yet the judge must make a decision. ... Thus, the very limitations of a code invite the cooperation of the judge, and, whether it is

desirable or not, every time a judge resolves an ambiguity or fills what is in effect, though possibly not in theory, a gap he will be creating law."⁸

- 3.23 Choosing the words used to define good faith may lead to differences between the outcomes of statutory interpretation on the one hand, and the common law application of precedent on the other.
- 3.24 The lapsed *Franchising Bill 2010* (WA) is a good example of the difficulty and risk in attempting to define good faith in a statute. That bill, which was the subject of public consultation but was not enacted, defined **act in good faith** as meaning to act "*fairly, honestly, reasonably and cooperatively*". These elements derive from the unwritten law.⁹ On its face, the definition appeared reasonable. However, the problem with the definition lay with the concepts it did not import from the unwritten law. The bill applied a plainly stated requirement to act in good faith (as defined). The problem with this approach was that the bill created a prescriptive obligation to act in good faith, without providing a clear opportunity to assess particular circumstances of each case. For example, it was unclear whether an obligation to act "co-operatively" should be applied absolutely or whether "co-operation" was to be limited in circumstances where a franchisor's interests conflicted with a franchisee's.
- 3.25 This problem is pronounced in the case of good faith, because there is limited consensus on the composition of the duty. In a speech delivered in 2006, McDougall J explored this problem and observed:

*"Thus, I do not think that it is fruitful to enquire, in some a priori way, as to the content of the concept of "good faith" in a contractual context. It is necessary to look at the particular contract, to see what might be comprehended as a particular expression of the general concept of good faith, and then to enquire whether that particular term, or a term having that particular content, should be implied, or whether it is excluded by express terms or necessary implication from them."*¹⁰

- 3.26 While franchise agreements have enough in common that a case may be made for some form of implied duty in every franchise agreement, pre-determining the circumstances in which such a duty was breached would be impossible in the abstract.

⁸ Scarman, Leslie George (1967) "Codification and Judge-Made Law: A Problem of Coexistence," *Indiana Law Journal*: Vol. 42: Iss. 3, Article 3.

⁹ Sir Anthony Mason "Contract, Good Faith and Equitable Standards in Fair Dealing" (2000) 116 LQR 66; *Alcatel Australia Pty Ltd v Scarcella* (1998) 44 NSWLR 349; *Tomlin v Ford Credit Australia* [2005] NSWSC 540.

¹⁰ Justice Robert McDougall, "The Implied Duty of Good Faith in Australian Contract Law" 21 February 2006.

- 3.27 As is clear from cases like *Garry Rogers Motors (Aus) Pty Ltd v Subaru (Aust) Pty Ltd*,¹¹ *Far Horizons Pty Ltd v McDonalds Australia Ltd*¹² and *Meridian Retail Pty Ltd v Australian Unity Retail Network Pty Ltd*,¹³ courts do not apply a definition of good faith in isolation from the circumstances in which breach is alleged. As a consequence, in deciding whether an implied duty of good faith has been breached, courts have necessarily taken into account the parties' legitimate business interests in the context of the particular terms of the franchising agreement. What was proposed under the lapsed Franchising Bill 2010 (WA) may have prevented, or at least inhibited such a balanced approach.
- 3.28 It might be argued that this kind of problem could be addressed with more careful drafting. However, the point of the above example is not to dwell on one specific illustration of an unintended consequence but more generally, to highlight the inherent risk of redefining good faith in the Code.
- 3.29 Finally, importation is also likely to preserve the relevance of the existing and growing volume of jurisprudence on good faith in franchising. As is discussed above, the existing cases implying a duty of good faith in franchising demonstrate a flexible application of good faith principles, taking the parties' legitimate interests into account.
- 3.30 Importing the unwritten law, rather than redefining good faith in the Code, would preserve the existing, valuable role of these decided cases for franchisees, franchisors and their advisors.

The unconscionable conduct provisions of the CCA already provide appropriate remedies to address instances of unfairness in dealings between franchisors and franchisees

- 3.31 As has been discussed above in section 3.2, the Committee's view is that the unwritten law most likely already imposes an obligation to act in good faith into agreements between franchisor and franchisee. As outlined above, there are now numerous cases where such a duty has been found to exist.¹⁴
- 3.32 To the extent that the duty of good faith so implied is not sufficient, the Committee's view is that the existing provisions of the ACL provide adequate protection to the parties to franchise agreements.

¹¹ (1999) ATPR 41-703.

¹² [2000] VSC 310.

¹³ [2006] VSC 222.

¹⁴ See, for example: *Garry Rogers Motors (Aus) Pty Ltd v Subaru (Aust) Pty Ltd* (1999) ATPR 41-703; *Burger King Corporation v Hungry Jack's Pty Ltd* [2001] NSWCA 187 at [159]; and *Far Horizons Pty Ltd v McDonalds Australia Ltd* [2000] VSC 310 at [120].

3.33 The Parliamentary Joint Committee on Corporations and Financial Services noted in its December 2008 report¹⁵ that, in addition to the Code, the conduct of parties to a franchise agreement is regulated by the following provisions of the ACL:

- (a) Sections 21 and 22 prohibiting unconscionable conduct;
- (b) Section 18 prohibiting misleading or deceptive conduct;
- (c) Section 29 false or misleading misrepresentations about goods or services; and
- (d) Section 37 prohibiting false or misleading representations about the profitability or risk or other material aspect of any business activity.

3.34 The Committee agrees with this summary, and notes that section 18 of the ACL (in particular), is perhaps the most often raised provision of the ACL in franchising disputes.

3.35 In addition, provisions regulating restrictive trade practices under the CCA more broadly, in particular the prohibition against exclusive dealing contained in section 47 of the CCA, are highly relevant to many franchise systems. Section 47 provides a notification and review mechanism for exclusive supply arrangements, which are regularly employed in franchise systems (and are often the source of disputes between franchisor and franchisee).

3.36 In this section, however, we focus only on the unconscionable conduct provisions of the ACL, given their direct relevance to (and, to some extent, overlap with) the concept of a duty of good faith.

Legislative history of the unconscionable conduct provisions

3.37 Sections 20 and 21 of the ACL deal with conduct that is 'unconscionable' in two different contexts. Section 20 prohibits conduct that is unconscionable with the meaning of the common law, whereas section 21 is broader and is intended to address (among other things) unfair dealing in relational contracts such as franchise agreements.¹⁶

3.38 The legislative history of the unconscionable conduct provisions can be somewhat confusing, particularly when trying to follow their development in the Courts. Relevant to this submission, however, we note that:

¹⁵ Parliamentary Joint Committee on Corporations and Financial services "*Opportunity not opportunism: improvising conduct in Australian franchising*", December 2008, paragraph 3.36, page 19.

¹⁶ Paul Finn, University of South Australia Trade Practices Workshop – 2006 paper titled 'Unconscionable Conduct?' page 15 and Michael O'Bryan, University of South Australia Trade Practices Workshop – 2006 paper titled 'Unconscionable Conduct'.

- (a) unconscionable conduct regulation was first extended to business transactions in 1998, in what was then section 51AC of the Trade Practices Act 1974 (TPA) (with section 51AB applying to dealings with consumers);
- (b) section 51AC of the TPA subsequently became section 22 of the ACL, when the ACL commenced on 1 January 2011 (with section 51AB becoming section 21 of the ACL); and
- (c) sections 21 and 22 of the ACL were subsequently consolidated¹⁷ as a new section 21 of the ACL, which applies to unconscionable dealings with both consumers and in business transactions; and
- (d) the non-exhaustive list of matters that a court may (but need not) have regard to in determining a contravention of section 51AC of the TPA, subsequently became section 22(3) of the ACL when it was enacted, and is now found in section 22 of the ACL as amended on 1 January 2012.

3.39 For the purposes of this submission, it is useful to look at the history of what was section 51AC of the TPA, because it is this section (dealing with unconscionable conduct in business transactions), which is of primary relevance to the present inquiry. The section was specifically intended to address unfair dealing in relational contracts (such as franchise agreements).

3.40 Accordingly, for convenience (and to avoid confusion given the legislative history outlined above), we have referred throughout this submission to "**Section 51AC**". These references should be read as including the relevant ACL provisions which succeeded section 51AC of the TPA.

Meaning of "unconscionable conduct"

3.41 In applying Section 51AC, the Courts have made clear that 'unconscionable' is not limited to the meaning of the word at common law or at equity, but takes its ordinary dictionary meaning.¹⁸ The ordinary or dictionary meaning of the word 'unconscionable' was explained in *Hurley v McDonald's Australia Ltd.*¹⁹

"For conduct to be regarded as unconscionable, serious misconduct or something clearly unfair or unreasonable, must be demonstrated ... Whatever unconscionable means in s 51AB and s 51AC, the term carries the meaning given by the Shorter Oxford English Dictionary, namely, actions showing no

¹⁷ Pursuant to the *Competition and Consumer Legislation Amendment Act 2011*.

¹⁸ *ACCC v Allphones Retail Pty Ltd (No 2)* (2009) 253 ALR 324 at [113] (Foster J).

¹⁹ (2000) ATPR 41-741 at [22].

regard for conscience, or that are irreconcilable with what is right or reasonable ... The various synonyms used in relation to the term "unconscionable" import a pejorative moral judgment ..."

- 3.42 The judgment of Foster J in *ACCC v Allphones Retail Pty Ltd (No 2)* (2009) 253 ALR 324 at [113] provides a succinct summary of a number of propositions of general application thus far established in the context of section 51AC, namely:
- (a) the scope of the section is wider than that of section 51AA (now section 20 of the ACL). The meaning of unconscionable for the purposes of s 51AC is not limited to the meaning of the word according to established principles of common law and equity;²⁰
 - (b) the ordinary or dictionary meaning of 'unconscionable', which involves notions of serious misconduct or something which is clearly unfair or unreasonable, is picked up by the use of the word in section 51AC. When used in that section, the expression requires that the actions of the alleged contravener show no regard for conscience, and be irreconcilable with what is right or reasonable. Inevitably the expression imports a pejorative moral judgment;²¹ and
 - (c) normally, some moral fault or moral responsibility would be involved. This would not ordinarily be present if the critical actions are merely negligent. There would ordinarily need to be a deliberate (in the sense of intentional) act or at least a reckless act.²²

Should "unconscionable conduct" be more clearly defined?

- 3.43 The Court in *Allphones* recognised that the authorities referred to do not prescribe a precise definition which would be able to be applied to every set of circumstances presented to the Court for consideration. The application of the meaning accorded to the concept was said to always be a matter of judgment and will depend upon a careful consideration of the circumstances of each case.²³
- 3.44 The Committee agrees that it is neither practical nor desirable to proscribe specific acts as being unconscionable in every case. The same applies to any duty of good faith that might

²⁰ *ACCC v CG Berbatis Holdings Pty Ltd (No 2)* (2000) 96 FCR 491 at [24]-[25] (French J); *ACCC v Simply No-Knead Franchising Pty Ltd* (2000) 104 FCR 253 at [31] (Sundberg J); *ACCC v 4WD Systems Pty Ltd* (2003) 200 ALR 491 at [183] (Selway J) and *Pacific National (ACT) Ltd v Queensland Rail* (2006) 28 ATPR 46-268 (p 53,515) at [918] (p 53,527) (Jacobson J).

²¹ *Hurley v McDonalds Australia Ltd* (2000) 22 ATPR 41-474 (p 40, 578) at [22] (p 40,585) (Heerey, Drummond and Emmett JJ). This helpful articulation of the meaning of the word when used in s 51AC was followed by Selway J in *ACCC v 4WD Systems Pty Ltd* (2003) 200 ALR 491 at [183]-[185] (pp 487-488) and by Sundberg J in *ACCC v Simply No-Knead Franchising Pty Ltd* (2000) 104 FCR 253 at [30] (p 264).

²² *ACCC v 4WD Systems Pty Ltd* (2003) 200 ALR 491 at [185] (Selway J).

²³ *ACCC v Allphones Retail Pty Ltd (No 2)* (2009) 253 ALR 324, at [114].

be legislated. It is apt to note, in this context, the following passage from a Regulatory Impact Statement prepared in response to the *Parliamentary Joint Committee on Corporations and Financial Services'* 2008 report on franchising:

"The Franchising Code was introduced, in part, in recognition of the imbalance in bargaining power between franchisors and franchisees. Nevertheless, as the Joint Committee (on Corporations and Financial Services) noted, franchising is a relationship between two separate commercial parties. The Franchising Code does not prohibit both parties from pursuing their own individual interests nor does it prohibit normal hard commercial dealings which may be perceived as 'unfair' by one party. This approach recognises that while franchisees may benefit from minimum disclosure and procedures that must be followed by franchisors in their dealings with them, the Code provisions should not unreasonably constrain franchisors from making business decisions in not only their own interests but also for the benefit of the entire franchise system."

- 3.45 Section 51AC was designed to give the Courts the discretion to address conduct which is clearly unfair or unreasonable, while recognising that conduct which may be unconscionable in one context, may not in others.
- 3.46 Consistent with this approach, section 22 of the ACL sets out a number of non-exhaustive factors to which the court may have regard in determining whether there has been a contravention of section 21. It is worth setting these out in full, with emphasis added (in **bold**) to highlight the key elements that these provisions are tailored to address:²⁴
- (a) the relative **strengths of the bargaining positions** of the supplier and the customer; and
 - (b) whether, as a result of conduct engaged in by the supplier, the customer was required to comply with **conditions that were not reasonably necessary** for the protection of the **legitimate interests** of the supplier; and
 - (c) whether the customer was **able to understand** any documents relating to the supply or possible supply of the goods or services; and
 - (d) whether any **undue influence or pressure** was exerted on, or any **unfair tactics** were used against, the customer or a person acting on behalf of the customer by the supplier or a person acting on behalf of the supplier in relation to the supply or possible supply of the goods or services; and
 - (e) the amount for which, and the circumstances under which, the customer **could have acquired identical or equivalent goods or services** from a person other than the supplier; and

²⁴ Note that we have set out the text from section 22(1), which deals with unconscionable conduct by a supplier of goods or services (most likely relevant to the conduct of a franchisor under a franchise agreement). Section 22(2), which we have not set out, is substantively identical, but deals with unconscionable conduct by an acquirer of goods or services (most likely relevant to the conduct of a franchisee under a franchise agreement).

- (f) *the extent to which the supplier's conduct towards the customer was consistent with the **supplier's conduct in similar transactions** between the supplier and other like customers; and*
- (g) *the requirements of any **applicable industry code**; and*
- (h) *the requirements of any other industry code, if the customer acted on the reasonable belief that the supplier would comply with that code; and*
- (i) *the extent to which the supplier **unreasonably failed to disclose** to the customer:*
 - (i) *any intended conduct of the supplier that **might affect the interests** of the customer; and*
 - (ii) *any risks to the customer arising from the supplier's intended conduct (being **risks that the supplier should have foreseen** would not be apparent to the customer); and*
- (j) *if there is a contract between the supplier and the customer for the supply of the goods or services:*
 - (i) *the extent to which the **supplier was willing to negotiate** the terms and conditions of the contract with the customer; and*
 - (ii) *the terms and conditions of the contract; and*
 - (iii) *the conduct of the supplier and the customer in complying with the terms and conditions of the contract; and*
 - (iv) ***any conduct that the supplier or the customer engaged in**, in connection with their commercial relationship, after they entered into the contract; and*
- (k) *without limiting paragraph (j), whether the supplier has a contractual **right to vary unilaterally a term or condition of a contract** between the supplier and the customer for the supply of the goods or services; and*
- (l) *the extent to which the supplier and the customer **acted in good faith**.*

3.47 What is clear from the above list, is that many of the elements that proponents of a statutory duty of good faith to franchise relationships might seek to ascribe to that duty, are already relevant factors to be considered when applying section 22 of the ACL.

Are the unconscionable conduct provisions effective?

3.48 The Committee acknowledges that some have suggested that the unconscionable conduct provisions in the ACL have failed to address unconscionable conduct in franchise relationships properly. For these change advocates, imposition of a duty of good faith is seen as the answer to the perceived failings of Section 51AC. However, the Committee submits that it is both inaccurate to view such a duty as extending the law beyond what already exists, and premature to conclude that the existing unconscionable conduct provisions are ineffective.

3.49 While there has been relatively little enforcement action taken by the ACCC under Section 51AC, the majority of cases that it has brought have been resolved successfully. The February 2010 report, *Strengthening statutory unconscionable conduct and the Franchising Code of Conduct*, reported²⁵ that the ACCC had, between 1998 and 2010, litigated 19 cases in relation to Section 51AC. Of those:

- (a) nine were settled, with consent declarations that the respondents had infringed;
- (b) four were settled without consent declarations;²⁶
- (c) the ACCC was successful in four matters;²⁷ and
- (d) the ACCC was unsuccessful in two matters.

3.50 This suggests that the ACCC reached a successful outcome in 17 of the 19 cases it commenced. This hardly suggests that Section 51AC has proved ineffective (in contrast, it might be said, with what used to be section 51AB of the TPA, relating to unconscionable conduct in dealings with consumers, where the ACCC has had much less success in its enforcement actions to date).

3.51 The Committee's view is that the unconscionable conduct provisions of the ACL provide substantial scope for action to be taken by the ACCC, and for the Courts to provide redress to victims of conduct which is clearly unfair or unreasonable.²⁸ As with any prohibition importing notions of 'fairness', it will take time and further judicial consideration for the full force of the provisions to be understood, but the Committee submits it is premature to conclude that the existing provisions do not provide adequate redress.

²⁵ The Treasury and the Department of Innovation, Industry, Science and Research (Cth), *Strengthening statutory unconscionable conduct and the Franchising Code of Conduct* (February 2010), Appendix C, page C-5

²⁶ This includes the case of *ACCC v Allphones Retail Pty Ltd & Ors*, which had been listed for trial at the time of the government's report, but subsequently settled on undisclosed terms.

²⁷ This includes the case of *ACCC v Seal-A-Fridge Pty Ltd*, which had commenced at the time of the government's report, and in which Seal-A-Fridge was subsequently found to have breached section 51AC.

²⁸ It should also be noted that the enforcement powers and remedies for breach of the unconscionable conduct provisions were also significantly bolstered with the introduction of the ACL in 2010. In addition to injunctions and damages, the enforcement powers and remedies now also include (amongst others) civil pecuniary penalties of up to \$1.1 million for a corporation and up to \$220,000 for individuals, remedial compensation and the ACCC may seek compensation for non-parties (as it did in the *Allphones* case).

4 Enforcement of the Franchising Code

Civil penalties

- 4.1 The Explanatory Statement to the Code suggests that its purpose is to strike a balance between the need to raise standards of conduct in the franchising sector without endangering the vitality and growth of franchising.²⁹
- 4.2 Nevertheless there have been numerous suggestions that the balance is not yet right, and that it would be improved by the introduction of penalties for breaches of the Code. The arguments made for the introduction of civil penalties for breaches of the Code are that:
- (a) penalties would operate as an effective deterrent to breaching the Code, and this would assist the ACCC in its enforcement role;³⁰
 - (b) due to the cost of justice, franchisees do not possess the resources to pursue franchisors, ie the sector is characterised by an imbalance of power and therefore the state should intervene;³¹
 - (c) it is inconsistent for penalties not to exist, given that penalties do exist for other breaches of the CCA and ACL;³²
 - (d) the introduction of penalties will increase the confidence of investors, franchisees and franchisors in the franchising sector.³³
- 4.3 The Committee's view is that the points set out above do not outweigh the public cost and regulatory risk associated with the introduction of civil penalties. Each of these points is explored in more detail below.

Deterrence and the ACCC's enforcement role

- 4.4 The 2008 report '*Opportunity not opportunism: improving conduct in Australian franchising*'³⁴ states that there is deep and widespread frustration amongst franchisees

²⁹ Explanatory Statement, Trade Practices (Industry Codes – Franchising) Regulations 1998, p2.

³⁰ Report of Parliamentary Joint Committee on Corporations and Financial Services into the *Inquiry into the Franchising Code of Conduct*, paragraph 9.35.

³¹ '*The case for imposing monetary penalties for breaches of mandatory industry codes of conduct*', Zumbo (2011) 19 ACCL 112, at 112. See also Evidence Economics and Industry Standing Committee, *Inquiry into Franchising Bill 2010 (WA)*, Western Australian Legislative Assembly, Perth, 11 April 2011, p3 (Ms Jacqueline Finalyson).

³² Zumbo, op cit.

³³ '*Penalties for breaches of the Franchising Code of Conduct: A Western Australian perspective*', Zumbo (2012) 40 ABLR 387.

over the perceived inaction by, and ineffectiveness of, the ACCC in pursuing complaints against franchisors who are alleged to be in breach of the Code.³⁵

- 4.5 As recognised by commentators, various avenues of public enforcement for breaches of the Code are already available to the ACCC, such as:
- (a) public warning notices (section 51ADA); injunctions (section 80), non-punitive orders (section 86C), undertakings (section 87B);
 - (b) applying to a court to remedy losses on behalf of franchisees who were not part of the legal proceedings, but suffered harm from the same act or omission (section 51ADB);
 - (c) seeking remedial orders from a court (eg variation of a contract) (section 87); and
 - (d) conducting audits to monitor compliance with the Code (s 51ADD).
- 4.6 In addition, penalties are of course available in cases where franchisors breach the competition and consumer law protections found in the CCA and the ACL, including for unconscionable conduct under section 21 of the ACL.
- 4.7 Despite complaints by franchisees, it is unclear that significant breaches of the Code and ACL are occurring. In the ACCC's 'Small Business, Franchising and Industry Codes Half Yearly Report' for July-December 2012,³⁶ the ACCC reported that 2,338 complaints and enquiries from small businesses, franchisees and franchisors were recorded by the ACCC info centre over the six month period. However, the ACCC identified that only 88 of those complaints were Code-related issues, and the ACCC did not elect to seek any remedies in relation to those complaints, possibly indicating that in the ACCC's view the complaints did not warrant a regulatory response. Over sixty five percent of franchising complaints made to the ACCC related to non Code related issues (ie consumer protection or competition related issues)³⁷ for which penalties are available.³⁸

³⁴ Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Inquiry into the Franchising Code of Conduct, Opportunity not Opportunism: Improving Conduct in Australian Franchising* (2008).

³⁵ Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Inquiry into the Franchising Code of Conduct, Opportunity not Opportunism: Improving Conduct in Australian Franchising* (2008), 9.32.

³⁶ Australian Competition & Consumer Commission, Parliament of Australia, *Small Business in Focus, Report No.5* (2012).

³⁷ *Ibid.*

³⁸ The ACCC reported that in this period there were 65 complaints that related to misleading conduct/false representations and 47 relating to unconscionable conduct.

The cost of justice

- 4.8 Part of the justification for the introduction of penalties appears to be that penalties will enable the ACCC to take action against franchisors, given that franchisees are usually unable to do so due to lack of resources or the need to maintain a working relationship with the franchisor.
- 4.9 Access to justice issues are important and complex. Past responses to these issues have included state funding of impecunious litigants, creation of the role of ombudsman and the establishment of low-cost courts and tribunals where each party bears its own costs. These avenues avoid or mitigate shifting private litigation costs to the public purse.
- 4.10 It is unclear that the state should fund regulatory action as a response to cost of justice issues and the imbalance of power / resources between participants in the franchising sector. Similar issues and imbalances exist in other commercial relationships (such as distribution agreements) and the policy justification for funding regulatory action in one industry sector over another is problematic.
- 4.11 It is also unclear that an ACCC prosecution will assist the individual franchisee, or other franchisees of the same franchisor. Any civil penalty will be retained by Government, although a franchisee might subsequently seek a related commercial settlement. Prosecution of a franchisor also has the potential to harm the brand of the franchisor, which could have undesirable flow on effects to the franchising business as a whole, and to its other franchisees. Further, prosecution of a franchisor could delay pursuit of civil remedies by franchisees.

The existence of civil penalties for other breaches of the CCA and ACL

- 4.12 Commentators have argued that it is anomalous for penalties not to exist for breaches of the Code, given that penalties are imposed under the CCA and ACL. However, although penalties are proscribed for offences regarded as relating to 'norms of business conduct', regimes relating to particular industries, such as the industry codes covered by section 51AD, the Part IIIA access regime, and the Telecommunications Access Regime in Part XIC are generally not supported by penalties.
- 4.13 Imposing penalties for breach of the Code does not perhaps give sufficient weight to the dicta of the High Court in *Ketchells*.³⁹ In that case the High Court found that the purpose of the Code is to 'regulate the conduct of persons in the franchising industry in order to improve business practices, to provide some protection to franchisees proposing to enter into franchise agreements and to decrease litigation' (at paragraph 25 of the joint

³⁹ *Master Education Services Pty Ltd v Ketchell* (2008) 236 CLR 101.

judgment). The High Court rejected the argument that the effect of a breach of the Code was always to vitiate the relevant franchise agreement, emphasising the flexible remedies available in the Act, and noted that the benefit of this flexibility was that the remedy could be made to fit the circumstances of the case. These remedies are less likely to be explored if franchisees come to rely on the imposition of civil penalties.

The relationship of civil penalties and the confidence of investors, franchisees and franchisors in the franchising sector

- 4.14 The Commonwealth "Guide to Framing Commonwealth Offences, Civil Penalties and Enforcement Powers" states:

*"It is particularly important that civil penalties be used in appropriate and justifiable contexts".*⁴⁰

- 4.15 Civil penalty proceedings 'are concerned with public wrongs and moral culpability, and not merely conduct causing damage'⁴¹ and their purpose is to deter⁴² and 'punish the offender.'⁴³
- 4.16 As civil penalties are 'founded on the notion of preventing or punishing public harm',⁴⁴ for their imposition to be justified the conduct to which they are attached should involve a public harm. The imposition of civil penalties will be appropriate if the cost to the public purse is justified by the scale of public benefits that would accrue from a successful prosecution.
- 4.17 It is unclear that the public benefits achieved through the imposition of civil penalties for breaches of the Code would outweigh public enforcement costs. Complaints about franchisor conduct do not appear to primarily relate to breaches of the Code.⁴⁵ Existing

⁴⁰ Australian Government Attorney-General's Department, *A Guide to Framing Commonwealth Offences, Civil Penalties and Enforcement Powers* (2007), pp.62

⁴¹ Vicky Comino, 'Effective Regulation by the Australian Securities and Investments Commission: The Civil Penalty Problem' (2009) 33 *Melbourne University Law Review* 802."

⁴² *Schneider Electric (Australia) Pty Ltd v ACCC* [2003] FCAFC 2.

⁴³ Australian Law Reform Commission, *Securing Compliance: Civil and Administrative Penalties in Federal Jurisdictions* DP 65 (2002), 2.46.

⁴⁴ Australian Law Reform Commission, *Securing Compliance: Civil and Administrative Penalties in Federal Jurisdictions* DP 65 (2002), 2.46.

⁴⁵ Australian Competition & Consumer Commission, Parliament of Australia, *Small Business in Focus, Report No.5* (2012), although note that the 'Franchising Australia 2012' Griffith University report (see below) suggests that 'compliance with the system' is the cause of 46% of disputes (p61). It is not clear from the Report whether 'compliance with the system' is equivalent to compliance with the Code.

regulatory remedies have not been pursued, possibly because the ACCC does not consider that there is a need to do so, either because the breaches are largely technical in nature or because no clear breach is evident.

- 4.18 Further, the franchisee-franchisor relationship is essentially a private relationship between two businesses. The damage that results from the contravening conduct of a franchisor is often limited to damage to the particular franchisee. Where the outcome of a dispute primarily affects the private rights of the disputants, government resources may be better focused elsewhere.
- 4.19 Commentators suggest that the introduction of penalties would serve the policy benefit of maintaining 'a high degree of confidence' by franchisees and potential franchisees in the franchising sector.⁴⁶ However, it is unclear whether the introduction of penalties would make a significant difference to confidence in the franchising sector. Despite the absence of penalties, the 2012 Griffith University *'Franchising in Australia'* report suggests that growth in the sector has been relatively constant over the last ten years (subject to the effects of the GFC).⁴⁷ The Griffith report also estimates the proportion of franchisees in dispute with their franchisor in 2011 as 1.5%, which proportion is relatively constant over the last decade.⁴⁸
- 4.20 The Griffith report also refers to the loss of confidence that can result from regulatory changes noting that regulatory uncertainty was cited as a significant challenge by 36% of franchising respondents.⁴⁹ Further, the Griffith report cites that 65% of franchisors utilise a Code of Conduct compliance program, and over the last few years, a majority franchisors have moved towards managing compliance programs through enlisting the assistance of a third party law firm.⁵⁰ This may suggest that a positive effect of the 2010 changes to the Code was to increase franchisor awareness of the need to monitor compliance, partly achieving the public benefit that might otherwise be sought through the introduction of penalties.
- 4.21 However, the Griffith report suggests that only 4% of franchisors were audited for compliance by the ACCC.⁵¹ The ACCC January 2013 Small Business Report⁵² states that

⁴⁶ Zumbo (2012) 40 ABLR 387 at 390.

⁴⁷ 'Franchising Australia 2012', Griffith University 2012 report p9-10.

⁴⁸ *Ibid*, p 13.

⁴⁹ *Ibid*, p 42.

⁵⁰ *Ibid* at page 64.

⁵¹ *Ibid* at 58.

it audited 13 franchisors (the Griffith report noted that there are around 1180 franchise systems in Australia),⁵³ and that the majority were found to be complying with the Code.

- 4.22 An alternative to the introduction of civil penalties may be to provide the ACCC with more resources to audit franchise businesses. The benefits of this approach are that it would better educate franchisors about the need for compliance, provide the ACCC with more opportunities to seek remedial action where necessary, and provide evidence one way or the other regarding the assertions of confidence-destroying non-compliance by franchisors with the Code.

Restriction on use of civil penalties for significant breaches of the Code

- 4.23 One possible way of minimising the public burden and maximising the benefits that might arise from the introduction of civil penalties for breach of the Code is to modify the application of the penalty regime such that it applied only to significant breaches of the Code. Technical breaches of the Code would not be prosecuted, leaving it to the ACCC to identify these and respond to them some other way.

- 4.24 The Committee does not support this approach. It is difficult to identify in advance what breaches are 'significant' and which are technical or unworthy of prosecution. In practice this approach is likely to boil down to reliance on the ACCC's prosecutorial discretion. Neither franchisors nor franchisees are likely to find this satisfactory: franchisors because of the uncertainty it creates, and franchisees because the ACCC's approach to managing perceived non-compliance with franchisors has to date not been considered sufficiently aggressive in the eyes of some franchisees and commentators.⁵⁴

- 4.25 Further, it is unclear that relying on the ACCC's discretion to take appropriate action in response to an infringement would be appropriate. This Committee has previously expressed concern around the ACCC's use of its discretion in the issue of infringement notices, which are intended to be issued as a way of rapidly and cost-effectively dealing with relatively minor, potential infringements of the ACL. The ACCC has on a number of occasions issued multiple infringement notices in relation to particular conduct which has resulted in a very high penalty,⁵⁵ which is not, in the Committee's view, an intended outcome of the infringement notice remedy, being the imposition of a penalty through an administrative process rather than through the courts.

⁵² ACCC, *Small Business, Franchising and Industry Codes Half Yearly Report* (July – December 2012).

⁵³ *Ibid* at p9.

⁵⁴ Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Inquiry into the Franchising Code of Conduct, Opportunity not Opportunism: Improving Conduct in Australian Franchising* (2008), 9.32.

⁵⁵ For example, 27 infringement notices totalling \$178,200 were issued simultaneously to Singtel Optus in the 'MaxCap' matter (refer: <http://www.accc.gov.au/content/index.phtml/itemId/977517>).

4.26 If the ACCC were granted the ability to seek similar penalties or issue infringement notices to participants in the franchise industry, it is possible that (in the case of, for example, a technical breach regarding the contents of a disclosure document) a franchisor could receive multiple infringement notices relating to that event, which would potentially amount to a significant financial penalty.

Alternatives to civil penalties

4.27 Other ways of addressing franchisee concerns may be more effective than introducing civil penalties.

4.28 For example:

- (a) as suggested above, the ACCC could be better resourced to conduct a larger number of audits of franchisor compliance, and be tasked with reporting in detail on the compliance of audited franchisors with the Code;
- (b) franchisees could be given access to a Franchising Ombudsman which could also serve the purpose of educating franchisees about what is and is not a breach of the Code, and
- (c) the Code could be amended to require franchising contracts to include provisions that each party bear its own costs of a franchising dispute.

4.29 Alternatively there may be scope to conduct more empirical research into the nature of the complaints against franchisors by franchisees so as to determine whether introducing civil penalties would significantly change the existence of those complaints.

If a civil penalty regime is used, what is the appropriate approach?

4.30 For the reasons discussed above, the Committee does not support the enactment of a civil penalty regime for breaches of the Code.

4.31 However, if a civil penalty regime were to be enacted that raises the question of how such a regime would operate, having regard to the current terms of the Code. The Code is an industry code concerned with achieving minimum standards of conduct in industry rather than imposing a strict form of regulation,⁵⁶ and as result the Code is general and imprecise in its terms. It is therefore not drafted in such a way that it can clearly be determined whether or not a breach has in fact occurred, and for this reason the imposition of a civil penalty on breach becomes problematic. Imprecise language also leaves open the

⁵⁶ Discussion Paper, page 30.

possibility of contravention for both conduct that may not justify the application of a penalty and conduct that does.

- 4.32 Those governed by a civil penalty regime need to be able to determine what the law requires of them and to be sure enough of its meaning to make informed decisions about their actions. In other words, they need to know the exact nature of their duties and liabilities. This is particularly important in regulated industries. Uncertainty in this respect increases costs of business for both franchisors and franchisees and is likely to encourage more litigation as defendants look to clarify their position under a civil penalty regime. Uncertainty also dilutes the intended deterrent effect of a civil penalty regime.

Any civil penalty regime must ensure fairness and be able to be enforced in a structured and non-arbitrary way

- 4.33 The imprecise language of the Code means that it is not, in the view of the Committee, appropriate to apply a blanket penalty regime to the Code. Before a penalty regime could be imposed, the Code would require amendment so as to be clearer in its terms. Alternatively, if a civil penalty regime was to be imposed, consideration ought be given to confining the civil penalty regime to those aspects of the Code that are determined to be so serious as to warrant the imposition of civil penalties, with consideration being given to whether or not it is necessary to amend those particular aspects of the Code to be more precise in their terms.
- 4.34 Some examples of sections of the Code that lack precision and could thereby create difficulties in enforcement are as follows:
- (a) Section 4(1) of the Code. This section defines what is meant by 'franchise agreement'. The meaning of a 'system or marketing plan substantially determined, controlled or suggested' by the franchisor is unclear. For example, will this include control exerted by a licensor of a trade mark over the use of their trade mark (as is required in order to maintain ownership under the Trade Marks Act 1995)? How much must be 'suggested' in order to trigger the operation of the section?
 - (b) Section 6B of the Code. This section outlines circumstances in which a franchisor must issue a new disclosure document, following an 'extension of the scope' of a franchise agreement. The meaning of 'extend the scope' is unclear. For example, if a franchisee moves premises into a larger site, will this be an extension of scope? What about if their marketing area is increased, or they are authorised to use an additional business name? What if the range of goods and services they are authorised to sell is increased?

- (c) Section 3 of the Code. This section defines what constitutes a 'motor vehicle' (agreements granting motor vehicle dealerships are deemed to be franchise agreements under the Code). The definition of 'motor vehicles' is imprecise. For example, while it is clear that road-worthy vehicles such as tractors will be regulated, does the definition include a ride on lawn mower?
- (d) Section 10 of the Code. This section requires that a franchisor must provide a prospective franchisee with a sample franchise agreement along with the disclosure document. On a literal application of this section, the sample provided must be identical to the one the franchisee will be required to execute. Often, simple changes will need to be made to the franchise agreement, such as to update the contact details for the franchisee or the premises address. Is the franchisor required to update the sample franchise agreement and re-issue a new disclosure document each time such a change is made?

- 4.35 Further, if a civil penalty regime was to be adopted, careful consideration should be given to what the appropriate quantum of the penalty ought to be having regard to the particular breach that has occurred. This again is problematic because most of the relevant provisions of the Code concern disclosure. How is it to be determined which aspect of the disclosure regime should attract a penalty and what the appropriate quantum of such penalty is? It might prove problematic to try and prioritise particular breaches of the Code, or to apply the principle recommended in paragraph 3.1.2 of the Commonwealth Attorney General's *Guide to Framing Commonwealth Offences*⁵⁷ that "A penalty should be consistent with penalties for existing offences of a similar kind or of a similar seriousness". It is difficult to determine whether, for example, a failure to provide part of the required content of a disclosure document should have a penalty on par with the penalties prescribed for breaches of the ACL, or what an appropriate comparator might be.
- 4.36 Whilst it might be suggested that an alternative to the implementation of a civil penalty regime, may be to give the ACCC power to issue infringement notices, the Committee and the Business Law Section of the Law Council of Australia are generally opposed to the use of infringement notices. This is because they effectively reverse the onus of proof and thereby risk undermining fundamental principles of justice.
- 4.37 Granting the ACCC the power to issue infringement notices also raises many of the same fundamental issues discussed in section 4.1 above, which militate against the imposition of financial penalties for breach of an industry code.

⁵⁷ Australian Government Attorney-General's Department, *A Guide to Framing Commonwealth Offences, Infringement Notices and Enforcement Powers* (September, 2011)

- 4.38 If an infringement notice regime is to be introduced, the Committee considers that there must be clear direction issued to the regulator in the legislation that the issue of such a notice cannot be accompanied by the regulator extracting an enforceable undertaking in relation to the matter under dispute under the relevant legislation, for to do so undermines immediately the assertion by the Government that the issue of an infringement notice does not carry with it an implication of guilt on the part of the person to whom the notice is issued.
- 4.39 The Committee notes that the same issues arise as to certainty where prosecutorial discretion is involved, such discretion being exercised by reference to internal ACCC policy, which will likely change from time to time. Further, as noted above, it is open to the ACCC to issue multiple infringement notices for matters that may technically involve a number of contraventions but arise out of one course of conduct. This is undesirable from the point of view of certainty and proportionality.

5 Overlapping state and federal regulation and enforcement

Need for consistent and uniform national regulation

- 5.1 One area of particular concern for the Committee is the potential for inconsistencies to arise between the State-based franchising regulation and the Code. As the Discussion Paper itself highlights, four inquiries have examined franchising in Western Australia and South Australia in recent years. These inquiries have either led to or responded to calls for state-specific legislation to regulate franchising in addition to the national Franchising Code.
- 5.2 As the Discussion Paper highlights, the South Australian *Small Business Commissioner Act 2011* commenced on 22 March 2012 and the South Australian Government has stated its intention to consider using these laws to introduce a State-specific franchising industry code to apply in South Australia, which would be in addition to the national Code. There have also been attempts to regulate franchising through the introduction of private members' bills in Western Australia, such as the Franchise Agreements Bill 2011 (WA). Meanwhile, a further private members' bill in New South Wales, the Small Business Commissioner and Small Business Protection Bill 2012 (NSW), would impact on franchising arrangements.
- 5.3 The Committee agrees with the use of industry codes as a means of regulation of business, including small business. However, the Committee believes that State-based

regulation, while well intended, is a retrograde step. Important policy considerations arise with respect to the introduction of State industry codes:

- 5.4 First, the significant administrative and financial costs that businesses are likely to incur with overlapping regulation by the State and Commonwealth are against the interests of small business. The Committee believes that this cost and administrative burden is well recognised and is unwarranted. The Code already provides a sound national basis for regulation.
- 5.5 Second, differences in regulation between States has the potential to increase transaction and compliance costs for small business significantly, particularly franchising organisations and businesses that operate across multiple States and Territories within Australia.
- 5.6 Accordingly, in the Committee's view, regulation of franchising should occur on a consistent and uniform national basis.
- 5.7 Indeed, the need for consistent and uniform national regulation has been a central tenet of Australian competition and consumer regulation. The Hilmer Report into National Competition Policy, for example, identified the need for Australia to be treated and regulated as a single integrated market and has guided the development of regulatory policy in Australia for the last two decades. More recently, harmonisation of Australian consumer legislation has occurred within the context of the Australian Consumer Law.
- 5.8 The Productivity Commission recently commented in its June 2012 assessment of COAG's Regulatory and Competition Reform Agenda that "*excessive, poorly designed and overlapping regulation place a significant cost burden on Australian businesses and consumers*" and "*despite having processes in place to counter forces leading to excessive regulation, much regulation continues to be poorly justified and implemented in Australian jurisdictions, and that the costs to business and the community are large*" (page 36). The Productivity Commission also relevantly commented:

"A particular problem relates to regulatory overlap or inconsistency between jurisdictions. As an indication of the likely magnitude of such unnecessary costs, the Commission recently published estimates of the impacts of selected COAG business regulation reforms. The Commission found that the full implementation of 17 of the 27 Seamless National Economy reforms, aimed at reducing the regulatory burden imposed on businesses that operate across jurisdictions, could in the longer run provide cost reductions to business of around \$4 billion per year and increase GDP by nearly one half of a per cent (around \$6 billion per year). The Commission found that only \$143 million of the benefits had been realised thus far (PC 2012a)."

5.9 In light of these conclusions, the Committee submits that:

- (a) The current review of the Code should highlight the fundamental importance of the Code in ensuring a consistent and uniform national approach to the regulation of franchising throughout Australia.
- (b) If a State does have particular concerns with the current franchising regulatory framework, those concerns should be more properly raised and addressed at a national level, as is occurring in the context of the current review, not at a State level. To assist a national approach, it may also be appropriate for the Council of Australian Governments (COAG) to endorse the use of the Code as the primary instrument for regulating franchising in Australia.

6 Further Contact

6.1 The Committee would be pleased to discuss any of the matters outlined in this submission further should it be desired. To facilitate further discussions, please contact either:

- (a) Josh Simons (Partner, Minter Ellison) on (08) 8233 5428 or at josh.simons@minterellison.com; or
- (b) Sarah Russell (Barrister, Francis Burt Chambers) on (08) 9220 0493 or at srussell@francisburt.com.au, to facilitate further discussions.