

Franchising Alert

Small Business Commissioner Act 2011 – Backdoor Franchising Legislation

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After a sometimes heated debate, the *Small Business Commissioner Act 2011 (Act)* was passed by the South Australian Parliament in October 2011. While the Act is yet to come into operation it will have far reaching consequences for those engaged in franchising activity in South Australia.

The stated aim of the Act is to achieve greater support for small businesses in South Australia in relation to commercial disputes and non-compliance issues by providing a framework for small businesses to resolve their disputes through a Small Business Commissioner (**Commissioner**).

The Commissioner will have a broad range of powers and functions and is to perform them with a view to the development and maintenance of relationships between small business, other businesses and government that are based on “*dealings conducted fairly and in good faith*”.

However, the history of the Act suggests that it is, in reality, a form of backdoor State based franchising legislation. Once the Act comes into force it is expected that the Commissioner will be given power under it to regulate the conduct of franchisors operating in South Australia and enforce compliance with the national *Franchising Code of Conduct*.

When will this Act affect Franchisors

The Act gives the SA Government the power to adopt industry codes of conduct by regulations made under the *Fair Trading Act 1987 (SA)* and without further legislation by Parliament.

It is expected that one of the first codes to be prescribed will be the *Franchising Code of Conduct* either in its current form or, more likely, with modifications.

The Minister will in substance have the ability to modify the Code by regulation and without further legislation. At the same time, the Commissioner will be required to

enforce compliance and may seek civil penalties for non-compliance even though there is no provision for such action in the Franchising Code itself.

While the Act requires that the Minister consult with relevant stakeholders prior to any regulations being made, the Act does not state how that consultation will take place, nor does it state how, if at all, the Minister must address issues raised by stakeholders or provide them with any redress in the event that they are dissatisfied with the consultation process or the Minister’s response to it.

How will this Act affect Franchisors?

The conduct of franchisors is currently regulated at a national level by the Federal Government and the ACCC under the Franchising Code and the *Competition and Consumer Act 2010 (Cth)*. However, once that Franchising Code is prescribed under the Act a new regime of State based franchising regulation will come into force in South Australia.

All franchisors with franchises operating in South Australia will be subject to the Act and:

- the Commissioner will monitor the fair treatment of franchisees in their commercial dealings with franchisors;
- all complaints against franchisors by franchisees in relation to commercial dealings (ie alleged unfair market practices) will be made to and investigated by the Commissioner;
- the Commissioner will ‘facilitate’ resolution between franchisees and franchisors and decide what it considers is the appropriate dispute resolution process (regardless of the parties’ views);
- the Commissioner may investigate a breach by a franchisor of an industry code;

- a breach of the Franchising Code by a franchisor may result in the Commissioner taking action in the Magistrates Court to impose civil penalties:
 - in the case of a body corporate – not exceeding \$50,000; and
 - in the case of a natural person – not exceeding \$10,000.
- an **alleged** breach of the Franchising Code by a franchisor may result in the imposition of an expiation notice (on the spot fine):
 - in the case of a body corporate – not exceeding \$6,000; and
 - in the case of a natural person – not exceeding \$1,200.
- the Commissioner may compel a franchisor to provide information that it requires for the performance of its functions under the Act. The Commissioner can request information without a complaint being made against the franchisor or proving that reasonable grounds exist for the request;
- a franchisor will not be compelled to disclose or produce information where that information might tend to incriminate the franchisor or is subject to legal professional privilege;
- confidentiality attaches to any information provided to the Commissioner. However, the exceptions to this provision are extremely wide (eg information may be disclosed to any person concerned in the administration of another law relating to trade or commercial practices or the protection of consumers);
- fines of up to \$20,000 may be imposed where a franchisor fails to provide information

In addition to the new enforcement provisions, the Franchising Code itself is likely to change for the purpose of South Australian law. Tony Piccolo, a Labour MP who has championed the Act, has foreshadowed in the media that a franchising code prescribed under the Act will contain an obligation of good faith in the franchising relationship. Recommendations made by a South Australian Parliamentary enquiry in 2008 (of which the relevant Minister was the presiding member) may shed light on other changes the government will seek to introduce. They included:

- Registration of franchise agreements;
- Continuous disclosure obligations on franchisors;
- Amendments to the alternative dispute resolution requirements; and

- Mandating that the exclusion of goodwill payments to franchisees at the end of a franchise arrangement constitutes unconscionable conduct.

National application of the SA Act

This State based legislation will clearly regulate the conduct of franchisors and franchisees in their dealings within South Australia.

However, the extra-territorial provisions of the *Fair Trading Act* may yet mean that it also operates to regulate dealings between interstate franchisors and their franchisees in SA as well as dealings between franchisors located in South Australia and their franchisees wherever they are located.

The Act is therefore likely to create a deal of uncertainty for franchisors and franchisees alike and give rise to difficult legal and practical issues of cross border conflict between State and Federal laws and Code obligations.

One obvious and undesirable area for conflict is the power of the Commissioner to investigate and resolve disputes in any manner considered appropriate and the now well established Franchising Code processes for franchise dispute mediation.

The Federal Minister for Small Business, Senator Sherry, has expressed the Commonwealth's concern at this possible conflict and noted the possibility of a challenge under section 109 of the Commonwealth Constitution.

What should Franchisors do?

You should continue to ensure compliance with the national *Franchising Code of Conduct*.

We predict that the SA Minister will move quickly to prescribe the *Franchising Code of Conduct* (either in its present form or in a modified form) as a state Code of Conduct. Once that occurs we anticipate an early test of the Act's objective of ensuring that business dealings are "*conducted fairly and in good faith*" as the Commissioner is pressed by franchisees to aggressively enforce the Franchising Code, prosecute breaches and test the limits of his enforcement powers in South Australia and beyond. That may lead to the Constitutional challenge foreshadowed by Senator Sherry.

However, unless and until the Courts clarify the position, Franchisors should ensure they understand their rights and obligations under the Act, especially in relation to any request or investigation by the Commissioner, and take careful advice before responding.

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