

The Secretary,

Parliamentary Joint Committee on Corporations and Financial Services

Department of the Senate

PO Box 6100 Parliament House

Canberra

ACT 2600

Mr Chairman,

I would like to submit my personal views and concerns in relation to the current, outdated franchise laws.

I am 39 years of age and have been employed by Competitive Foods Australia Limited within the KFC Division since leaving school 24 years ago. Besides offering extensive career opportunities throughout my career, CFAL has also encouraged me to attend University, in which I'm proud to have received a Bachelor of Business, Masters of Business and Bachelor in Human Resources. Without the support of CFAL this would not have been achievable.

Evidently, I have an invested interest in the outcome of this inquiry, as my current position is under threat. Although under the current economic climate, employment elsewhere is obtainable; my long term loyalty to the company and their ongoing support is paramount to my future career prospects.

It is testing, to be solely a bystander and watch franchisees and small businesses become innocent victims of bullying tactics and franchisor opportunism, therefore I insist that my concerns be heard.

Franchisor opportunism is the name given to predatory conduct and strong arm tactics by franchisors which depends upon the exploitation of a pre-existing power relationship between a franchisor and franchisee, which makes the franchisee vulnerable or an “economic captive” to the demands of the franchisor.

Additional regulation is needed to complete the existing regulatory scheme in two key respects:

- Express recognition of a duty of good faith, to reflect the relational nature of franchising and to protect franchisees against the improper use of power by franchisors under standard form contracts.
- Establishing minimum standards of conduct in relation to franchise renewals, by adopting a good cause procedure that removes the incentive for franchisors to engage in opportunistic conduct and make profits at the expense of their franchisees.

These reforms are long overdue and are consistent with the main principles of regulation in the franchising industry, that have been recognized since

the late 1970s by the Swanson and Blunt Committees, and more recently by the Reid and Matthews Committees.

The economic logic of franchisor opportunism is that, in the absence of regulation, it is attractive for the franchisor to take over profitable outlets for less than their full market value. Three ways in which a franchisor can reap substantial profits by this conduct include:

- a. buy the business cheaply and then sell it for full value to another franchisee;
- b. operate the business as a company owned store and take 100% of the business profits (now that its viability has been established) and not merely a small % royalty;
- c. 'clip the ticket' by churning successive new franchisees who pay franchising fees, and higher royalties (ie. an established business may support a higher royalty due to the lower risks, than a start-up site).

In November 2007, CFAL experienced the needless closure of one of its fully operational KFC Restaurants at Rockingham in Perth. Three more restaurants are scheduled for closure in December 2008, with another 46 to close progressively as their terms expire over the next 20 years. These closures have exposed a serious void in franchising regulation in Australia, which affects not only CFAL and its employees, but all franchisees, large and small.

CFAL have operated the KFC Franchise in WA for nearly forty years, and now the current Franchisor, [REDACTED], are refusing to renew Franchise Agreements as they fall due.

[REDACTED] have offered no reason for doing this. CFAL has slowly and successfully built brand equity and recognition within the Western Australian market commencing in 1968 at KFC Melville. Since then, CFAL have opened and established another 49 stores with in Western Australia.

It is my perception that the working relationship between the franchisee and franchisor has unfortunately progressed to a dysfunctional state. [REDACTED] have offered to buy back the network of 50 stores at a reduced rate of up to 40%. This amount is said to represent their pre-expiry cash flows, rather than their ongoing concern value. Due to the fact the owner of CFAL, Mr. Jack Cowin rejected this offer, [REDACTED] are using bully tactics by not renewing any upcoming leases. Franchisors have no reason to oppose duty of good faith. [REDACTED] are clearly taking advantage of their position of power by engaging in opportunistic behavior.

Incidentally this is the second occasion in which KFC (then owned by [REDACTED], [REDACTED] predecessor) has used its power of renewal to obtain opportunistic benefits. This earlier occasion occurred in 1999 when [REDACTED] advised CFAL that it would only renew 12 of CFAL's franchise agreements which were then under consideration on condition that CFAL either (i) agreed to divest its interest in the [REDACTED] business; or (ii) sold all of its KFC restaurants to a third party approved by [REDACTED].

CFAL have had ongoing support from the West and South Australian Governments. In March 2008, the W.A. Government enquiry recommended more disclosure in relation to non-renewal and expiry of franchise agreements, including entitlements to goodwill payments.

The South Australian parliamentary enquiry in June 2008 recommended amending the Code to include good faith and renewal obligations and a definition of unconscionability, in s.51AC.

In conclusion, franchising has revolutionised retailing in Australia. The number of franchisors operating in Australia has increased by approximately 58% in 10 years from 693 in 1998 to an estimated number of 1,100 in 2008. This number of franchisors serves a national population estimated at 21,400,000 at August 25, 2008, or one franchise system for every 19, 454 Australians.

It is of interest that in the United States a duty of good faith is implied in every contract governed by the Uniform Commercial Code (UCC). A general principle of good faith is also part of all contractual relationships in many European jurisdictions. These are jurisdictions where franchising continues to thrive. Indeed the duty is thought by many to provide an important measure of security for contracting parties.

As a sub-franchisor for Australia, Mr. Jack Cowin is acting reasonably in his own interests by seeking stronger regulation of franchising laws; however he is also acting in the best interests for the Australian economy for now and in the future.

The amendment of this franchising loophole is detrimental to small businesses, franchises and employees alike.

My assumptions are that the Australian Government would act in the best interests of the Australian people, not for an American based franchise.

Mr. Jack Cowin has the master Franchise for Burger King (Hungry Jacks) in Australia; the law change will also affect his Franchise business within the Hungary Jack division. However, Mr Cowin is not concerned about that, as he knows this law is unjust on both sides of the fence.

Attached for your perusal, is an overview chronology of the franchising industry, which will show that this loophole has been of serious concern for a number of years and needs to be acted upon for the best interests of everyone involved. As you would be aware the franchise industrial contributes about 14% GDP to the economy, annually.

As outlined above it is not only one mans company or business that is affected here, it is the overall consequence that franchising laws has on future business, economy, employees and ultimately families that are affected by these archaic franchising laws.

Yours Faithfully,

Todd Gooch

FRANCHISE INDUSTRY: OVERVIEW CHRONOLOGY

- 1969 *First restaurant* opened by CFAL at Melville in Perth (KFC).
- 1974 *Trade Practices Act* (TPA) introduced.
- 1976 *Swanson Committee* recommended the TPA include a provision for fair compensation to franchisees for a wrongful failure to renew a franchise agreement (para 5.7).
- 1979 *Blunt Committee* recommended that the TPA include a provision giving franchisees a right to claim damages for wrongful termination or non-renewal (para 11.47)
- 1980 *Petroleum Retail Franchise Marketing Act* 1980 (Cth) introduced, s.17 provided a good faith right of renewal for petrol station franchises – now cl.32 of the Oilcode.
- 1997 *Reid Committee* acknowledged on-going problems with franchising and recommended protection against “unfair conduct” (ch. 6).
- 1998 *Franchising Code* introduced under Part IVB of the TPA.
- 1998 *Unconscionable conduct* provisions introduced in the TPA (s.51AC) based on model provisions recommended by the Reid Committee.
- 2006 *Matthews Committee* report into the disclosure provisions of the Code – recommended an express good faith obligation be included in the Code (Recommendation 25).
- 8/2007 *Amendments to the Code* in relation to certain disclosure issues, but excluded the good faith recommendation. These came into force in March 2008.

- 10/2007 *ALP Election Policy* : “Labour believes that the Franchise Code should include good faith obligations as long as the scope of this obligation is well defined”.
- 11/2007 *Closure of KFC Rockingham* due to refusal of [REDACTED] [REDACTED] [REDACTED] to renew the franchise agreement.
- 11/2007 *Minister Bailey* promised to “move swiftly if we are returned to government to close off this loophole” (West Australian) in response to Rockingham closure.
- 3/2008 *WA government inquiry* recommended more disclosure in relation to non-renewal and expiry of franchise agreements, including entitlements to goodwill payments.
- 4/2008 *South Australian Parliamentary inquiry* recommended amending the Code to include good faith and renewal obligations and a definition of unconscionability in s.51AC.
- 6/2008 *Federal Parliamentary Inquiry* in relation to franchising convened.
- 12/2008 *Threatened closure* of three more KFC restaurants in WA by [REDACTED] at Whitfords, Beechboro and Thornlie, when existing franchise agreements fall due for renewal.