



11 May, 2018

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

Dear Committee Members,

Submission to the Parliamentary Committee's Inquiry into the Operation and effectiveness of the Franchising Code of Conduct

1. About KFC Australia

Kentucky Fried Chicken Pty Ltd ("**KFC Australia**") is the Australian licensee of the trade marks and systems behind KFC, the longest operating quick service restaurant franchise system in Australia.

The first KFC in Australia was launched 50 years ago in Guildford NSW. There are now around 640 KFC restaurants in Australia. Of those, KFC Australia owns and operates 53 restaurants. The remainder are owned and operated by our community of franchisee partners.

The KFC system in Australia employs more than 35,000 people – around 1 in 7 Australians - making us a substantial creator of jobs in this country. KFC Australia has also been a registered provider of nationally recognised training qualifications for more than a decade and invests more than \$1.5 million in training annually: almost 1000 employees attain a nationally recognised qualification each year.

As a result of our successful franchising model, around 2 million Australians are able to enjoy our delicious food every week.

2. About our Franchisee Partners

The 60 franchisees who operate KFC restaurants in Australia comprise a range of different franchisees. At one end of the spectrum we have several "corporate franchisees" who own and operate large numbers of restaurants. Our largest franchisee partner in Australia is Collins Foods Limited, which operates 226 restaurants across multiple states. Our second, third and fourth largest franchisee partners are large private companies operating 70, 61 and 50 restaurants respectively. At the other end of the spectrum, we have many franchisee partners who operate just one or two restaurants and who personally run many aspects of the business to maintain a profitable business.

Our franchise agreements are for a minimum term of 10 years with a maximum contract length of 20 years. Around 25% of our franchisee partners have been successfully operating their restaurants for more than 20 years.

3. How we operate

KFC's business in Australia, like all businesses, is cyclical and enjoys periods of prosperity and challenge. Despite this cycle, long-term our business has grown and generated substantial wealth and employment for our franchisees.

We believe this is a testament to the close, productive relationships we seek to maintain and enjoy with our franchisees and to the fundamental strength of our business model. We also believe it is due to the high calibre of franchisees we have selected to be part of our system. Our franchisees not only have the financial capacity and sound business acumen to manage a business, but an energy and willingness to invest in our brand on an on-going basis.

One of the key traits of our franchise system is partnership and collaboration. In fact, our relationship with our franchise partners centres around a powerful "Franchise Partnership Pact" which sets out a list of principles as to how we interact. As franchisor, one of those guiding principles is "be mindful of franchisee economics in all we recommend". Another is "get franchisee input and involvement before decisions are made".

KFC Australia does not make decisions that could affect our franchise partners without first consulting with them and ensuring we understand any issues that may impact their business. As part of our collaborative approach, we have a range of forums, committees and councils that include our franchise partners as active members and participants. For example, we have an advertising co-operative, KFC Adco Limited ("**Adco**"), which governs KFC's advertising and marketing initiatives and manages all of the advertising contributions made by franchisees under the terms of our Franchise Agreements. Adco comprises equal numbers of franchise partners and KFC Australia representatives and meets several times a year.

We also have a Supply Chain Management Council, a Development Council, an Operations Council, a Human Resources "One System" council, a Workplace Health and Safety Council, an Information Systems Council, a Digital Council and a Business Model Working group. All of these councils and groups comprise representatives from both our franchisee community and KFC Australia and meet on a regular basis. Additionally, we have regular Franchisee Communications meetings where information about our business, our strategy and other key initiatives are presented and openly discussed with our franchisee partners.

We want to make sure our franchisee partners generate at least a reasonable, but preferably an exceptional, return on their investment. To this end, we aim to set our new or expanding franchisee partners up for success by requiring them to complete 6 months of management training in a KFC restaurant before they become a franchisee or are permitted to operate multiple restaurants (as the case may be).

We are considerate of our franchisee partner's position concerning the impact of new restaurant growth plans. We do not build or permit other franchisees to build new restaurants in locations that will significantly impact sales at an existing restaurant operated by another franchisee partner. We have a sales impact policy that we apply and tools we use to measure potential sales impact before any final approval to build is given.

Our supply chain is operated on a not-for-profit basis. We use our scale and purchasing power in an effort to negotiate the best possible pricing from our suppliers for the benefit of the franchise system, without

compromising on quality. We are open and transparent with our franchisee partners about pricing. When we receive a rebate from a supplier, we pass it back to our franchisees.

As with most franchised businesses, we do from time to time have different views from our franchisees on certain issues. However, we seek to address our differences in a timely and constructive manner and with healthy discussion and debate to reach solutions that are in the best interests of the franchise system as a whole.

4. Terms of Reference

This Submission addresses paragraphs (a) and (e) only of the Terms of Reference.

4.1 Paragraph (a): the operation and effectiveness of the Franchising Code of Conduct, including the disclosure document and information statement ... in ensuring full disclosure to potential franchisees of all information necessary to make a fully informed decision when assessing whether to enter a franchise agreement....

KFC Australia considers that the Franchising Code of Conduct (“**Code**”), the Disclosure Document and the Information Statement are effective in ensuring that franchisees have all of the information necessary to make a fully informed decision when assessing whether or not to enter into a franchise agreement.

We spend considerable time and effort to ensure our Disclosure Document properly discloses all information required to be disclosed to franchisees under the Code. We also take care to ensure that the Disclosure Document is updated and issued as and when required. Even though most of our franchisee partners are highly experienced operators, we always encourage them to seek their own legal, accounting and business advice before renewing or entering into a new franchise agreement.

If we have one criticism of the Code, it is that the prescriptive nature of the information required to be disclosed means that our Disclosure Document is lengthy (around 280 pages in total), complex and time consuming to prepare. The length and complexity of the document means some of our franchisee partners will not always take the time to read it in its entirety, which defeats the purpose of disclosure.

For there to be effective communication to franchisees of important information about a franchise system, we believe there would be benefit in simplifying the disclosure requirements rather than expanding them. At the same time it should be mandatory for new or inexperienced franchisees to seek proper professional advice before entering into a franchise agreement.

4.2 Paragraph (e): the adequacy and operation of termination provisions in the Franchising Code of Conduct

KFC Australia believes the current termination provisions in the Code are adequate but that there is room for improvement.

Part of being a good franchisor is taking steps to preserve and enhance the brand. From time to time, this will include taking steps to prevent non-compliant franchisees from damaging the reputation of the brand to the detriment of the franchise system and in turn, the businesses of other compliant franchisees.

One issue we have with the Code is that it does not give a franchisor the right to immediately terminate a Franchise Agreement in circumstances where a franchisee deliberately or intentionally breaches the *Fair Work Act 2009*. As it stands, clause 27(4) of the Code provides that if a franchisee has remedied a breach, then the franchisor may not terminate the franchise agreement for that breach. In the absence of such a right we are concerned it will be difficult for us to take steps to protect the many young individuals employed by the franchisee in its restaurants, as well as the reputation of our brand and our own position as franchisor. Accordingly, we would like to see the Code amended to provide an additional right of termination to address this scenario.

A second issue regarding the termination provisions concerns our inability to terminate a franchise agreement where a franchisee commits the same or a similar breach of the Franchise Agreement over and over again. In other words, where there is a “serial offender” who potentially puts the reputation of the brand and the businesses of our compliant franchisee partners at risk.

We believe the Code should be amended to provide for an immediate right of termination in circumstances where a franchisee commits multiple breaches of the same or a similar nature within a certain timeframe (eg 12 months), whether or not that franchisee has remedied each breach.

Our position on further reform

As a long-standing, well-regarded franchisor, KFC Australia considers that it should not be “tarred with the same brush” as some other franchise operators that have ineffective business models or who operate in an unethical or unscrupulous manner.

We will support in principle further regulation, policies and initiatives that:

- are clear, certain and simple to execute;
- require new and inexperienced franchisees to receive proper professional advice and education on the risks associated with franchising before purchasing a franchise for the first time;
- foster greater compliance with existing legislation; and
- address clearly abhorrent or unethical behaviour.

However, we will not support further regulation that has the effect of over-burdening or indirectly “punishing” those franchisors who do the right thing in their franchising activities and by their franchisees. This is because ultimately such additional regulation will result in franchisors and in turn, franchisees, incurring additional compliance costs.

For instance, we will not support further regulation or initiatives that:

- create unnecessary additional administrative and legal costs for KFC Australia or our experienced franchisee partners;
- are vague or uncertain;
- unduly interfere with the rights of the parties to enter into and rely on commercial contracts;
- make franchising commercially disadvantageous relative to other forms of comparable business arrangements;
- make franchisors even further accountable for breaches of laws by franchisees or suppliers; or
- make Australia a less attractive investment option by fundamentally changing the balance of return in our franchising arrangements.

On behalf of KFC Australia, thank you for the opportunity to make this submission.

Yours sincerely,

Sally Glover
Chief Legal & Corporate Affairs Officer, KFC SOPAC