

**craveable
brands.**

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4 May 2018

Parliamentary Joint Committee on Corporations and Financial Services
PO Box 6100
Parliament House
Canberra ACT 2600

By email: corporations.joint@aph.gov.au

Dear Sir/Madam,

Inquiry into the Operation and Effectiveness of the Franchising Code of Conduct

Craveable Brands is an Australian-owned franchisor operating in the quick service restaurant sector through the Red Rooster, Chicken Treat and Oporto brands across 570 locations. We welcome the opportunity to provide this submission to the Committee as part of its inquiry into the Franchising Code of Conduct.

As a long-term participant in the market, Craveable Brands is a strong advocate for the importance of the franchise sector to Australia's economy and its significant contribution to investment and employment.

Craveable brands employs 540 people directly across Australia. Through our franchise network our brands employ a further 11,900 people across 570 stores in both metropolitan and regional locations.

Four hundred of our stores are franchises, representing approximately 0.5% of the market in Australia.

In relation to its brands, the company partners with franchisees to grow and develop their businesses with an ongoing focus on innovation, brand positioning and channel expansion. The overwhelming majority of Craveable's franchisee owners are happy with the support they receive in areas such as financial assistance, training, marketing, IT, store design and market access. Reflective of this sentiment, some endorsements from our franchisees are included as an addendum of this letter.

We note that a submission has been lodged with the Committee by the 'Franchisee Association of Craveable'. While it is important to note that Craveable Brands is unaware of the specific members of this Association or who they represent (as we have not been contacted by the Association) we welcome the opportunity to address the issues that have been raised. We consider the assertions made by the Association are inaccurate and omit important context that is essential to a proper understanding of the operation of a broader franchise system. Claims of stores nationwide on the verge of collapse are a ridiculous assertion,

Craveable Brands has a best practice framework to support its franchisees. Importantly:

- All three brands (Red Rooster, Chicken Treat and Oporto) are growing in both sales and profitability, with the average franchisee earning on average \$135,000 per year with annual sales growing 4.3% per years, 59% more than the average \$84,600 full-time worker in Australia
- Recent tender outcomes have delivered material benefits to franchisees with savings in excess of \$11,000 to \$25,000 per store per year
- extensive induction and development programs
- ongoing coaching and training through a business consultant structure

Craveable Brands Pty Ltd ABN 42 151 143 065

red rooster

oporto

chicken treat

- consistent and regular state meetings
- a Franchise Advisory Council (FAC)
- annual conferences to learn, collaborate and build strategies.

Overall, we believe the Franchising Code of Conduct provides a robust and effective framework for the sector and has been subject to regular review and enhancement. Nonetheless, Craveable Brands has identified some specific areas where we believe the Code could be improved including the complexity of disclosure documents, franchisor rights of termination for breaches of the Fair Work Act and addressing the right to immediately terminate for an irremediable breach.

If there are any questions or concerns arising from this submission, please feel free to contact me at any time at

Yours sincerely,

Brett Houldin
Chief Executive Officer

Franchisee Endorsements

Oporto

██████████, an 18-year veteran in Oporto and currently member of our Franchise Advisory Council stated:

"Oporto has a strong business and a strong franchise network. Our sales have been growing at record rates of more than 10% over the last few years. We have a strong working relationship with the Oporto management team. I have been with Oporto for over 18 years and the team is the strongest we have had in that time."

"A range of media are quoting incorrect facts about Oporto. Over the last 3 years sales have increased more than 30%. We have a strong franchise system and an engaged Franchise Advisory Council which I am a part of. We have issues like any business however we collectively work these through. Our profitability like all business is under pressure from electricity prices, labour rates and input costs, however we are actively addressing these as a group. This includes working with suppliers for efficiencies and cost reductions. New stores which have opened, including my recent store in ██████████, is performing above expectations."

Red Rooster

The Franchise Advisory Council has unanimously endorse the following statement:

The Red Rooster" Franchise Advisory Council (made up of franchisee delegates) does not share the views expressed by the Association. Specifically,

- That the views expressed in the Association's submission are not shared by the Red Rooster Franchise advisory Council
- The approach taken by this Association is not endorsed by the Red Rooster Franchise Council
- That the Craveable Brands Association refused to meet with members of the Franchisee Advisory Council and to date has not engaged or communicated directly with the FAC.

██████████, ██████████ said,

"I have been involved with Red Rooster for the last two and a half years as a Franchise Partner, during this tenure I have found the brand to be supportive, transparent and above all else committed to the growth of the brand and subsequently our respective businesses, having been involved in several franchised business's throughout my working life I am comfortable in the knowledge that from my personal experience the support and expertise they offer is second to none in the franchise sector and I would gladly have that conversation with anyone that would suggest differently."

██████████ said,

"I have a strong and supportive relationship with Red Rooster and Craveable Brands and I do not support or share the views of the 'Franchisee Association of Craveable' and their submission to the Parliamentary enquiry."

"I fully support the Craveable business model and have personally experienced good growth. I have also been given good support and guidance by Craveable on a range of initiatives."

Chicken Treat

██████████ 15 year veteran of Chicken Treat

"I'm extremely comfortable with the way that Craveable and Chicken Treat in WA have treated me as a franchise partner. Whenever there is an issue there's always an open line of communication and that's from the chairman all the way through the network. I do not agree with these claims in any way."

CRAVEABLE BRANDS PTY LTD



Submission to the

Parliamentary Joint Committee on
Corporations and Financial Services

into the

Operation & Effectiveness of the Franchising Code of Conduct

Executive Summary

This is a submission from Craveable Brands Pty Ltd to the Parliamentary Joint Committee on Corporations and Financial Services regarding its review of the Operation and Effectiveness of the Franchising Code of Conduct (**Franchising Code**).

1 Background

- 1.1 Craveable Brands Pty Ltd (**Craveable**) is a wholly owned Australian company operating in the quick service restaurant (QSR) sector and is home to three iconic Australian chicken brands, Red Rooster, Chicken Treat and Oporto.
- 1.2 Currently the group employs 540 people directly across Australia. Through our franchise network our brands employ a further 11,900 people across Australia. Craveable operates a fully franchised system with over 400 franchisees across 570 stores, including both metropolitan and regional locations.
- 1.3 In recent years the shared success of Craveable and its franchisees has been driven by investment in a transformation strategy focused on innovation, enhanced brand positioning and channel expansion.
- 1.4 With its operational genesis in Perth in the 1970's, Craveable has carved a unique place in the Australian corporate landscape.

2 The Craveable Brands Business Model

- 2.1 Craveable has a best practice framework to support its franchisees including:
 - extensive induction and development programs;
 - ongoing coaching and training through a business consultant structure;
 - consistent and regular state meetings;
 - a Franchise Advisory Council (FAC); and
 - annual conferences to learn, collaborate and build strategies.
- 2.2 A formal governance program is in place to monitor and approve business activities including:
 - new store selection;
 - lease negotiations and renewals;
 - franchisee support and investment; and
 - approval of restaurant purchases by franchisees.

3 Summary of Craveable Brands' Concerns regarding the Franchising Code

- 3.1 The Franchising Code plays an important role for all stakeholders in the Australian franchising sector, and is generally fit for purpose. Craveable has three specific concerns regarding the operation and effectiveness of the Franchising Code which it seeks to raise with the Committee.

These relate to:

- the complexity of current Disclosure Documents;
- the right of a franchisor to terminate for breaches of the Fair Work Act; and
- the right of a franchisor to immediately terminate for an irremediable breach.

4 General Views on the Franchising Sector

- 4.1 In 2014, Griffith University in conjunction with the Franchise Council of Australia published an authoritative study on franchising in Australia.¹
- 4.2 The study revealed that:
- there were 1,160 business format franchisors in Australia in 2014;
 - there were an estimated 79,000 units operating in business format franchises;
 - there were more than 460,000 people employed directly in the franchising sector; and
 - the sales turnover of the entire franchising sector was estimated at \$144 billion.
- 4.3 While these statistics are now somewhat out of date, they highlight the significance of the franchising sector in the Australian economy and as a source of employment.
- 4.4 The majority of franchisors (like ourselves) are responsible corporate citizens who care for their franchising network and have developed extensive processes and have systems in place to monitor Code compliance. We work together with our franchisees to maintain and increase growth and profit (as both are interrelated).
- 4.5 This view is substantiated by information reporting provided by the Australian Competition and Consumer Commission (**ACCC**) in 2017 on its website. The ACCC notes only five instances where the ACCC took action against franchisors in 2017.
- 4.6 We have no tolerance for those few in the franchising sector that regularly fail to comply with the Code and or other relevant legislation, and as a result bring disrepute to the franchising sector.

5 Disclosure

- 5.1 The disclosure of key terms, conditions and other information in a franchise agreement is a key element of a successful franchising system. However, Craveable Brands is concerned that the complexity of the disclosure requirements under the Franchising Code of Conduct invariably leads to extremely lengthy disclosure documents. This actually serves to defeat the public policy intent of the Code.
- 5.2 By way of example, our current disclosure document for each of our Brands is around 347 pages. We consider that the complexity and the length of the disclosure documents actually discourages prospective franchisees from reviewing the content.
- 5.3 Our view is supported by the ACCC as noted in its submission to the 2013 Franchising Code Review.
- 5.4 In its submission the ACCC stated:
- “There is anecdotal evidence (and complaint data) suggesting that many franchisees do not read, or at least do not understand, the disclosure document they receive before they enter into a Franchise Agreement. This is usually attributed to the length and complexity of most disclosure documents.”²*
- 5.5 We are of the view that the disclosure document should be simplified (and not expanded) or alternatively we would support the introduction of a one or two page summary document or risk statement that accompanies the disclosure document.

¹ Griffith University, *Franchising Australia 2014*, Griffith University, 2014

² Australian Competition and Consumer Commission, *ACCC Submission to the 2013 Franchising Code Review* Australia Competition and Consumer Commission, 2013

- 5.6 The use of a risk or summary statement was supported by the ACCC in its 2013 submission referenced above and was also supported in the “Report to the Hon Fran Bailey Minister for Small Business and Tourism October 2006” by the Franchising Code Review Committee.³
- 5.7 It was also alluded to by the Hon Dr Craig Emerson MP, then Minister for Small Business, when announcing the 2010 amendments to the Code where he asked the franchising sector to deliver a short “Plain English” document for franchisees setting out their rights and responsibilities.
- 5.8 The statement would be supplemental to the existing disclosure requirements under the Code and would emphasise the key costs, benefits and risks of a franchise system.

6 Termination Rights – Breaches of the Fair Work Act

- 6.1 The Franchising Code currently permits a franchisor to terminate immediately in special circumstances (clause 29 of the Franchising Code). We support the notion of supplementing those termination provisions contained in clause 29 by simplifying the termination process in the event of a significant breach or deliberate non-compliance of the Fair Work Act by a franchisee.
- 6.2 Currently clause 29 allows immediate termination where the franchisee has acted fraudulently.
- 6.3 The notion of acting fraudulently is difficult to prove and in our experience, only blatant circumvention of the Fair Work Act supported by statements from franchisee employees is sufficient to substantiate a claim of fraud.
- 6.4 We support supplementing these provisions by requiring franchisees to provide franchisors with sufficient evidence to substantiate a franchisee’s compliance with the Fair Work Act.
- 6.5 In our experience, whilst the majority of franchisees are fully compliant and work collaboratively to provide the necessary information to substantiate compliance with the Fair Work Act, there is a small minority of franchisees that refuse or make it difficult for a franchisor to collect the necessary information to substantiate compliance.
- 6.6 In our view if a franchisee deliberately and repeatedly frustrates this process and fails to provide the necessary information then there should be an immediate right on the part of the franchisor to terminate.
- 6.7 In addition, we support the creation of a new right to terminate (without the necessity for notice to remedy) where the franchisee has deliberately / intentionally breached the Fair Work Act. In those instances the franchisee should not be afforded time to remedy such a breach. Our view centres on the fact that these types of breaches can significantly damage the reputation of a brand and as a direct consequence affect the businesses of the majority of other franchisees who are endeavouring to do the right thing.
- 6.8 Accordingly we are of the view the Code should be amended to add:
- a requirement that franchisees must provide proper information in a timely manner to substantiate compliance with the Fair Work Act and to the extent that they fail to do so the franchisor should have the opportunity to terminate immediately; and
 - a requirement permitting a franchisor to terminate immediately (without the necessity for issuing a breach notice) where a franchisee has deliberately engaged in conduct that breaches the provisions of the Fair Work Act.

³ Office of Small Business, *Review of the Disclosure Provisions of the Franchising Code of Conduct*, Report to the Hon Fran Bailey MP Minister for Small Business and Tourism, 2006

7 Termination Rights – Clarity around Irremediable Breaches

- 7.1 We consider that the Code is deficient in that it does not address the rights of a Franchisor to immediately terminate in respect of an irremediable breach (although we consider this is implied).
- 7.2 We advocate that the Code should be amended to specifically address this issue by stating that a Franchisor has a right to immediately terminate for an irremediable breach.
- 7.3 There is logically no point in issuing a breach notice and allowing a reasonable period to lapse when there is no possibility of the breach being rectified.

8 Response to the Submission made by the “Franchisee Association of Craveable” (the “Submission”)

- 8.1 We note that a submission has been lodged with the Committee by a group called the Franchisee Association of Craveable, and we welcome the opportunity to address the issues raised in this document. We preface our comments by noting that:
- We do not know who the members of the Association are or how many active members it has;
 - We do not know who the Association represents;
 - We do not believe the submission is representative of the views of the franchisee majority within Craveable Brands;
 - We have never been contacted by the Association; and
 - We consider the assertions and claims in the Submission are inaccurate and omit important context that is essential to the proper understanding of the operation of a broader franchise system.
- 8.2 The Submission makes some general assertions about our franchise network. We note that franchisees are required to provide us with regular financial information. This enables us to review the profitability of each store and work with individual franchisees on implementing action plans if necessary and where appropriate provide suitable financial support. In general terms we note our system is healthy and growing.
- 8.3 In relation to the issue of Cost of Goods, Craveable utilises its scale to leverage effective buying power across 570 restaurants and three brands.

Craveable endeavours to ensure that the price supplied to franchisees on any product or service provided to the franchise network is better than that which can be obtained by an individual franchisee on a sustainable basis. This is in the direct commercial interest of both franchisor and franchisee.

In sourcing the best suppliers, Craveable has primary regard to:

- Pricing;
- Quality;
- Ethical sourcing; and
- Sustainability.

There is a mechanism contained in each of our franchise agreements that allows franchisees the opportunity to request that Craveable formally evaluate suggested routes to procure better quality or cheaper supplies.

In relation to rebates, these are expressly permitted under our franchise agreements and we disclose the necessary information required in our disclosure documents, including the identity of suppliers. It should be noted that Craveable has recently achieved significant savings on some key products, with a material quantum of savings to be passed to franchisees as a result.

The Submission refers to benchmarking to other franchised systems. While Craveable conducts its own benchmarking on an ongoing basis, the systems noted have different products and offerings and therefore may not be directly comparable.

- 8.4 The Submission raises the issue of Loyalty Programs, which Red Rooster and Oporto introduced in 2015. These programs were heavily invested in by Craveable and introduced to the brands in an effort to more effectively market to the brands' most loyal customers and drive increased visits, sales and marketing fund return on investment.

The loyalty programs enable the brands to better understand their loyal customers' purchasing behavior and then communicate with them directly, in a more relevant and personalised manner in real time via email, SMS and social media.

The Loyalty programs have approximately 350,000 members for Red Rooster and 120,000 for Oporto and have been globally recognised for their effectiveness in international industry awards. It has been a sound investment with loyalty members on average spending more per visit and visiting three times more often than non-loyalty customers.

- 8.5 While the Submission identifies a concern with Craveable representing three iconic Australian chicken brands, we are firmly of the view our brands can co-exist in the same market. Each brand has very distinct differences in terms of geographical footprint, store design, product offering and target audience. With ownership common for over 10 years, there are many examples where more than one Craveable brand successfully operates in the same market. Whilst the core protein is chicken, the unique meals are positioned to different customer demographics seeking distinct flavours and experiences.

- 8.6 The Submission discusses the issue of Home Delivery. This was trialed by Red Rooster franchisees (who expressed an initial interest to do so) in 2014 and carefully rolled out to the franchise network in stages.

It was very clear from the trials that our customers valued the option to access delivery. Significant cost modelling was presented from franchisees during the trial and expansion. There were information sessions conducted by Craveable in every market to work through concerns and identify operational best practice.

At a broader operating environment level, we note that Morgan Stanley forecast that from 2016 to 2018, the online takeaway market in Australia will increase by over 50%.⁴

Given the increasing importance of delivery in the takeaway market, Red Rooster implemented delivery in order to listen to the voice of the customer, gain important market share, provide margin and growth to franchisees and grow franchisees' businesses over the longer term. In particular Craveable (and many franchisees) wanted to provide a point of differentiation within the QSR marketplace.

It is important to note that home delivery is not compulsory although 260+ Red Rooster restaurants (out of a total of 360) have engaged in home delivery.

- 8.7 The Submission makes assertions concerning transparency of the marketing fund. Craveable Brands is fully compliant with the obligations contained in the Code regarding financial statements around marketing funds. While we acknowledge the historical importance of "Free to Air Media spend" as raised by the Association, Craveable's ongoing research and monitoring of traditional and new media channels has led us to adjust our media mix to also capture digital media as its consumption has rapidly increased.

- 8.8 Disclosure is an important part of the franchising sector and the legal requirements for disclosure are set out comprehensively in the Code.

Craveable views these obligations seriously and is fully compliant with the requirements of the Code in respect of each of our three brands.

A review of each of our Disclosure Statements commences around June each year and is undertaken over the course of three to four months due to its complexity. Each section of our Disclosure Statement is carefully reviewed by our executive management team and updated in accordance with the requirements of the Code.

⁴ Morgan Stanley Research, *Online Aggregators in Australia*, 15 January 2018

8.9 The Submission discusses the issue of building insurance. As noted we take out umbrella insurance for two reasons. Administratively this ensures that every franchisee has building insurance in place. Secondly, given the number of stores covered by this insurance policy, Craveable is able to achieve competitive premium rates as a result of our aggregate buying power. Having one policy also assists in potentially a more efficient claim resolution process. We recharge this to our franchisees under our licensing arrangements on a pro rata basis. The policy and premiums we pay are reviewed on an annual basis.

8.10 The issue of technology costs is raised in the Submission. We have introduced additional technology software and hardware into our systems to ensure we are able to run the most efficient restaurants with market-leading, standardised infrastructure to maximise up-time and to ensure full compliance with legislative requirements. Craveable has significantly enhanced the technology solutions across our restaurants with minimal incremental cost to franchisees.

Craveable also considers it essential for each franchisee business to have systems and tools in place to manage their workforce time and attendance ensuring compliance with the Fair Work Act. In this regard, the use of biometric fingerprint scanners for the purposes of staff clocking on and off is recognised by the Fair Work Ombudsman as being one of the most secure methods for employees to use to record hours worked.

The implementation of Zuus (a workforce shift scheduling app) is another example of ensuring our franchisees meet the standards and expectations set out in the Fair Work Act.

8.11 We are fully compliant with our obligations in respect of leasing as contained in the Code. Each licence we enter into with our franchisees contains a copy of our head lease which discloses the annual rent we pay as head lessor.

If we negotiate new rental terms, we ensure the franchisee is fully aware of the key terms and they are required to sign a form that specifically sets out any changes such as rent.

In addition, there are legislative requirements in every State requiring us to provide additional disclosure under the various Retail Leasing Acts. Where applicable we provide that disclosure including the annual rent.

We do not receive any rebates from landlords.

8.12 The Submission makes unfounded allegations in respect of restaurant sales involving Association members. Craveable categorically rejects any claim that it has interfered in the sales process of any franchisee sale, acted any differently in the way it deals with breach notices as between different franchisees, or has taken to harassing any of its franchisees regarding small or minor issues. We note that these claims are totally unsubstantiated.

To the extent there are any significant unresolved issues with franchisees, Craveable promotes the utilisation of mediation. This is considered to be both cost effective to franchisees and an excellent means of resolving franchise disputes.

9 Franchisee Engagement

9.1 Craveable believes the engagement and partnership with its franchisees to be paramount in a successful business model and the opportunity to deliver sustainable growth.

9.2 We measure the engagement of franchisees formally every two years through a third party process. The results have seen high levels of participation and top quartile engagement.

9.3 Regular interactions by Craveable management with franchisees in store, through state meetings and FAC meetings are also a key part of our commitment to ongoing engagement with franchisees.

10 Franchisee Support

- 10.1 Craveable has a formal process to support franchisees when adverse circumstances arise.
- 10.2 Support can be in the form of rent, royalty and marketing fund relief and is generally on a short term basis. As Craveable is on the head lease for approximately 400 locations, support is primarily provided in the form of rent relief.

11 Conclusion

- 11.1 The franchising sector is a mature and important part of the Australian economy, employing hundreds of thousands of Australians.
- 11.2 We consider that the majority of franchisors are not only compliant with the Franchising Code but are keen to ensure the effectiveness and sustainability of franchising systems in Australia. This certainly represents the position of Craveable.
- 11.3 We consider that as a whole the Franchising Code is working effectively and do not believe that broad-ranging changes are necessary.
- 11.4 We do however recognise the need to review the current form of disclosure and termination rights in respect of the failure of franchisees to comply with their requirements of the Fair Work Act.