



Re: The Fair Work Amendment (Protecting Vulnerable Workers) Bill 2017

Executive Summary

Making franchisors liable for labor violations by their franchisees will have the perverse effect of hurting vulnerable workers by reducing employment opportunities and damaging the largest vocation training industry in Australia. Franchising accounts for 8% of Australian GDP and is a major contributor to employment and job creation. While improving the monitoring, compliance and penalties for franchisees breaching employment law is commendable, it can be achieved without damaging the fundamentals of the franchise model by imposing a joint employer standard upon it. These provisions in fact weaken the bill's aims, as they would result in one of two scenarios:

- 1) Either the franchisors would scale back the services they provide their franchisees in order to demonstrate they are not joint employers, or,
- 2) If the standard was unavoidable, they would slow their growth and expansion and likely invest in fewer franchise opportunities and increase the number of corporate owned stores, meaning fewer opportunities for prospective small business owners in Australia.

Furthermore, international franchisors, which account for a significant share of the market would face an even greater burden, being physically and legally more distant from their franchisees. This added risk and barrier to expansion would lead to a slowdown in the expansion of American and international franchise businesses in Australia, reducing opportunities, trade, job creation and mutually beneficial economic relations.

IFA endorses the aim of strengthening labor law compliance in Australia and specifically endorses the submissions made by the Franchise Council of Australia. **IFA writes to clarify the unique impact this legislation would have on international franchisors in hopes that harm can be minimized.**

About the IFA

The International Franchise Association (IFA) is the world's oldest and largest organization representing franchising worldwide. Celebrating over 57 years of excellence, education and advocacy, IFA works to protect, enhance and promote franchising. IFA members in the United States and around the world include franchise companies in over 300 different business format categories, individual franchisees and companies that support the industry in marketing, law and business development. Most IFA members are already engaged in or are seriously considering engaging in international expansion.

Impact on US Franchises

There are more than 90 United States franchises active in Australia, and IFA knows first-hand that your market is appealing to additional franchisors considering international growth. U.S. brands figure prominently among the largest franchise networks in Australia. 10 of the bigger American brands (including Subway at almost 1,500 units, McDonald's at more than 900 units and KFC at over 600 units) collectively account for more than 5,000 units.

U.S. franchisors in Australia are operating from the opposite side of the globe. This yields obvious challenges of visibility for franchisors with respect to the subtleties of the conditions of employees of Australian franchisees. One of the reasons companies use the franchise model internationally is to benefit from the superior knowledge of local market conditions that franchisees offer. Knowledge of compliance with local workplace laws is but one of the areas where international franchisors commonly look to their franchisees.

Franchisors tend to use different development models for international growth than they do for domestic growth. By far the most common international development model is master franchising. In this model, the international franchisor awards rights for a country (or region) to a master franchisee. The (Australian) master franchisee operates a limited number of units directly and then sub-franchises. In sub-franchising, the master franchisee awards the right to operate individual units to sub-franchisees. The master franchisee trains and supports the sub-franchisees and shares their royalties with the international franchisor. This structure means **the franchisor has almost no direct engagement with or oversight of sub-franchisees**. Because they are operating twice removed from sub-franchisees, this puts international franchisors in an impossible position if they are to be held responsible for workplace violations in units operating under their trademarks. **Many franchisors would not grow into markets with these conditions or curtail existing plans to protect themselves from liability they cannot control.**

Negative Impact

As a matter of illustration, in 2016 IFA commissioned a report by FRANdata on the impact in the U.S. if franchisors were made liable for labor violations committed by their franchisees. FRANdata conducted a comprehensive examination of decades of regulatory findings for more than 2,900 franchise brands. This analysis was supplemented with industry white papers, government data, and recent telephone surveys. Survey participants collectively represent over 300 franchisors, more than 15,000 franchised businesses, and over 6,700 lenders. Lending information was retrieved from U.S. Small Business Administration's (SBA) published data for more than 1.1 million SBA guaranteed loans over the 15-year period from 2000 to 2015. The views of these executives and franchise business owners were overwhelmingly clear.

FRANdata's interviews and analysis pertain to the U.S., but similar dynamics should apply in Australia. Among the most interesting findings are:

- An estimated **40,000 franchise businesses, affecting more than 75,000 locations, would be at risk of failure because of the joint-employer status**, which would increase labor and operating costs beyond operating margins.

- As a result of business failures, downsizing, and a decline in the rate of new franchise business formation, **more than 600,000 jobs may be lost or not created.**
- The equity value of franchise businesses is expected to drop by a third to a half. Rising costs will have a negative multiplier effect on valuations. Potentially, hundreds of thousands of franchise business owners will see the equity they have built in their businesses over years decline as the advantages of the franchise model are stripped away, causing higher operating costs.
- Loss of the franchise business model's operating efficiencies, combined with rising costs, will render the **investment in a franchise business less attractive** to entrepreneurs seeking to start new businesses.
- The combination of negative valuations, a decrease in the rate of investment in new franchise businesses, an increase in the rate of franchise business failures, and a lower rate of job creation in the franchising industry will have **an overall negative impact on GDP contributions.**

The full report can be accessed at: <https://www.frandata.com/joint-employer-impact-study/>

The franchise model has an inherent aspiration of mutuality. The franchisor receives a limited percentage of the franchisee's revenues (usually 5 to 7%) in royalty and therefore has a strong incentive to want to help franchisees succeed. International franchising puts major global brands and best practices into Australian hands. The franchisor receives royalties and the overwhelming majority of the earnings and benefits such as jobs and supply chain remain in local hands.

Conclusion

Franchising provides a path of employment, job training and advancement for employees on a massive scale, including to people who would not otherwise be able to find similar opportunity. Imposing unmanageable liabilities on international franchisors will produce dramatically reduced expansion and job creation, **hurting precisely the people the Australian Government is setting out to protect.** By accounting for the unique circumstances of international franchisors, the Australian Government can minimize this harm.

IFA truly understands the concerns which have motivated the Australian Government to consider legislation and abhors the workplace violations that have occurred. A response that addresses those responsible is appropriate. A joint employer standard threatening parties without control would overreach and undermine that aim. **IFA hopes that the Australian Government will account for the increased oversight difficulties for international companies with franchisees in Australia.**