

# **RESPONSE TO CONSULTATION PAPER ON FRANCHISE LAW**

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## **INTRODUCTION**

The following is a response to the Manitoba Law Reform Commission's Franchise Law Consultation Paper published in May 2007. The "Paper" addresses the question of whether Manitoba needs franchise legislation and provides a review of the state of franchise law in Canada, Australia, and the United States. Finally, the Paper poses a series of questions with regard to what should be done in Manitoba. The Reform Commission's report may be found online at <<http://www.gov.mb.ca/justice/mlrc/projects.html>>.

This response discusses the need for franchise law in Manitoba, drawing from the experience of other provinces. Having done so, a discussion of the issues raised in the Law Reform Commission's Paper will ensue.

## **IS FRANCHISE LAW NEEDED IN MANITOBA?**

### **1. The Need for Franchise Law in Manitoba**

The Legislative Assembly of Manitoba has already had the opportunity of discussing the question of whether franchise law is needed in the province. Mr. Jim Maloway, MLA for Elmwood, introduced *Bill 18, The Franchises Act*, at the 3rd session of the 35th Legislature in 1992. The Bill followed the Alberta *Franchises Act*<sup>1</sup> very closely, providing for the delivery by a franchisor to a franchisee of a statement of material facts containing prescribed information, and further providing that no person shall trade in a franchise in the Province

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<sup>1</sup> R.S.A. 1980, c. F-17 (repealed).

of Manitoba until an application for registration in prescribed form, and a prospectus in respect of the offer of the franchise, is filed with the Manitoba Securities Commission and a receipt is issued for such prospectus. However, the Bill did not receive second reading and did not pass into legislation.<sup>2</sup>

For the purposes of this paper, Mr. Maloway's 1992 attempt is useful as it produced a series of discussions in the Legislative Assembly dealing with the need for franchise legislation in the province. Mr. Maloway introduced Bill 18 on March 3, 1992, arguing that franchise legislation is needed in the province because, up until then, Manitobans had lost large amounts of money buying franchises ranging from \$5,000 to \$100,000. Overall, he described the issue as a "growing problem."<sup>3</sup> Mr. Steve Ashton, MLA for Thompson, addressed the Assembly in support of the Bill, stating that its introduction is not only warranted due to the "hard times we are faced with" but also as a major public service. The "hard times" which he mentions are in reference to the activities bordering on fraud, at the hand of franchisors, that franchisees have had to face because of a lack of protection of their rights.<sup>4</sup> He further stated:

I ask the question why the government is not doing anything to prevent people from being ripped off as they are on an almost daily basis by those, Mr. Speaker, who are misleading them about their abilities to deliver the kinds of promises we have seen in terms of franchises.<sup>5</sup>

Agreeing with Mr. Ashton and Mr. Maloway, Ms. Becky Barrett, MLA for Wellington, delivered a comprehensive speech in favor of Bill 18. Ms. Barrett emphasized the emergence of franchises over the past 20 to 30 years and their popularity with many individuals and families in Manitoba who wish to invest in franchises. Moreover, she pointed out a series of factors in support of franchise legislation. First, franchisees

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<sup>2</sup> Frank Zaid, *Canadian Franchise Law*, (Toronto: Thomson-Carswell, 2006), p. 2-142Z.45.

<sup>3</sup> Manitoba, Legislative Assembly, *House Debates (Hansard)*, Vol. 21, (3 March 1992), (Hon. Denis Rocan); Legislative Assembly of Manitoba, "House Debates," 3rd Session of 35<sup>th</sup> Legislature (3 March 1992), online: Hansard <[http://www.gov.mb.ca/legislature/hansard/3rd-35th/vol\\_21.html](http://www.gov.mb.ca/legislature/hansard/3rd-35th/vol_21.html)>.

<sup>4</sup> Manitoba, Legislative Assembly, *House Debates (Hansard)*, Vol. 56 (30 April 1992), (Hon. Denis Rocan); Legislative Assembly of Manitoba, "House Debates," 3rd Session of 35<sup>th</sup> Legislature (30 April 1992), online: Hansard <[http://www.gov.mb.ca/legislature/hansard/3rd-35th/vol\\_56.html](http://www.gov.mb.ca/legislature/hansard/3rd-35th/vol_56.html)>.

<sup>5</sup> *Ibid.*

usually have virtually no experience with franchising, so that legislative protection is needed. Second, there are no laws in Manitoba to guarantee the safety and security of franchisees' funds against fraud and illegal actions on the part of the franchiser. Third, if Alberta, possessing a government that is not known for its progressive legislation that supports and protects individuals, already has an Act in place, it is evidence that Manitoba is far behind.<sup>6</sup> She concluded her speech with the following remark:

I...urge government members to join us in supporting Bill 18, which is a very fine, necessary, important and certainly overdue piece of legislation.<sup>7</sup>

Regardless of the fate endured by Bill 18, it is important to note that these three MLAs recognized the need for franchise legislation in 1992 and, 15 years later, nothing has been done to fix the problem. The situation in Manitoba has not improved since 1992, as evidenced in the following cases.

In **John Deere Ltd. v. G.A.E.L. Inc.**,<sup>8</sup> the manufacturer, John Deere Ltd. ("Deere"), improperly terminated a dealership agreement. Although the Manitoba Court of Queen's Bench found that Deere had every right to terminate the agreement, the court found that Deere had done so with undue haste and unreasonably. Changing the locks on the dealership to prevent the dealer from re-entering the premises was not "reasonable termination." Had franchise legislation been in place, G.A.E.L. could have had protection against Deere under a good faith and fair dealing provision.

A recent example of a franchisor abusing his power to subdue a franchisee is **Halligan v. Liberty Tax Service Inc.**<sup>9</sup> The franchisor in this case unilaterally withdrew funding from the franchisee's store without notice and caused an immediate drop in the franchisee's revenue after the franchisee refused to use a particular name. In one instance, Liberty did not provide software that would work. Following Halligan's complaints, a replacement was mailed to him, even though his franchise

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<sup>6</sup> Manitoba, Legislative Assembly, *House Debates (Hansard)*, Vol. 82 (9 June 1992), (Hon. Denis Rocan); Legislative Assembly of Manitoba, 3rd Session of 35th Legislature: Tuesday June 9, 1992, online: Hansard <[http://www.gov.mb.ca/legislature/hansard/3rd-35th/vol\\_82.html](http://www.gov.mb.ca/legislature/hansard/3rd-35th/vol_82.html)>.

<sup>7</sup> *Ibid.*

<sup>8</sup> [1994] CarswellMan 323, 96 Man. R. (2d) 106.

<sup>9</sup> [2003] MBQB 174, 36 B.L.R. (3d) 75, 176 Man. R. (2d) 57.

location was in the same building as Liberty's head office. The court further describes Liberty as harassing Halligan even in the face of an injunction granted in 2001. The Manitoba Court of Queen's Bench provides a more detailed description of Liberty's action in its 2006 judgment of the same case. The Court described Liberty's conduct as malicious, high handed, and reprehensible. This is following a depiction of Liberty forcing Halligan out of business by withdrawing services during the tax season, setting up competing stores and referring clients away from Halligan.<sup>10</sup>

Both the Winnipeg Free Press and Winnipeg Sun reported on the most recent franchise scandal in the province. Mr. Hisham Alard arrived to Winnipeg from Syria in 2004 and was looking for business prospects. He found an advertisement about a Pizza One franchise in the newspaper. The franchise cost \$50,000. Mr. Alard's store never opened and he received nothing in return for his deposit.<sup>11</sup> Although this is the only Pizza One case that has been reported in Manitoba, there are several examples in Ontario.<sup>12</sup>

It is important to note in this context that a review of court decisions is unlikely to provide an accurate representation of franchise disputes because some franchise agreements require arbitration and do not reach the courts.<sup>13</sup> Nonetheless, the fact that some cases are still getting to court is somewhat indicative of what Mr. Maloway alluded to in 1992. In other words, Manitoba is facing a problem with franchisors abusing franchisees and legislation must be introduced to address the situation.

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<sup>10</sup> *Halligan v. Liberty Tax Services Inc.*, [2006] 8 WWR 97, 202 Man. R. (2d) 268.

<sup>11</sup> Alexandra Paul, "City Man Burned by Pizza Franchise Scam," *Winnipeg Free Press*, (12 February 2007), online: Winnipeg Free Press Live <<http://www.winnipegfreepress.com/local/story/3877052p-4484925c.html>>; Paul Turenne, "Avoid Being the Victim," *Winnipeg SUN* (12 February 2007), online: Winnipeg SUN Media <<http://www.anthonysfranchiseinformation.com/WinipegSun12Feb2007-2.htm>>.

<sup>12</sup> Some of the most recent Pizza One cases from Ontario include *Ramjit v. 3 of 1 Pizza & Wings (Canada) Inc.*, [2004] CarswellOnt 6402; *Scott v. 3 for 1 Pizza & Wings (Canada) Inc.*, [2003] CarswellOnt 3790; *MAA Diners Inc. v. 3 for 1 Pizza and Wings (Canada) Inc.* (2003), 30 B.L.R. (3d) 279; *Ali v. Triple 3 Holdings Inc.*, [2001] O.J. No. 5755.

<sup>13</sup> Manitoba Law Reform Commission, "Consultation Paper on Franchise Legislation," online: Current Projects <<http://www.gov.mb.ca/justice/mlrc/projects.html>> at 15.

## 2. The Ontario Example

When considering Manitoba's need for franchise legislation, there are two primary reasons why Ontario's experience should be taken into account. First, it is one of the three provinces in Canada to have franchise legislation, known as the most franchisee friendly version. This is important in Manitoba because, according to the Law Commission's report, it is a franchisee rather than a franchisor province.<sup>14</sup> Second, when drafting model legislation, the Uniform Law Conference of Canada followed Ontario's legislation as its base. However, rather than looking at Ontario's *Arthur Wishart Act (Franchise Disclosure), 2000*,<sup>15</sup> the following will consider articles and Legislative Assembly discussions to determine what factors influenced the province to introduce such legislation.

Ontario first addressed the idea of introducing franchise legislation with the Grange Report recommendations of 1971.<sup>16</sup> However, no act would come to fruition until the much-publicized *Pizza Pizza* case, **887574 Ontario Inc. v. Pizza Pizza Ltd. (1995)**,<sup>17</sup> demonstrated that franchisees were in dire need of protection. A new committee was formed and given the name Franchise Sector Working Team (FSWT). The FSWT delivered its report in 1995. Although the report was not conclusive on several issues, the members of the FSWT agreed that disclosure from franchisors to potential franchisees before a franchise was purchased was necessary. Three years after this report, the Ontario government published a consultation paper on proposed franchise disclosure legislation. This led to the introduction of Bill 93, which died on the order paper and was subsequently reintroduced as Bill 33. The latter passed its first reading in 1999 and received royal assent June 8, 2000.<sup>18</sup> This process sparked much legislative debate in support of franchise legislation.

The need for franchise legislation was directly addressed during Ontario's Legislative Assembly meeting of May 17, 2000, while Bill 33 received its second reading.<sup>19</sup> In describing the nature of the franchisor-

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<sup>14</sup> *Ibid.* at 47.

<sup>15</sup> S.O. 2000, c. 3.

<sup>16</sup> S.G.M. Grange, Report of *the Minister's Committee on Referral Sales, Multi-Level Sales and Franchises*, Ontario Ministry of Financial and Commercial Affairs (1971).

<sup>17</sup> 23 B.L.R. (2d) 59, [1995] O.J. No. 936 (Ont. Ct. Gen. Div.).

<sup>18</sup> Edward N. Levitt, "Ontario Franchise Legislation," online: Gowlings Resource Centre <<http://www.gowlings.com/resources/publications.asp?pubid=1159>>.

<sup>19</sup> Ontario, Legislative Assembly, *Debates (Hansard)*, No. 60A (17 May 2000), at 3087 (Hon. Gary Carr); Legislative Assembly of Ontario, "Official Records for May 17, 2000," online:

franchisee relationship, Mr. Tony Martin, MPP for Sault Ste Marie, spoke of the fear that is generated when franchisees deal with franchisors. This fear may be created when franchisees are forced to sign contracts of adhesion, restricting their ability to manage their business. Mr. Martin proceeded to tell a number of stories where franchisees had been abused by franchisors.

The most shocking story Mr. Martin told was about Mary Carlucci, a grocery store owner. In the 10 years as owner, she was able to turn her store into a very successful business, a vast improvement from what it used to be. One day, she received a phone call from the parent company to say that there was going to be a marketing meeting at the local hotel. While she was gone at the supposed marketing meeting, the parent company moved in and changed the locks, took over the cash registers and told family members who were there to go home. Ms. Carlucci no longer owns the store.<sup>20</sup>

Mrs. Claudette Boyer, MPP for Ottawa-Venyer, speaking in support of Bill 33, stated that the Bill should only be seen as the first step in regulating franchises. She further stated:

We really cannot deny the fact that legislation in this field is desperately needed. After hearing testimonials of people who lost their life savings and went through many hardships, it became clear to other members of the committee and myself that something had to be done.<sup>21</sup>

Mr. Jean-Marc Lalonde, MPP for Glengarry-Prescott-Russell, also spoke in support of Bill 33. In doing so, he stated:

Bill 33 is an Act concerning fair dealings between franchisees and franchisors. The only thing I can say is that this legislation is about five years too late for many franchisees in Ontario.<sup>22</sup>

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Debates (Hansard) <[http://www.ontla.on.ca/web/house-proceedings/house\\_detail.do?Date=2000-05-17&Parl=37&Sess=1&locale=en](http://www.ontla.on.ca/web/house-proceedings/house_detail.do?Date=2000-05-17&Parl=37&Sess=1&locale=en)>.

<sup>20</sup> *Ibid.*

<sup>21</sup> *Ibid.*

<sup>22</sup> *Ibid.*

The testimonials described in the Legislative Assembly of Ontario make it clear that franchise legislation is necessary to prevent franchisors from abusing franchisees. Protection was effected in Ontario by composing a franchises act that focused on pre-sale disclosure of material facts, the duty of good faith and fair dealing and the freedom to associate with other franchisees.

Although Manitoba does not have to adopt every provision from the *Arthur Wishart Act (Franchise Disclosure), 2000*, it is useful to have as an example of current franchise legislation. Ontario spent over 30 years conducting research, releasing reports, interviewing people and holding many House debates to introduce such legislation. Manitoba can now look at Ontario's experience and learn from it by not only taking advantage of the latter's research but also consider current issues with the franchise legislation and draft an improved version.

### **3. Uniform Law Conference of Canada (ULCC)**

The ULCC has done much work in relation to the introduction of franchise legislation across Canada. John Sotos and Frank Zaid delivered a report discussing franchise legislation at the ULCC's 2002 Annual Meeting.<sup>23</sup> The report supports the introduction of such legislation on the grounds that a lack of pre-sale disclosure means that franchisees are often entering into long-term agreements and complex contracts without an adequate opportunity of receiving relevant background information. Furthermore, franchise legislation will help to protect small business owners, hopefully prevent unnecessary disputes, and provide consumer confidence in the stability of franchisee units.<sup>24</sup>

Of particular concern for Manitoba, a "franchisee province," is the fact that, according to the report, franchisees in many cases are unsophisticated business investors who may be entering business for the first time. Their family savings or assets are often at risk through the granting of personal guarantees or security to the franchisor or lending institutions financing a transaction.<sup>25</sup>

Although the ULCC advocates for uniformity across Canada, even if it is not achieved, its message is clear: franchise legislation is needed.

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<sup>23</sup> Frank Zaid and John Sotos, "Status Report on National Franchise Law Project," (Paper Presented to the Uniform Law Conference of Canada Annual Meeting, August 2002), online: ULCC, Proceedings of Annual Meetings <<http://www.ulcc.ca/en/poam2/index.cfm?sec=2002&sub=2002ib>>.

<sup>24</sup> *Ibid.* at 23.

<sup>25</sup> *Ibid.* at 23-24.

Regardless of the differences that may exist between the Ontario, Prince Edward Island and Alberta Acts and the ULLC *Uniform Franchises Act [UFA]*,<sup>26</sup> the bottom line is that the four advocate for franchise legislation as a means of protecting franchisees from the abuse of franchisors and, consequently, generating more confidence in the system. In addition to leveling the playing field between franchisors and franchisees, a further consequence of uniform legislation may be the eventual standardization of fair business practices.

#### **4. Canadian Franchise Association (CFA)**

The Canadian Franchise Association (CFA) represents over 400 franchise companies and the professionals who support this way of doing business. Members must abide by the CFA's Code of Ethics, found in full on its website at <http://www.cfa.ca/page.aspx?url=CodeOfEthics.html>, as well as the Association's rules of disclosure.<sup>27</sup>

The CFA's Disclosure Document Guide, revised in 2002, sets similar disclosure requirements as those seen in Alberta and Ontario's franchise legislation. It covers issues ranging from the disclosure of business experience of the franchisor, franchise experience of the franchisor, information regarding other existing franchisees, bankruptcy and insolvency to existing litigation. The CFA recommends the inclusion of a certificate of disclosure where: the franchisor asserts that the information provided is in accordance with the CFA's disclosure policy, warns the franchisee to examine the franchise investment carefully and recommends the consultation of legal advisors prior to executing the agreement.<sup>28</sup>

The advantage that the CFA presents to franchisees residing in Manitoba is that it provides them with similar protection to other provinces where franchises are statutorily regulated. In other words, franchisees in Manitoba are protected in a similar way as a franchisee in Alberta, Ontario or Prince Edward Island, where franchise legislation has been introduced enforcing disclosure.

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<sup>26</sup> Uniform Law Conference of Canada, *Uniform Franchises Act [UFA]*, online: Selected Uniform Statutes

<[http://www.ulcc.ca/en/us/Uniform\\_Franchises\\_Act\\_En.pdf](http://www.ulcc.ca/en/us/Uniform_Franchises_Act_En.pdf)>.

<sup>27</sup> Canadian Franchise Association, "Welcome to the Canadian Franchise Association," online: About Us

<<http://www.cfa.ca/page.aspx?url=AboutUs.html>>.

<sup>28</sup> Canadian Franchise Association, "CFA Disclosure Rules," online: Already in Franchising <<http://www.cfa.ca/Page.aspx?URL=CFADisclosureRules.html>>.



The primary shortcoming of the CFA's Code of Ethics and Disclosure Requirements is that it is only binding on members of the CFA. This means that a franchisee will only be protected if the franchisor is a member of the Association. Furthermore, whereas Ontario and Alberta have introduced penalties for breach of their respective Acts, the CFA can only revoke a non-compliant member's membership from the Association. This is hardly a sufficient deterrent to an unscrupulous franchisor, who is likely not going to register with the Association to begin with.<sup>29</sup> As stated in the Uniform Law Conference of Canada's "Status Report on National Franchise Law Project," in 2002:

Voluntary codes by trade associations have inherent drawbacks in that they are not subject to governmental or statutory delegation of authority. Therefore, the most common remedy available to an industry association is expulsion of a non-compliant member. [...] non members of the association are unaffected by the policies or codes of conduct of the association in question.<sup>30</sup>

Regardless of this drawback, it is important to note that the existence of the CFA's Code of Ethics and Disclosure Requirements means that there are already several franchisors who are abiding by disclosure rules and having to provide disclosure documents to potential franchisees in Manitoba. These include such large companies as A&W Food Services of Canada Inc., Orange Julius of Canada Ltd., Boston Pizza International Inc., Canadian Tire Corporation Limited, Pizza Hut, Play it Again Sports, Second Cup Ltd., and Dairy Queen Canada, to name a few.<sup>31</sup>

The CFA recognizes and supports the requirement of disclosure and ethical behavior in franchise relationships. This is evident in the fact that the Association requires all of its members to abide by its rules and regulations where no such laws are already in existence. This is more proof that franchise legislation is necessary in Manitoba.

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<sup>29</sup> Frank Zaid and John Sotos, *supra* note 23 at 25.

<sup>30</sup> *Ibid.*

<sup>31</sup> For a full list of CFA members, please refer to the CFA's official webpage under the heading "Canadian Franchise Association Members," online: Search Franchise Opportunities <<http://www.cfa.ca/MemberListing.aspx?menu=18>>.

## 5. Securities Regulation

Discussing the need for franchise legislation that mandates disclosure invariably necessitates a contrast with securities regulation. This is primarily because in several instances, franchise agreements can be analogous to securities. Currently, the question of whether a franchise agreement is a security must be addressed on a case-by-case basis, with the amount of control the franchisee has over its investment as the determinative factor.<sup>32</sup> Much like franchise legislation in Canada, securities legislation requires that a prospectus be issued. The prospectus is a lengthy document that sets out details of the company, business management, finances, existing securities, and the securities being qualified. The prospectus must provide full, true and plain disclosure of all material facts. Certain facts are mandatory, such as the background of the issuer, its officers and directors. These requirements are vital for policy reasons.<sup>33</sup>

Traditionally, securities regulation aimed to protect its investors by barring unscrupulous, fraudulent or incompetent issuers from taking advantage of naïve, unsophisticated investors. Currently, objectives of securities regulation include the protection of investors, ensuring that markets are fair, efficient and transparent, and the reduction of systemic risk. Investor protection is achieved in Canada, in part, through disclosure. Issuers, promoters and dealers must disclose certain amounts and types of information, both at the time of issue and on a continuous basis. Full, true and plain disclosure is a cornerstone of investor protection, allowing investors to assess properly the risks of certain investments.<sup>34</sup>

After drawing a parallel between franchise legislation and securities regulation, one quickly realizes that the same policy reasons for requiring disclosure apply to franchise law. Forcing franchisors to disclose franchise information to potential franchisees, as in securities, will be conducive to informed decision-making. In other words, demanding disclosure will allow franchisees to more properly assess their investment, thereby achieving the goal of franchise legislation. Therefore, Manitoba should adopt franchise legislation dictating adequate disclosure to make informed investment decisions.

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<sup>32</sup> David Johnston and Kathleen D. Rockwell, *Canadian Securities Regulation*, 3rd ed. (Markham: LexisNexis Canada, 2003) at 37-38.

<sup>33</sup> *Ibid.* at 83-84.

<sup>34</sup> *Ibid.* at 3-4.

## **6. Conclusion**

Having considered the experience of franchisees in Manitoba and Ontario, it has become clear that there is often a power imbalance between franchisors and franchisees. Since many franchisees in Manitoba will be more inexperienced than the franchisors they intend to franchise with, there needs to be an instrument to level the playing field. This instrument is a franchise act. By providing disclosure of information pertaining to the franchise, as well as requiring that all parties act in good faith, a franchisee will receive some comfort that all parties are required to employ fair dealing, hopefully evening-out the aforementioned power imbalance. In addition, because franchisees will be better informed after receiving a disclosure document, as required by franchise legislation, the possibility of litigation between the parties arising out of a misunderstanding should decrease. In other words, since a franchisor will be obliged to educate franchisees with regard to the proposed investment by providing a disclosure document, franchisees will be more aware of what to expect from the franchisor, lessening the chances of a misunderstanding.

It is not always the case that franchise legislation favors franchisees. Introducing an act would reduce transaction costs for franchisors who will have developed, in connection with their obligation to comply with the act, a standard disclosure document for Manitoba. Having said that, it is important to remember that even if franchisees are in great need of protection, a franchise act should not be so onerous as to deter franchisors from entering the Province.

Overall, the introduction of franchise legislation in Manitoba is long overdue. The Province is in the fortunate position of being able to consider the experience of other provinces, such as Ontario, and of other entities, such as the ULCC and the CFA, in order to draft the most comprehensive and effective franchise legislation in the country. Although franchisees stand to gain the most from such legislation, many franchisors would not even notice a change, either because they are members of the CFA or because they have franchises in one of the three regulated provinces and are already in compliance with other franchise legislation. The need for franchise legislation in Manitoba is clear, and the time to introduce it is now.

## IF LEGISLATION IS DESIREABLE, WHAT ELEMENTS SHOULD BE INCLUDED?

### 1. Disclosure Elements

#### a. Scope of Disclosure of Material Facts

The question posed by the Manitoba Law Reform Commission under this heading is whether the province of Manitoba should adopt the ULCC approach to disclosure of “material facts” (setting out an extensive list of matter that must be disclosed whether or not the information is material in a situation) or the approach under current provincial regulations, which provides less detail.<sup>35</sup>

The *Uniform Franchises Act*<sup>36</sup> enforces an obligation upon the franchisor to disclose, *inter alia*, financial statements as prescribed, copies of all proposed franchise agreements and other agreements relating to the franchise to be signed by the prospective franchisee as well as “all material facts.” Consequently, as per section 6(1), a franchisee may rescind the franchise agreement no later than 60 days after receiving the disclosure document if it does not contain “all material facts.”

To understand the requirements set by the ULCC, it is imperative to understand the meaning of the phrase “material facts.” The *Uniform Franchises Act*, *supra*, defines “material facts” as follows:

“Material facts” means any information, about the business, operations, capital or control of the franchisor or franchisor’s associate or about the franchise or the franchise system that would reasonably be expected to have a significant effect on the value or price of the franchise to be granted or the decision to acquire the franchise.

Complementing the disclosure requirement of “material facts” is an extensive list of required information that must be disclosed found in

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<sup>35</sup> Manitoba Law Reform Commission, *supra* note 13 at 49.

<sup>36</sup> Uniform Law Conference of Canada, *supra* note 26.

the *Disclosure Document Regulations*.<sup>37</sup> To say that the list is extensive is certainly an understatement. The ULCC places a heavy burden on the franchisor to disclose a long list of information pertaining to the franchise. As a result, the franchisee will have a significant amount of information about the franchise they are looking into acquiring.

Some of the disclosure requirements set out in the *Regulations* include information about the franchisor, such as business background, the name of every associate, the name under which the franchisor intends to do business, the length of time the franchisor has offered the franchise to prospective franchisees and the number of franchises granted in the five years immediately before the date of the disclosure document. Furthermore, the franchisee must be informed as to whether, during the 10 years immediately preceding the date of the disclosure document, the franchisor, the franchisor's associate or a director, general partner or officer of the franchisor has been convicted of fraud, unfair or deceptive business practices or is in violation of a law that regulates franchises or business, or if there is a charge pending against the person involving such a matter, and the details of any such conviction or charge.<sup>38</sup> Other topics in the *Regulations* include required information about the franchise, a schedule of current franchisees, a schedule of current businesses, a schedule of franchise and business closure information and financial statements. Without a doubt, requiring a franchisor to comply with such an extensive list of requirements will lead to the production of a very large disclosure document.

In contrast to the ULCC, the three regulated Canadian provinces, Ontario, Alberta and Prince Edward Island, place a less onerous disclosure obligation upon the franchisor. This is because neither province has such an extensive list of disclosure requirements. Let us begin by considering Ontario's legislation.

Section 5(1) of the *Arthur Wishart Act (Franchise Disclosure), 2000*, requires a franchisor to provide a prospective franchisee with a disclosure document and s. 5(4) sets its contents. According to the latter section, the disclosure document shall contain "all material facts." Since the Ontario Act employs the same definition of "material facts" as the ULCC, the primary difference between the two is the disclosure required by the regulations of each. As a side note, since Ontario and the ULCC

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<sup>37</sup> Uniform Law Conference of Canada, *Disclosure Documents Regulation*, online: Selected Uniform Statutes

<[http://www.ulcc.ca/en/us/UFA\\_Disclosure\\_Documents\\_Reg\\_En.pdf](http://www.ulcc.ca/en/us/UFA_Disclosure_Documents_Reg_En.pdf)>.

<sup>38</sup> *Ibid.* at s. 3(c).

have adopted the same definition of “material facts,” it would be prudent that Manitoba consider including it in its own legislation.

The *Regulation Made Under the Arthur Wishart Act (Franchise Disclosure)*, 2000, Part II, sets out a list of elements, divided into seven sections, that must be included in a disclosure document. The Ontario Act and the ULCC’s UFA are very similar, with the latter requiring disclosure in greater detail. This is because the ULCC’s approach in drafting its UFA was to consider the Ontario legislation as a working model, inserting changes and modifications considered appropriate for both clarity, inclusionary and consistency purposes.<sup>39</sup> Therefore, if Manitoba were to adopt the ULCC disclosure requirements, it would implement a more detailed version than Ontario’s.

A clear example of the difference in drafting between the two is the disclosure requirement with regard to training. Whereas s. 6(5) of the Ontario regulations requires “a description of any training or other assistance offered to the franchisee by the franchisor or the franchisor’s associate, including whether the training is mandatory or optional, and if the training is mandatory, a statement specifying who bears the cost of training,” s. 4(1)(h) of the UFA adds that the franchisor must also disclose where the training or other assistance will take place. This is just one of many examples showing how the ULCC has drafted more detailed legislation than Ontario while using the latter as a model. This is an important point to consider.

Peter Macrae Dillon, a prolific author and head of Siskinds’ Franchise, Licensing and Distribution Team in London, Ontario, states, “Unfortunately, the ULCC chose to uphold and reinforce the Ontario Act as the gold standard of franchise legislation.”<sup>40</sup> Mr. Dillon refers to the ULCC’s choice as “unfortunate” on the grounds that Ontario has the world’s toughest disclosure standard. What makes the Ontario Act, and consequently the UFA, so tough is that it has a purely open-ended disclosure model. As a result, the failure of a franchisor to include any fact that might be found to be material in the franchisee’s decision to purchase will result in unlimited liability for the franchisor.<sup>41</sup>

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<sup>39</sup> Uniform Law Conference of Canada, *Uniform Franchises Act Report – August 2004*, online: Proceedings of Annual Meetings, Report of the Uniform Franchise Act Working Group  
<[http://www.ulcc.ca/en/poam2/CLS2004\\_Franchise\\_Working\\_Group\\_Rep\\_En.pdf](http://www.ulcc.ca/en/poam2/CLS2004_Franchise_Working_Group_Rep_En.pdf)> at 1.

<sup>40</sup> Peter Macrae Dillon, “Will Franchising Survive as a Business Model Under Canadian Laws and Regulations?” (Summer 2006) Vol. 26, No. 1 *Franchise Law Journal* 32 at 32.

<sup>41</sup> *Ibid.*

The franchisor must thus exercise utmost diligence when preparing disclosure documents under the Ontario Act or, if adopted, the UFA. A franchisor must determine what about the franchise and franchisor is material and disclose it.<sup>42</sup> However, taking into consideration that Bill 33, the *Arthur Wishart Act (Franchise Disclosure), 2000*, was called “An Act to require fair dealing between parties to franchise agreements, to ensure that franchisees have the right to associate and impose disclosure obligations on franchisors,” the onerous character of the Ontario Act suddenly makes sense. If the purpose of the Act is to provide franchisees with full disclosure so as to allow them to make a proper decision, requiring such stringent disclosure is justified. As Edward N. Levitt said:

For those looking for a franchise investment specifically, the disclosure requirements of the Ontario Act will allow them to more easily shop for the right one.<sup>43</sup>

If Manitoba chooses to adopt the ULCC standard, franchisors will be faced with a new and more stringent standard than Ontario’s. This is because not only must “all material facts” be disclosed, but also because franchisors will be faced with a more extensive list of requirements under the *Regulations*. Thus, if the goal for introducing franchise legislation in Manitoba is to aid franchisees and ensure that sufficient information is disclosed, allowing them to make informed decisions when purchasing a franchise, the ULCC standard should be adopted. However, if the province is concerned about placing a heavy burden on the franchisor, the Ontario standard should be adopted.

There is yet another alternative to the level of disclosure that may be required from franchisors. Both the Alberta and P.E.I. Regulations<sup>44</sup> provide that a disclosure document complies with the Act if it is “substantially complete.” The Alberta Court of Queen’s Bench interpreted the meaning of “substantially complete” in ***Emerald Developments Ltd. v. 768158 Alberta Ltd.***<sup>45</sup> The court held that technical compliance with the regulations is not necessary so long as the franchisee was given sufficient and timely disclosure of facts relevant to the decision to purchase.

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<sup>42</sup> Edward N. Levitt, *supra* note 18.

<sup>43</sup> *Ibid.*

<sup>44</sup> Alberta *Franchises Act: Franchise Regulations*, A.R. 240/95, s. 2(4); Prince Edward Island, *Franchises Act: Regulations*, PEI Reg. EC232/06, s. 3.

<sup>45</sup> [2001] A.B.Q.B. 143.

Including such a provision in Manitoba would give the franchisor more freedom to err, while still granting the franchisee the required disclosure necessary to make an informed decision. In other words, the disclosure standard established in **Emerald** is in accordance with the purpose of establishing franchise legislation. Peter M. Dillon suggests that to fix the problem of having such onerous provisions, Ontario and the ULCC could adopt the substantial compliance standard of the Alberta Act. Doing so, Mr. Dillon argues, would remove franchising from the category of absolute liability.<sup>46</sup>

In conclusion, since the primary purpose of establishing franchise legislation is to protect franchisees and help in making the decision to purchase a franchise, the ULCC provisions should be adopted. In doing so, the franchisee will not only be provided with all material facts but also with an extensive list of standard information as required by the regulations. Making such onerous provisions more manageable for franchisors should be a “substantial compliance” provision, allowing a franchisor to err in providing disclosure documents while still providing the franchisee with all necessary information.

#### **b. Additional Disclosure Categories**

The Manitoba Law Reform Commission is considering further expanding the disclosure requirements by adding new provisions. The following are provisions that could be added to Manitoba’s regulations if and when they are adopted.

(1) When Prince Edward Island introduced franchise legislation in 2006, it did not adopt the UFA “as is.” Instead, a few points were modified. For instance, PEI is the only jurisdiction that allows for disclosure documents to be delivered electronically. Incidentally, Manitoba should adopt a similar provision, since so much business is done electronically today. Similarly, Manitoba should consider other effects that the Internet may have on franchises. For instance, a franchisee should be aware as to if and how a franchisor may compete with them through the use of a website. This provision may be added to the regulations under a section pertaining to the franchisor’s policies and practices regarding territory. Clearly setting this out in the regulations will prevent any litigation arising out of encroachment issues. Furthermore, the franchisee will know exactly what the franchisor may and may not do through the Internet.

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<sup>46</sup> Peter Macrae Dillon, *supra* note 40 at 34.



(2) Another addition to Manitoba's legislation should be the inclusion of a franchisor's arbitration or mediation results with former franchisees. As stated in the Reform Commission's Report, "A review of court decisions is unlikely to provide an accurate representation of franchise disputes, however. Some franchise agreements require arbitration and do not reach the courts."<sup>47</sup> If the current ULCC *Regulation made under the Uniform Franchises Act* requires that a franchisor disclose the results of previous litigation under s. 3(c) and (d), and following the Commission's statement, it may be useful to also disclose the result of mediation/arbitration for the franchisee to get a clear picture of the franchisor's legal history. However, since mediation/arbitration is often conducted and decided in confidence, a franchisor should only be obliged to disclose the number of cases that were addressed, for the past 10 years, through mediation/arbitration. In addition, terms of settlement should not be disclosed as it would constitute a breach of the confidential nature of mediation/arbitration, and may dissuade franchisors from being cooperative in future disputes.

The Reform Commission also recommends disclosing settled litigation and terms of settlement. Settled litigation should be treated the same as mediation/arbitration results. Consequently, Manitoba should require franchisors to disclose the result and not terms of settled litigation. Doing so will not only allow the franchisee to determine if the franchisor is reasonable and will settle, rather than being litigious, but also clearly portray the franchise's legal history.

(3) Manitoba's legislation should also include a provision whereby the franchisor must disclose franchise support resource and methods. This will not only allow a franchisee to choose a franchise that provides them with the desired support but will also benefit the franchisor that has such a system in that they will be preferred by several franchisees. This provision will be beneficial to both parties.

Manitoba would not be the first jurisdiction to adopt such a provision. For instance, Australia's *Trade Practices Act 1974* requires that a franchisor provide its potential franchisees with a summary of the conditions of the franchise agreement that deal with obligations of the franchisor, including an obligation to provide training both before and after the franchised business starts.<sup>48</sup> Furthermore, Article 142 Bis of

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<sup>47</sup> Manitoba Law Reform Commission, *supra* note 13 at 15.

<sup>48</sup> Australia, *Trade Practices (Industry Codes – Franchising) Regulations 1998*, SR 1998 No. 162 [Franchising Regulations], online: FCA – Franchising Code of Conduct

<<http://www.franchise.org.au/content/?action=getfile&id=28>> at s. 15.1(a).

Mexico's *Law to Develop and Protect Industrial Property* requires that a franchisor disclose to the franchisee all the necessary training required by the franchisee's employees, including the manner in which the franchisor will provide technical assistance.<sup>49</sup>

(4) Last, repeated sales of the same franchised outlet should be added to the disclosure requirements. A franchisee needs to know if the same franchise location has been sold repeatedly. This will in turn prevent a franchisor from constantly re-selling the same location, knowing that it will shut down soon, while blaming the franchisee for the store's failure and keeping the franchisee's deposit and other fees. In other words, this will alert a franchisee to either not get involved with a franchisor offering a location that has closed several times in a short period of time or adjust the price to reflect the poor location.

### **c. Wrap-Around Disclosure Document**

Regulations under the PEI and Alberta Acts contain "wrap-around" provisions. These permit a franchisor to use as its disclosure document a foreign document that has been authorized by the franchise laws of another jurisdiction, if supplementary information is included which discloses any additional information needed to make the foreign document comply with domestic disclosure requirements.<sup>50</sup> For example, subsection 3(2) of the regulations under the PEI Act states that a franchisor may use a document that is prepared and used to comply with the disclosure requirements under the franchise law or jurisdiction outside Prince Edward Island as its disclosure document to be given to a prospective franchisee in PEI, if the franchisor includes supplementary information with that document to bring it into compliance with the disclosure requirements under the PEI Act.<sup>51</sup> The question facing Manitoba is whether a wraparound provision should be included in its franchising legislation.

Prior to answering the question, it is helpful to consider the statutory requirement of "clarity of disclosure." Section 5(6) of the *Arthur*

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<sup>49</sup> Camara de Diputados del H. Congreso de La Union (Centro de Documentacion, Informacion y Analisis), *Ley de la Propiedad Industrial*, online: <<http://www.cddhcu.gob.mx/LeyesBiblio/pdf/50.pdf>>.

<sup>50</sup> Arthur J. Trebilcock, "Disclosure – The Advanced Course: Tricky Disclosure Issues and Some Drafting Tips," (Paper presented to the Ontario Bar Association's 6th Annual Franchising Conference: The Domino Effect, November 2006) [Toronto: OBA Continuing Legal Education, 2006] at 12.

<sup>51</sup> Edward N. Levitt, "Annual Legislative Update," (Paper presented to the Ontario Bar Association's 6th Annual Franchising Conference: The Domino Effect, November 2006) [Toronto: OBA Continuing Legal Education, 2006] at 45.

*Wishart Act (Franchise Disclosure) 2000*, demands that all information in a disclosure document must be accurately, clearly and concisely set out. Since one of the purposes of the Act is to rectify a perceived information imbalance between the franchisor and a prospective franchisee, any disclosure that is confusingly worded or formatted frustrates that purpose.<sup>52</sup> The requirement of “clear and concise” disclosure caters to parties unfamiliar with franchising. Mr. Trebilcock states:

Try to see the disclosure through the mind of a reader who has no experience in franchising, and no familiarity with the business being franchised. [...] So if you draft a disclosure document, take the time to provide a clear, concise description of the required contract provisions.<sup>53</sup>

Since this is quite a sensible requirement, it is important to maintain disclosure documents both clear and concise even with the addition of a “wrap.”

As stated earlier, Manitoba is a franchisee province. Thus, for the most part, franchisors are coming into Manitoba to sell their product and services, and not the other way around. It is imperative to take this into consideration when thinking about adding a “wrap-around” provision to Manitoba’s franchise legislation because of the origin of the foreign document that a franchisee would be receiving. When one looks at the list of CFA members, it is clear that the vast majority of franchisors coming into Canada hail from the United States.<sup>54</sup> Therefore, those franchisors coming into Manitoba will either be from the United States or other Canadian jurisdictions.

According to Edward N. Levitt, if a franchisor comes to Manitoba from a Canadian jurisdiction with a Canadian disclosure document, a “wrap-around” document for Manitoba makes good business sense.<sup>55</sup> The requirements vary slightly from province to province, so that adding a “wrap-around” clause will not be too costly for the franchisor or confusing to the franchisee reading it. Conversely, there would be a concern that a large and complex disclosure document from a foreign jurisdiction, containing a great deal of inapplicable information for

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<sup>52</sup> Edward N. Levitt, *supra* note 18.

<sup>53</sup> *Ibid.*

<sup>54</sup> Canadian Franchise Association, *supra* note 31.

<sup>55</sup> Edward N. Levitt, *supra* note 18.

prospective franchisees would not be clear and concise.<sup>56</sup> This, however, may not be the case with a disclosure document from the United States.

Currently, most U.S. franchisors use a uniform disclosure format called the Uniform Franchise Offering Circular or UFOC, which will become mandatory in 2008.<sup>57</sup> Thus, in a few years, all franchisors coming from the U.S. will have a UFOC at their disposition. A typical UFOC contains considerably more information than any of its Canadian counterparts. Therefore, a Canadian franchisee will have more information at their disposal when making the decision to purchase. The requirement that “plain English” be used and its standardized format with clear headings will ensure that the document will be clear and concise.<sup>58</sup> Therefore, if Manitoba were to adopt a “wraparound” provision, franchisees would still get a comprehensible disclosure document and franchisors will not have to go through the extra time and expense of composing a new one.

In the alternative, although adding a “wrap” will make a document comply with domestic law, the province’s extensive disclosure requirements (whether they emulate Ontario or the ULCC) may require that a franchisor change such a considerable portion of the body of text of the UFOC that it may be easier to create a new one to comply with Manitoba law.<sup>59</sup> The Ontario Superior Court of Justice commented on the use of a UFOC in **1518628 Ontario Inc. v. Tutor Time Learning Centres LLC**.<sup>60</sup> The court noted that the 200-page UFOC did not meet Ontario’s requirements because it did not have to be updated to reflect all material facts as they exist on the date that it is delivered to the prospective franchisee. Not only is it significant that the Superior Court rejected the UFOC as proper disclosure, but also, and primarily in this instance, that the UFOC was a 200-page document. If a wrap-around clause is added to such an extensive document, it is quite possible that it will cease to be as clear and concise as required by law, creating more difficulties for the franchisee.

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<sup>56</sup> *Ibid.*

<sup>57</sup> Manitoba Law Reform Commission, *supra* note 13 at 36-37.

<sup>58</sup> Peter Macrae Dillon, “The Case for the Use of Wrap-Around Disclosure Documents in Canada,” (Fall 2004) Vol. 24, No. 2 *Franchise Law Journal* 73 at 76; or online: Siskinds Resources, Articles of Interest

<<http://www.franchiselaw.ca/pdf/A%20Case%20for%20the%20Use%20of%20Wrap%20Around%20Disclosure%20Documents%20in%20Canada.pdf>> at 5.

<sup>59</sup> Debi M. Sutin and Arthur J. Trebilcock, “The Case Against the Use of Wrap-Around Disclosure Documents in Canada,” (Fall 2004) Vol. 24, No. 2 *Franchise Law Journal* 83 at 83.

<sup>60</sup> [2006] CarswellOnt 4593.

Assuming that the majority of franchisors enter Canada through Ontario, rather than Alberta, they will have to create a “new” disclosure document in compliance with the *Arthur Wishart Act (Franchise Disclosure), 2000*.<sup>61</sup> Consequently, when that same franchisor comes to Manitoba from Ontario, it will already have in its possession a Canadian disclosure document that will be easily adaptable to meet Manitoba’s requirements. Therefore, compliance by means of a wrap will be accomplished easily, clearly and concisely.

To accomplish the clarity requirement while using a wrap, Manitoba’s legislation should demand that franchisors provide both an index and summary of provisions. Doing so will allow franchisees reading the document to not only navigate through it with great ease but also to read the addenda and body together as one. Thus, when a franchisor decides to use a wrap, he will also have to include an index and summary to meet the clarity requirement. The layout of disclosure documents will be discussed later on under the heading “Additional Suggestions.”

In conclusion, Manitoba should only adopt a wrap provision if it also adopts the requirement that disclosure documents be clear and concise. This will ensure that franchisees will receive documents that meet the purpose of the Act, that is, to help them make well informed decisions. Moreover, if a franchisor foresees that adding a wrap will not produce a clear document, they will have the option of producing one specific for Manitoba.<sup>62</sup> In addition, Manitoba legislation should enforce the application of indexes and summaries when a wrap is used, allowing the reader to navigate through them with greater ease. At the same time, including a wrap will allow franchisors to enter the province with their foreign disclosure documents while still having to inform themselves of the domestic disclosure requirements in order to deliver an adequate wrap.

#### **d. Exceptions for Confidentiality, Site Selection or Refundable Deposit Agreements**

Disclosure documents must be delivered to a prospective franchisee 14 days before the signing of an agreement relating to the

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<sup>61</sup> Debi M. Sutin and Arthur J. Trebilcock, *supra* note 59.

<sup>62</sup> Edward N. Levitt, “The Prince Edward Island *Franchises Act*: Canada’s Newest Franchise Statute,” online: Mondaq, Canada: Franchise & Distribution @ Gowlings – November 2006  
<<http://www.mondaq.com/article.asp?articleid=44774>> (to view article, you must become a member of “mondaq” at no cost).

franchise or the payment of consideration relating to the franchise. All Acts except Ontario's exempt confidentiality and site selection agreements from the disclosure requirement; the Alberta Act also exempts fully refundable deposits.<sup>63</sup> Should franchisors in Manitoba be able to require a refundable deposit or enter into a confidentiality or site selection agreement with a franchisee before providing disclosure?<sup>64</sup>

### **i. Refundable Deposits**

Refundable deposits work in such a way that if the negotiations result in a franchise being granted by the execution of an agreement, the deposit will be credited towards the franchise fee. Otherwise, the deposit will be returned to the applicant, usually minus an administrative fee.<sup>65</sup> It is likely that the purpose of such a payment is for the franchisee to demonstrate that they are serious about purchasing a franchise and are not simply conducting a market investigation hoping to steal trade secrets from a franchisor. Initially this appears to be a good idea. However, such an arrangement exposes the franchisee to unscrupulous franchisors claiming to refund the deposit but who, in reality, will refuse to do so given the opportunity.

The Ontario Superior Court of Justice heard such cases on two separate occasions. First, in **Ali v. Triple 3 Holdings Inc.**,<sup>66</sup> and second in **Scott v. 3 for 1 Pizza & Wings (Canada) Inc.**<sup>67</sup> In Ali, the plaintiff franchisee paid a deposit before signing the Franchise Agreement. When the franchisor declined to alter the agreement to suit Mr. Ali's needs, Mr. Ali requested his deposit back and Triple 3 refused. In Scott, the plaintiff franchisee had to go to court in order to obtain a refund of his deposit, having received nothing in return.

Although these two cases are examples of a franchisee requesting the deposit back after receiving a disclosure document, they serve to demonstrate how easily a franchisor can abuse the franchisee by refusing to refund the deposit. The defendant in Scott went as far as to

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<sup>63</sup> Section 4(7) of the Alberta *Franchises Act, R.S.A. 2000, c. F-23* states that for the purposes of subsections 2(a) and 5(a), an agreement that contains only terms and conditions relating to any one or more of the following is not a franchise agreement: (a) a fully refundable deposit; (b) the keeping confidential or prohibiting the use of any information or material that may be provided to the prospective franchisee; (c) the designation of a location or territory of the prospective franchised business.

<sup>64</sup> Manitoba Law Reform Commission, *supra* note 13 at 50.

<sup>65</sup> Frank Zaid, *Franchise Law* (Toronto: Irwin Law, 2005) at 16.

<sup>66</sup> [2001] O.J. No. 5575.

<sup>67</sup> [2003] CarswellOnt 3790.

argue that Scott had contracted with another party and that, consequently, 3 for 1 did not have the deposit. If Manitoba's franchise legislation was to require a refundable deposit before a disclosure document is issued, not only will a franchisee be exposing himself to potential abuse but he also will be paying money into an enterprise he knows very little about. Considering that the purpose of such legislation is to protect franchisees and help them make an informed decision, this provision would seriously endanger that goal. Therefore, Manitoba should not allow franchisors to claim refundable deposits before issuing disclosure documents.

However, since franchisors may still be desirous of proof of a franchisee's legitimate interest, an alternative is required. After all, preparing disclosure documents and providing franchisees with other informational materials comes at a cost to franchisors. Thus, Manitoba legislation should allow franchisors to request that franchisees make a deposit, in trust, with their own lawyers as a show of faith. This deposit should not exceed 5% of the total franchise fee, up to a maximum of \$5,000, since doing otherwise would be too onerous on franchisees. In including this requirement, franchise legislation would ensure franchisors still receive assurance of a franchisee's legitimate interest while at the same time protecting the franchisee's money from unscrupulous franchisors. This deposit could then be used towards the franchise fee or as a retainer for the franchisee's legal costs.

#### **ii. Confidentiality Agreements**

The purpose behind Confidentiality Agreements is to protect franchisors. Developing a successful franchise system can only come about as a result of the expenditure of considerable time and money by the franchisor. Each element of the system, from the development of the products and services to the advertising fund and marketing program, contains valuable information proprietary to the franchisor. With so much invested in the business system, the franchisor may require that the franchisee keep the franchise system strictly confidential.<sup>68</sup> A typical confidentiality clause may look as follows:

The franchisee acknowledges that its knowledge of the operation of the Franchised Business will be derived from the information disclosed to the directors, officers, employees and agents of the Franchisee by the Franchisor pursuant to

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<sup>68</sup> Frank Zaid, *supra* note 65 at 20.

this agreement and that certain of such information, including, without limitation the contents of the Manual, is proprietary, confidential and a trade secret of the franchisor. The Franchisee agrees that it shall maintain absolute confidentiality of such information during and after the term of this agreement and that it shall ensure that such persons will not use any such information in any other business or in any manner.<sup>69</sup>

It should be noted that protecting franchise trade secrets and confidential information benefits franchisees as well as the franchisor. Franchisees would lose much of the economic value of their business if the information they rely upon to operate their franchise became publicly available such that others could easily duplicate the franchise business and then compete with actual franchisees.<sup>70</sup>

From a franchisor's perspective, requesting a franchisee to sign a confidentiality agreement before providing any disclosure is rather sensible. This is because a franchisor will want to be sure that a franchisee will not steal any secrets from the franchise, refuse to sign the franchise agreement, and then open a competing store. From a franchisee's perspective, signing a confidentiality agreement prior to receiving a disclosure document makes no difference whatsoever. There is nothing at risk. The ULCC recommends that confidentiality agreements should be able to be entered into prior to disclosure and states that a prospective franchisee would not be prejudiced in this regard.<sup>71</sup> Therefore, to protect franchisors from unscrupulous franchisees that want to steal trade secrets, Manitoba's legislation should allow franchisors to issue confidentiality agreements before providing disclosure.

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<sup>69</sup> Daniel F. So, *Canadian Franchise Law Handbook*, (Markham: LexisNexis Canada Inc., 2005) at 143.

<sup>70</sup> Mark S. VanderBroek and Christian B. Turner, "Protecting and Enforcing Franchise Trade Secrets," (Spring 2006) Vol. 25, No. 4, *Franchise Law Journal* 191 at 192.

<sup>71</sup> Uniform Law Conference of Canada, *Uniform Franchise Act with Commentary*, online: Proceedings of Annual Meetings, 2004 Regina, Commercial Law Documents <[http://www.ulcc.ca/en/poam2/CLS2004\\_Uniform\\_Franchise\\_Act\\_and\\_Commentary\\_En.pdf](http://www.ulcc.ca/en/poam2/CLS2004_Uniform_Franchise_Act_and_Commentary_En.pdf)> at 15.



If Manitoba chooses to follow a format similar to Ontario's legislation, a franchisor would be in violation of the Act by having the prospective franchisee sign a confidentiality agreement before they receive a proper disclosure document. Section 5(1)(a) of the Ontario Act requires that a disclosure document must be provided 14 days prior to the signing of any agreement. Consequently, Manitoba would have to follow Alberta, PEI and the ULCC and specifically permit such pre-disclosure confidentiality agreements by excluding confidentiality agreements from the definition of a franchise agreement.<sup>72</sup>

### iii. Site Selection Agreements

Unlike the *Arthur Wishart Act (Franchise Disclosure)*, 2000, the PEI and Alberta Acts as well as the UFA exclude site selection agreements from the definition of "franchise agreement." Accordingly, and unlike Ontario, these agreements may be entered into in advance of a disclosure document being given.<sup>73</sup> If the franchise is a turnkey operation, where the franchisor is in charge of development and selection of premises and the franchisee simply has to unlock the door to begin operating its business, no site selection agreement is needed. However, when the franchisee is partially or completely responsible for choosing and developing the location, a site selection agreement will be needed.<sup>74</sup>

A site selection agreement is a breed of commitment agreement. Under a commitment letter, the supposed franchisee's pre-opening obligation is to procure premises for the franchised business. The site selection agreement may impose certain site and lease criteria and approvals with which the franchisee must comply in order to move forward with the development of the franchise. Often, the site selection agreement requires the franchisor to review promptly and approve or reject the site.<sup>75</sup>

The ULCC recommends that an agreement which is restricted to designation of a location should be able to be entered into prior to disclosure and should therefore be exempt from disclosure. A prospective

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<sup>72</sup> Edward N. Levitt, *supra* note 51 at 20.

<sup>73</sup> Larry Weinberg, "Franchise Law e-LERT – Canadian Franchise Law – Legislative Updates," online: Cassels Brock Resources <<http://casselsbrock.com/publicationdetail.asp?aid=827>>.

<sup>74</sup> Frank Zaid, *supra* note 65 at 14.

<sup>75</sup> Kevin M. Shelley and Jonathan J. Toronto, "Preliminary Agreements: How to Avoid Unintended Contractual Obligations," (Fall 2005) Vol. 25, No. 2, *Franchise Law Journal* 47 at 53; or online: Franchise Law Journal <[http://www.abanet.org/forums/franchising/franchise\\_law\\_journal/05/franchiseljssummer2005.pdf](http://www.abanet.org/forums/franchising/franchise_law_journal/05/franchiseljssummer2005.pdf)>.

franchisee would not be prejudiced in this regard.<sup>76</sup> Consequently, section 10 of the UFA states that an agreement is not a franchise agreement or any other agreement relating to the franchise if the agreement only contains terms in respect of designating a location, site or territory for a prospective franchisee.

In theory, receiving the site selection agreement before the disclosure document could be beneficial for the franchisee. This is because rather than having to become familiar with a very large document prior to signing the Franchise Agreement, the franchisee will have more time to consider each document separately. Consequently, allowing a franchisor to issue a site selection document prior to the disclosure document will result in a franchisee being able to make a well-informed decision. In other words, having become well acquainted with both documents due to the added reading time, a franchisee will be more informed when making the decision to purchase. Thus, Manitoba's legislation should follow Alberta, PEI and the ULCC and exclude site selection documents from the definition of franchise agreements, allowing a franchisor to issue the former prior to the latter.

## **2. Exemptions**

The general policy behind the disclosure requirement is to provide prospective franchisees with information relating to the franchise, the franchise system, and the costs of operating and establishing a franchised business. There are a number of provisions in place in all regulated Canadian jurisdictions whereby franchisors may be exempt from delivering a disclosure document to a prospective franchisee or financial statements in conjunction with the production of a disclosure document.<sup>77</sup> The question facing Manitoba at the moment is whether the ability to exempt certain franchisors from the requirement to provide financial statements or to implement for other exemptions from the requirements of legislation or regulations is appropriate.<sup>78</sup>

### **a. General Exemptions from Legislation or Regulations**

Broadly speaking, general exemptions from franchise legislation and regulations exempt a party selling or renewing a franchise in certain

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<sup>76</sup> Edward N. Levitt, *supra* note 62.

<sup>77</sup> Paul D. Jones and Daniel F. So, "Houdini's Franchise Law: Exclusions and Exemptions to Disclosure in Canada," (Paper presented to the Ontario Bar Association's 6th Annual Franchising Conference: The Domino Effect, November 2006) [Toronto: OBA Continuing Legal Education, 2006] at 25.

<sup>78</sup> Manitoba Law Reform Commission, *supra* note 13 at 51.

circumstances from having to provide disclosure documents. The question facing Manitoba under this heading is whether the ability to implement exemptions from the requirements of legislation or regulations is appropriate.

Every regulated jurisdiction in Canada has implemented general exemptions. Section 5 of the Alberta *Franchises Act*,<sup>79</sup> section 5(7) of Ontario's *Arthur Wishart Act (Franchise Disclosure), 2000*, and section 5(7) of PEI's *Franchises Act* cover the authorized exemptions in each province. Since every regulated jurisdiction in Canada contains exemptions, Manitoba should not be the exception. The fact that each Act contains exemptions does not mean that a potential franchisee will be forced to purchase a franchise without sufficient information about the business. For example, section 5(7)(c) of the *Arthur Wishart Act (Franchise Disclosure), 2000* states that disclosure requirements will not be enforced in the grant of an additional franchise to an existing franchisee if that additional franchise is substantially the same as the existing franchise that the franchisee is operating and if there has been no material change since the existing franchise agreement or latest renewal or extension of the existing franchise agreement. In such a case, the franchisee would already possess all the required information to make the purchase, hence the exemption.

When drafting an exemptions section for Manitoba, the differences between Alberta and Ontario should be noted. For instance, Ontario does not have an equivalent of Alberta's section 5(1)(g). The section creates an exemption from disclosure when the sale of a right to a person to sell goods or services within or adjacent to a retail establishment as a department or division of the establishment, if the person is not required to purchase goods or services from the operator of the retail establishment is effected. More importantly, Alberta has incorporated one further exemption by allowing the Minister to exempt any class of persons or person, any sale of a franchise, or any class of sale of a franchise, or any franchise or class of franchise from any or all provisions of the Act or regulations upon becoming satisfied that to do so would not be prejudicial to the public interest.<sup>80</sup> This is an important difference because it allows the Minister to create further exemptions upon application where the occasion so warrants.

Manitoba should follow Alberta's example and adopt its exemptions section. Not only is the section more extensive but also it contains the further exemption that allows a Minister to grant an

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<sup>79</sup> R.S.A. 2000, c. F-23, s. 5.

<sup>80</sup> S.A. 1995 c. F-17.1, s. 6.

exemption where to do so *would not be prejudicial to the public interest*. In keeping with the act's purpose of aiding the franchisee to make an informed decision, an exemption will still allow the franchisee to do so while fostering expediency.

**b. Exemption from Franchisor's Obligation to Provide Financial Statements**

Financial disclosure is a very sensitive topic. Consequently, most franchisors are wary to disclose sensitive financial information in the form of financial statements required to be provided as part of a disclosure document. The general requirement to disclose financial information about the franchisor is to inform the prospective franchisee of the financial health and success of their prospective franchisor. The provisions in Alberta, PEI and Ontario providing franchisors with an exemption from disclosing financial statements were intended to provide mature, established and financial viable franchisors that have a consistent record of good relations with franchisees and who comply with the law from having to disclose financial information to prospective franchisees, or where to so exempt would not prejudice the public interest.<sup>81</sup> In order to better understand the financial document disclosure exemption, it is necessary to consider the actual provisions.

Section 11 of the *Regulations Made Under the Arthur Wishart Act (Franchise Disclosure), 2000*,<sup>82</sup> contains the tripartite test for the financial exemption. It is important to note that this is a self-declaratory process, and the onus to satisfy the tests rests on the applicant. A franchisor must thus establish that: (1) the franchisor has a net worth on a consolidated basis based on its most recent audited or review engagement financial statement of not less than \$5 million or \$1 million if it is controlled by a corporation that has a net worth of not less than \$5 million; (2) the franchisor has had at least 25 franchisees operating in Canada or in a single country other than Canada during the five year period prior to the disclosure document, or it is controlled by a corporation that satisfies this requirement; and (3) the franchisor, its associates, officers, directors, or general partners have not had any judgment, order or award made in Canada against them relating to fraud, unfair or deceptive business practices, or a law regulating franchises, including the *Arthur Wishart Act (Franchise Disclosure), 2000* in the five years prior to the date of the disclosure document.<sup>83</sup>

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<sup>81</sup> Frank Zaid, *supra* note 65 at 34-35.

<sup>82</sup> O. Reg. 581/00.

<sup>83</sup> Daniel F. So, *supra* note 69 at 112.

In contrast, Alberta has incorporated a two-pronged test that does not contain the third step from Ontario's regulations. According to section 1 of the *Franchises Act Exemption Regulation*,<sup>84</sup> a franchisor will not be required to include financial statements in a disclosure document given to a prospective franchisee if:

(a) the franchisor has a net worth on a consolidated basis according to its most recent financial statements, which have been audited or for which a review engagement report has been prepared, of not less than \$5 million or of not less than \$1 million of the franchisor is controlled by a corporation that has a net worth of no less than \$5 million;

and

(b) the franchisor has had at least 25 franchisees conducting business at all times in Canada during the 5-year period immediately preceding the date of the disclosure document, has conducted business that is the subject of the franchise continuously for no less than 5 years immediately preceding the date of the disclosure document, or is controlled by a corporation that meet the two previous requirements.

It may be argued that Alberta has not included the third requirement from Ontario's test in an attempt to restrict it to purely financial matters. In other words, as the fact that a franchisor, its associates, officers, directors or general partners have not had any judgments made against them relating to fraud, unfair or deceptive business practices or a law regulating franchises, has no relation to the franchise's past and current financial status, it should have no influence on whether an exemption with regards to financial statement should apply. After all, a franchisee will come to learn of the franchisor's previous convictions or pending charges through Schedule 1 of the *Regulations*.<sup>85</sup>

Regardless of the specific requirements behind Alberta and Ontario's exemptions, incorporating them into Manitoba's legislation is a

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<sup>84</sup> Alta. Reg. 312/2000, s. 1.

<sup>85</sup> A.R. 240/95 Sched. 1; 317/2000, s. 2.

sensible idea. Taking only the first two steps in each test in consideration, it is clear that only those franchisors who are so large and well established that very little doubt may exist as to their financial status will be exempt from delivering financial statements. This means that a franchisee will still be able to make an informed decision, knowing that no disclosure document was provided because of the franchisor's size. However, if Manitoba were to incorporate this exemption, a provision should be added allowing a franchisee to still demand financial statements. If the franchisee is required to invest a very large sum in order to acquire the franchise, s/he should be able to consider the company's financial situation by looking at a statement. Assuming that this is a very sensitive topic for the franchisor, the franchisee may be required to sign a confidentiality agreement that the financial statements will not be disclosed to anyone outside the franchise, thus successfully protecting such sensitive information. Ideally, Manitoba should introduce a liquidity test, since a franchise may have a seemingly good net-worth but be illiquid. However, doing so would make Manitoba too strict, possibly deterring incoming franchisors.

What of the third step in Ontario's test? The requirement that the franchisor, its associates, officers, directors or general partners have not had any judgments made against them relating to fraud, unfair or deceptive business practices or a law regulating franchises should be included in Manitoba's franchise legislation. Although it may not be specifically related to financial issues, legislation should require a franchisor to be as transparent as possible, especially where they have been charged or convicted of such offences.

In conclusion, Manitoba should adopt the exemption in question to allow large franchisors to refrain from disclosing sensitive financial information. Furthermore, Ontario's provision should be adopted with an addendum allowing a franchisee to request disclosure of financial documents where the franchisor has applied for an exemption. If the request is granted, the franchisor should be allowed to require the franchisee to sign a confidentiality agreement protecting all financial information.

### **3. Franchise Relationship Regulation**

The relationship between a franchisor and his franchisees has often been likened to a partnership or marriage. These analogies are valid because of the interdependence of the parties, the division of responsibilities, the collective effort for the common good and the sharing of the fruits of that effort. But like a partnership or marriage, a franchise relationship can turn sour and become a bitter experience for all

concerned.<sup>86</sup> Consequently, legislative provisions are necessary to ensure the preservation of this delicate relationship.

Until the year 2000, when Ontario introduced the *Arthur Wishart Act (Franchise Disclosure), 2000*, Alberta was the only Canadian jurisdiction to have regulated the franchise relationship. However, because the population in Alberta represents less than 10 percent of the total Canadian population, the franchise relationship throughout Canada was governed primarily by common law.<sup>87</sup> Since the year 2000, the introduction of franchise legislation in Ontario, PEI and possibly New Brunswick has increased the statutory protection of the franchise relationship.

### **a. Current Legislation, Bill 32 and the UFA**

#### **i. Alberta**

Alberta first introduced franchise relationship provisions in 1995, when it replaced the old *Franchises Act*.<sup>88</sup> The new Act adopted two relationship provisions, addressing the duty of fair dealing and the franchisee's right to associate. Section 7 of the Act states that every franchise agreement imposes on each party a duty of fair dealing in its performance and enforcement. Section 8(1) of the Act states that a franchisor or its associate must not prohibit or restrict a franchisee from forming an organization of franchisees or from associating with other franchisees in any organization of franchisees. Furthermore, a franchisor or its associate must not directly or indirectly penalize a franchisee for associating with others.

The common law continues to play an important role in presiding over franchise relationships. In **Thompson v. Cinnaroll Bakeries Ltd.**,<sup>89</sup> the defendant, who held an exclusive franchise for Cinnabon bakeries in Western Canada, allowed the agreement to expire and opened up a new store at its own cost. The plaintiff franchisor claimed breach of contract by the defendant for failing to renew the agreement. The Alberta Court of Queen's Bench decided that, according to the franchise agreement, the defendant would be bound to renew should the renewal be offered on the same terms as before. Where reasonable changes are proposed, it would

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<sup>86</sup> Edward N. Levitt, "The Franchisor/Franchisee Relationship," online: Gowlings Resource Centre

<<http://www.gowlings.com/resources/publications.asp?pubid=1134>>.

<sup>87</sup> Allan D.J. Dick and Markus Cohen, "The Duty of Good Faith and Fair Dealing in Canada," (Fall 2004) Vol. 24, No. 2 *Franchise Law Journal* 89 at 89.

<sup>88</sup> R.S.A. 1980, Ch. F-17 (repealed).

<sup>89</sup> [2002] A.B.Q.B. 1112.

be unreasonable for the defendant to refuse to renew the agreement. However, since the defendant was not acting unreasonably by refusing to renew due to significant changes introduced by the franchisor, there was no breach of contract.

## ii. Ontario

Ontario was the second Canadian jurisdiction to regulate franchise relationships, doing so in 2000. Section 3(1) of the *Arthur Wishart Act (Franchise Disclosure), 2000*, emulates Alberta's duty of fair dealing. However, the Ontario Act is more extensive than the Alberta Act since it provides that:

A party to a franchise agreement has a right of action for damages against another party to the franchise agreement who breaches the duty of fair dealing in the performance or enforcement of the franchise agreement.<sup>90</sup>

The Ontario Act also establishes that, for the purposes of the fair dealing section, the duty of fair dealing includes the duty to act in good faith in accordance with reasonable commercial standards.<sup>91</sup> The commercial reasonableness standard of good faith has received a fair amount of criticism. Some suggest that enforcement of a contract should be about enforcement of the objective intention of the parties and not a wholesale enforcement of norms and concepts external to the contract. However, including reasonable commercial standards in the definition of fair dealing provides the concept of fair dealing with the contextual clarification it requires and is consistent with the standard of good faith already applied in the Canadian common law.<sup>92</sup>

The right to associate is also addressed by the Ontario Act, once again, emulating Alberta. However, Ontario has two additional sections. First, section 4(4) states that any provision in a franchise agreement or other agreement relating to a franchise which purports to interfere with, prohibit or restrict a franchisee from exercising their right of association is void. Second, section 4(5) grants the franchisee a right of action for damages if a franchisor or franchisor's associate contravenes the

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<sup>90</sup> *Arthur Wishart Act (Franchise Disclosure) 2000*, 2000, c. 3, s. 3(2).

<sup>91</sup> *Ibid.* at s. 3(3).

<sup>92</sup> Edward N. Levitt and Deborah E. Palter, "Ontario Passes Franchise Disclosure Act," online: Canadian Franchise Association, Government Relations <[http://www.cfa.ca/page.aspx?url=Legal\\_ontario.html](http://www.cfa.ca/page.aspx?url=Legal_ontario.html)>.



association section. The common law has potentially expanded the scope of the duty of good faith and fair dealing. In **530888 Ontario Ltd. v. Sobeys Inc.**,<sup>93</sup> the Ontario Superior Court of Justice stated that parties to a contract are expected to fulfill their contractual obligations honestly and in good faith. Furthermore, the court asserted that commercial relationships are not immune from the imposition of fiduciary duties. Justice Lax stated:

The concept of power dependency is fact driven. Fiduciary duties will be imposed in appropriate circumstances to govern the manner in which discretion is exercised.

This decision is of particular importance in that it distinguishes **Jirna Ltd. v. Mister Donut of Canada Ltd.**,<sup>94</sup> a landmark Supreme Court of Canada ruling stating that the franchise relationship does not give rise to fiduciary duties. The current state of the common law is that a franchisor may be a fiduciary but only where the facts so warrant.

### iii. PEI

Prince Edward Island boasts the newest franchise legislation in Canada, with the *Franchises Act*<sup>95</sup> coming into force on July 1, 2006. Like the Ontario Act and Alberta Act, the PEI Act has enacted relationship provisions enforcing the duty of fair dealing and the right of franchisees to associate and organize.<sup>96</sup> PEI has followed Ontario's fair dealing provisions closely. However, section 3(1) of the PEI Act extends the duty of fair dealing by adding "including the exercise of a right under the agreement." Regardless of any differences, for all provinces, the duty of fair dealing is a mutual obligation between franchisors and franchisees, whereas the right to associate is designated to protect the interests of franchisees.<sup>97</sup> Furthermore, PEI struck the phrase "in the performance or enforcement of the franchise agreement" from Ontario's right of action section under fair dealing, so that the section reads:

A party to the franchise agreement has a right of action for damages against another

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<sup>93</sup> [2001] CarswellOnt 240.

<sup>94</sup> [1975] 1 S.C.R. 2.

<sup>95</sup> R.S.P.E.I. 1988, Cap. F-14.1.

<sup>96</sup> Lawrence Weinberg and Jayne Westlake, "Canada's East Coast Provinces Pursue Interest in Franchise Law," online: Franchise UPDATE Archive, Past Articles <<http://www.franchiseupdate.com/articles/193/>>.

<sup>97</sup> *Ibid.*

party to the franchise agreement who breaches the duty of fair dealing.<sup>98</sup>

In contrast to the procedure followed in enacting fair dealing provisions, PEI adopted Ontario's association provision verbatim.

#### **iv. New Brunswick**

The Provincial Legislature of the Province of New Brunswick proposed Bill 32, entitled *Franchises Act*, at a first reading on February 23, 2007. If passed, the Bill will impose on franchisors and franchisees a duty of good faith and fair dealing. The legislation will also protect the right of franchisees to associate.<sup>99</sup> Although New Brunswick altered the order, it followed PEI's fair dealing provision, extending the performance and enforcement of the franchise agreement to include the exercises of a right under the agreement. Once again, Ontario's association provisions were adopted verbatim.

#### **v. ULCC**

The *Uniform Franchises Act* contains the same fair dealing provision as PEI. The expansion of the section from its Ontario counterpart means that the duty of fair dealing will not only apply during the performance and enforcement of the agreement but also in the exercise of a right under it. The ULCC argues that the addition of the words "in the exercise of a right" is necessary because the duty of fair dealing incorporating the duty of good faith and commercial reasonableness standards in the Ontario Act does not extend to express contractual provisions granting the franchisor discretionary authority over rights to be exercised during the term of the contract that may be carried out without regard to fair dealing.<sup>100</sup> When drafting its model act, the ULCC chose to follow Ontario's association provisions rather than Alberta's. The reason for this decision is that the Alberta Act has been drafted in the negative, that is, that a franchisor or its associate may not prohibit or restrict a franchise from forming an organization while the Ontario Act has been drafted in the affirmative, where a "franchisee may associate with other franchisees."<sup>101</sup>

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<sup>98</sup> R.S.P.E.I. 1988, Cap. F-14.1, s. 3(2).

<sup>99</sup> Richard Leblanc, "New Brunswick Reintroduces Franchise Legislation," *FranNews* (Spring 2007), online: Miller Thomson LLP, Publications, Newsletters <[http://www.millerthomson.ca/mtweb.nsf/web\\_files/mtte72nkn8/\\$File/Franchise%20Newsletter%20April\\_07\\_v2\\_cropped.pdf?openelement](http://www.millerthomson.ca/mtweb.nsf/web_files/mtte72nkn8/$File/Franchise%20Newsletter%20April_07_v2_cropped.pdf?openelement)> at 1.

<sup>100</sup> Uniform Law Conference of Canada, *supra* note 71 at 9.

<sup>101</sup> *Ibid.*

**b. Recommendation for Manitoba**

The question at hand is what relationship provisions Manitoba ought to adopt. The options range from Alberta's narrower provisions to PEI, New Brunswick and the ULCC's wider provisions; Ontario stands in the middle of the spectrum. All relationship provisions pertain to the duty of good faith and the right of franchisees to associate.

With regard to the duty of fair dealing, Manitoba ought to adopt the widest provisions. Since these extend the duty from a pre-contractual obligation to apply to the exercise of a right under the agreement, franchisees will be protected throughout their entire relationship with the franchisor. Conversely, franchisors will be protected from franchisees since the duty is reciprocal. It is necessary to note that the common law assumes that parties to a contract are equal and capable of looking out for their respective interests. Since this is not the reality in a franchise relationship, due in part to the power imbalance between a franchisor and franchisee, legislation is needed to compensate for this shortcoming.<sup>102</sup> Thus, the duty of good faith and fair dealing must be included in Manitoba's franchise legislation.

A right of action should also be granted to ensure that parties abide by the requirements or risk facing legal action. Lastly, the expansion of the duty of fair dealing to include reasonable commercial standards ought to be adopted as well. As stated earlier, including reasonable commercial standards in the definition of fair dealing provides the concept of fair dealing with the contextual clarification it requires and is consistent with the standard of good faith already applied in the Canadian common law.<sup>103</sup>

Manitoba's franchise legislation should also grant franchisees the right to associate, emulating the Ontario and PEI Act as well as the New Brunswick Bill. Since associations may be beneficial to both franchisors and franchisees, a franchisee's right to associate or join an organization should be protected. As Edward N. Levitt stated:

The association can assist in dispute resolutions between the franchisor and franchisees, provide a useful feedback mechanism for all sorts of issues affecting the system, assist the franchisor in dealing with franchisees who operate poorly or

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<sup>102</sup> Daniel F. So, *supra* note 69 at 212.

<sup>103</sup> Edward N. Levitt and Deborah E. Palter, *supra* note 92.

contrary to the interest of everyone in the system, raise the level of commitment of all franchisees and assist in the introduction of new products and services into the system.<sup>104</sup>

### **c. Additional Franchise Relationship Issues**

Current franchise relationship legislation in Canada only addresses a small portion of relationship issues. Although extending the duty of fair dealing to include the performance of the contract may provide more protection to franchise parties, several areas remain where no protection is issued. These include contract termination, renewal of contract, transfers and sale of a franchise by a franchisee.

#### **i. Contract Termination**

The issue under this heading is whether Manitoba ought to introduce termination provisions limiting a franchisor's right to terminate a contract only to instances where there is good cause. However, prior to discussing whether some form of legislation should be adopted, it is necessary to consider whether Manitoba is in need of statutory termination provisions or if the common law has addressed the issue sufficiently so that no legislation is needed.

Manitoba's Court of Queen's Bench has already addressed the issue of termination in two instances. In **John Deere Ltd. v. G.A.E.L. Inc. (1994)**,<sup>105</sup> the Court stated that reasonable notice is required to terminate an agreement and that termination rights must not be exercised on the basis of questionable and flimsy grounds. Furthermore, Monnin J. found that the termination clause in the dealer agreement must have "reasonableness" read into it. In **Halligan v. Liberty Tax Service Inc.**,<sup>106</sup> the Court found that the franchisor's attempt to terminate the contract was malicious and, thus, a breach of the duty of good faith. Overall, Manitoba's common law forces a franchisor to give reasonable notice upon termination, to have reasonable grounds to do so and to act in good faith.

Although Manitoba's Court of Queen's Bench has established certain requirements upon termination, several questions that arise

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<sup>104</sup> Edward N. Levitt, "Franchisee Associations," online: Gowlings Resource Centre, <<http://www.gowlings.com/resources/publications.asp?Pubid=1137>>.

<sup>105</sup> 96 Man. R. (2d) 295.

<sup>106</sup> [2006] 8 W.W.R. 97, 202 Man. R. (2d) 268.

upon termination remain unanswered. First, there is no explanation as to what reasonable grounds for termination may be and, second, there is nothing specific with regard to providing notice. Should a franchisor allow the franchisee to cure the default? How much time should the franchisee be allotted to cure the default? Should there be exemptions to providing a franchisee with the right to cure? Since Manitoba's common law does not address the issue of franchise termination, a statutory provision should be introduced.

Iowa's legislation should be considered as a model since it is recognized as being the most comprehensive.<sup>107</sup> Iowa's termination provisions begin by stating:

Except as otherwise provided by this chapter, a franchisor shall not terminate a franchise prior to the expiration of its terms except for good cause. For the purposes of this section, "good cause" is cause based upon a legitimate business reason.<sup>108</sup>

The Iowa Act further states that "good cause" includes the failure of a franchisee to comply with any material lawful requirement of the franchise agreement, provided that the termination by the franchisor is not arbitrary or capricious when compared to the actions of the franchisor in other similar circumstances.<sup>109</sup> The Act provides the franchisee with the opportunity to cure the alleged default after receiving written notice stating the basis for the proposed termination. The Act also includes an exemption for termination without providing the franchisee the opportunity to cure, such as when the franchisee or the business to which the franchise relates is declared bankrupt.<sup>110</sup>

The length of time a franchisor will grant a franchisee to cure an alleged default is an essential matter pertaining to termination of a franchise agreement. Iowa's legislation states that after service of notice, the franchisee shall have a reasonable period of time to cure the default, which in no event shall be less than 30 days and no more than 90 days.<sup>111</sup> In contrast, Australia's *Trade Practices Act 1974* states that the franchisor must allow the franchisee a reasonable time to remedy the breach. A "reasonable time" is however limited by the subsequent section

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<sup>107</sup> Manitoba Law Reform Commission, *supra* note 13 at 52.

<sup>108</sup> 1992 *Franchises Act*, Iowa Code § 523H.7.1.

<sup>109</sup> *Ibid.*

<sup>110</sup> *Ibid.* at §523H.7.2 and §523H.7.3.

<sup>111</sup> *Ibid.* at §523H.7.2.

to no more than 30 days.<sup>112</sup> Similarly, the *California Franchise Relations Act* requires that a franchisee's reasonable opportunity to cure the failure should not exceed 30 days.<sup>113</sup>

Manitoba should follow Australia and California's example in setting a 30-day limit. Iowa's limit of 90 days appears to be an excessive time in which to require a franchisor to endure a defaulting franchisee. Adopting a shorter limit will induce a franchisee to cure the default faster, to the franchise's benefit, and shall have no detrimental effect on the franchisee. In addition, Manitoba could introduce an exception to this limit when the parties initially agree to a longer, but never shorter, period through the franchise agreement. To provide a further incentive for a franchisee to comply, the termination clause in a franchise agreement should be statutorily required to include a liquidated damages section, whereby a franchisor establishes what a franchisee will have to pay in compensation in case of failure to remedy the default. Non-compliance with the request to cure the default should render the contract void, allowing the franchisor to sell the franchise to other potential franchisees.

It is important to note that Iowa's legislation covers the termination by a franchisor in instances where the franchisee is in default. What happens when the franchisor simply wants to terminate the contract for no particular reason? Manitoba should introduce a section addressing this issue as well. In doing so, Manitoba's franchise legislation should allow a franchisor wishing to terminate the franchise agreement without good cause to do so, only after paying a penalty. Upon termination, a franchisor would have to pay the *pro rata* value of the franchise plus a portion of the cost of the business as assessed by an independent business advisor. For instance, if the franchisee had originally paid a \$250,000 franchise fee for a five year period and the contract is cancelled on year four, then the franchisor should pay the franchisee \$50,000, which is the amount the franchisee had paid per year under the agreement. Introducing such a clause would not only ensure that franchisors exercise caution in terminating agreements, but also ensure that franchisees who had counted on the franchise's income still manage to receive it.

By adopting such legislation, Manitoba would become the first Canadian jurisdiction to protect franchisees from contract termination

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<sup>112</sup> Australia, Trade Practices (Industry Codes – Franchising) Regulations 1998, *supra* note 48 at ss. 21(2)(c) and 21(3).

<sup>113</sup> Cal. Bus. & Prof. Code §20020.

while providing franchisors with a guideline as to what steps to take in order to terminate a franchise contract adequately.

## ii. Renewal of Contract

The franchise agreement may include a right of renewal for the franchisee, which right is exercisable only if the franchisee has complied with certain conditions. Typical conditions precedent to the exercise of a renewal option are that the franchisee (i) is in good standing under the franchise agreement and all other agreements with the franchisor; (ii) provides to the franchisor written notice of its intent to renew; (iii) agrees to execute the then current standard franchise agreement used by the franchisor for the grant of new franchises; and (iv) agrees to pay the franchisor a renewal fee.<sup>114</sup> In the absence of renewal, the franchisor will be free to retain, re-license, close, or re-organize the business for its own account.<sup>115</sup>

Since Manitoba courts have yet to hear a franchise renewal case, it is necessary to look to other jurisdictions to determine if the common law already provides sufficient protection upon renewal. In **Sultani v. Blenz The Canadian Coffee Co.**,<sup>116</sup> the British Columbia Supreme Court held that a duty of fair dealing imposed on a franchisor does not go so far as to compel a party to renew an expiring relationship when it is not commercially reasonable to do so, and where there is no express right of renewal contained in the agreement. In **Thompson v. Cinnaroll Bakeries Ltd.**,<sup>117</sup> the Alberta Court of Queen's Bench held that, according to the franchise agreement, the franchisee was bound to renew the contract unless significant changes had been made to the original contract, such as an increase in royalty payments and loss of exclusivity in a specific market.

The precedent established by renewal cases fails to adequately address the renewal of franchise agreements. It fails to deal with situations where oral promises to renew are not upheld as well as instances where the franchise agreement does not mention the option of renewal, where franchise parties are not bound to exercise good faith and fair dealing. It is clear that legislation is necessary to complement the

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<sup>114</sup> Frank Zaid, *supra* note 65 at 14.

<sup>115</sup> Paul J. Bates and R. David House, "Canadian Franchise Disputes," (Paper presented to the 6<sup>th</sup> Annual Franchise Conference: The Domino Effect, November 2006) [Toronto: Ontario Bar Association Continuing Legal Education] at 10.

<sup>116</sup> [2005] B.C.J. No. 846.

<sup>117</sup> [2002] ABQB 1112.

common law, forcing parties to exercise their best business behavior when dealing with each other upon renewal.

Having established that Manitoba is in need of renewal provisions, one should consider how other jurisdictions with franchise legislation address the matter. Since none of the Canadian provinces with franchise regulation include renewal clauses, one must look abroad. The United States, having implemented different renewal provisions in several of its states, provides the most complete example.

California boasts the most extensive non-renewal clause, found in the *California Franchise Relations Act*. Article 4, Section 20025 of the Act states that no franchisor may fail to renew a franchise agreement unless he provides the franchisee at least 180 days prior to written notice of its intention not to renew. Furthermore, the franchisor must allow the franchisee during the 180-day period to sell his business to a purchaser meeting the franchisor's requirements for granting a new franchise. A franchisor may refuse renewal where he withdraws from distributing his products or services through franchises in the geographic market served by the franchisee.<sup>118</sup> The following provisions, however, restrict this section:

- (1) Upon expiration of the franchise, the franchisor agrees not to seek to enforce any covenant of the non-renewed franchisee not to compete with the franchisor or franchisees of the franchisor; and
- (2) The failure to renew is not for the purpose of converting the business conducted by the franchisee pursuant to the franchise agreement to operation by employees or agents of the franchisor for such franchisor's own account; and
- (3) Where the franchisor determines to sell, transfer or assign its interests in a marketing premises occupied by a franchisee whose franchise agreement is not renewed pursuant to this paragraph:
  - (A) The franchisor, during the 180-day period after giving notice offers such franchisee a right of first refusal of at least 30 days' duration of a bona fide offer, made by another

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<sup>118</sup> Cal. Bus. & Prof. Code §20025.



to purchase such franchisor's interest in such premises; or  
(B) In the case of the sale, transfer, or assignment to another person of the franchisor's interest in one or more other controlled marketing premises, such other person in good faith offers the franchisee a franchise on substantially the same terms and conditions currently being offered by such other person to other franchisees.<sup>119</sup>

Lastly, in addition to the 180-day notice, the Act allows for non-renewal when the franchisor and franchisee fail to agree to changes or additions to the terms and conditions of the franchise agreement, if such changes or additions would result in renewal of the franchise agreement on substantially the same terms and conditions on which the franchisor is then customarily granting original franchises. In such instances, the franchisor may give the franchisee written notice of a date which is at least 30 days from the date of such notice, on or before which a proposed written agreement of the terms and conditions of the renewal franchise shall be accepted in writing by the franchisee. Such notice, which given no less than 180 days before the end of the franchise term, may state that in the event of failure of such acceptance by the franchisee, the notice shall be deemed a notice of intention not to renew at the end of the franchise term.<sup>120</sup>

Under the *Illinois Franchise Disclosure Act of 1987*, it is deemed a violation of the Act for a franchisor to refuse to renew a franchise of a franchised business without compensating the franchisee either by repurchase or by other means for the diminution in the value of the franchised business caused by the expiration of the franchise. This shall be so where (a) the franchisee is barred by the franchise agreement (or by the refusal of the franchisor at least six months prior to the expiration date of the franchise to waive any portion of the franchise agreement which prohibits the franchisee) from continuing to conduct substantially the same business under another trademark, servicemark, trade name or commercial symbol in the same area subsequent to the expiration of the franchise; or (b) the franchisee has not been sent notice of the

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<sup>119</sup> *Ibid.* at §20025(e).

<sup>120</sup> *Ibid.* at §20025(f).

franchisor's intent not to renew the franchise at least six months prior to the expiration date or any extension thereof of the franchise.<sup>121</sup>

Iowa's 1992 *Franchises Act* establishes that a franchisor shall not refuse to renew a franchise unless both of the following apply: (a) the franchisee has been notified of the franchisor's intent not to renew at least six months prior to the expiration date or any extension of the franchise agreement; or (b) any of the following circumstances exist:

- (1) Good cause exists, provided that the refusal of the franchisor to renew is not arbitrary or capricious [good cause means based on legitimate business reasons];
- (2) The franchisor and franchisee agree not to renew the franchise;
- (3) The franchisor completely withdraws from directly or indirectly distributing its products or services in the geographic market served by the franchisee, provided that upon the expiration of the franchise, the franchisor agrees not to seek to enforce any covenant of the non-renewed franchisee not to compete with the franchisor or franchisees of the franchisor.<sup>122</sup>

Moreover, as a condition of renewal of the franchise, a franchise agreement may require that the franchisee meet the then current requirements for franchises and that the franchisee execute a new agreement incorporating the then current terms and fees for new franchises.<sup>123</sup>

In deciding what renewal provisions Manitoba should adopt, it is important to remember that California contains the most complete renewal regulation. In doing so, it provides sufficient protection to franchisees facing the prospect of renewing a franchise agreement. However, if Manitoba were to adopt this provision, a few additions should be made. Manitoba's legislation should mimic Iowa and demand non-renewal only where good cause exists. This will ensure that franchisors will not capriciously refuse to renew franchise agreements. Moreover, the provision allowing a franchisor the right of non-renewal upon

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<sup>121</sup> Ill. Comp. Stat. §705/20.

<sup>122</sup> Iowa Code §523H.8.1.

<sup>123</sup> *Ibid.* at §523.H.8.2.

withdrawing from distributing its products in a certain area should be qualified by a provision forbidding the franchisor from re-entering the same area for a reasonable time. This time may range from six months to one year.

Neither the common law nor current legislation deal with situations where a franchisee wishes to renew the agreement but at a different location. This may occur in situations where the franchisee believes in the franchise, but the location has proven unfavorable. Manitoba legislation should address such situations by allowing franchisees the right to renew the agreement in such instances. However, this right should be limited to a certain distance from the original location. Doing so will allow the franchisor to expand the franchise while still allowing current franchisees to run successful operations.

In conclusion, Manitoba should include a renewal section for the following reasons. First, granting the franchisee a six-month notice period allows him/her the opportunity to make post-franchise arrangements. Second, if the parties agree not to renew, the franchise agreement should be allowed to expire. Third, if the franchisor is withdrawing operations from a particular area, he should not be forced to stay by a franchisee, when the former has no desire to do so. However, the franchisor should be required to compensate the franchisee for the loss suffered through the denial to renew. Thus, Manitoba should include a renewal provision demanding six months notice of non-renewal, as well as allowing for non-renewal when it is mutually agreed upon and when the franchisor is withdrawing from the particular service area.

### **iii. Transfers**

The franchisee will typically be restricted in its ability to transfer its rights and obligations because the franchisor's grant of rights is based on factors that are personal to the franchisee. The franchisee's ability to secure a mortgage or encumber, transfer or assign its rights and obligations under the franchise agreement will usually be subject to having obtained the franchisor's prior consent.<sup>124</sup> The issue at hand concerns whether Manitoba should adopt transfers provisions regulating the transfer of a franchise by the franchisee to a transferee.

Introducing legislation may be useful to prevent franchisors from refusing franchisees the ability to transfer the franchise by rejecting all possible candidates. However, since terms of transfer are often included

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<sup>124</sup> Frank Zaid, *supra* note 65 at 19.

in franchise agreements, the duty of fair dealing will require the franchisor to act in good faith and in accordance with reasonable commercial standards when considering the possibility of a transfer. Therefore, a franchisee will be protected if the franchisor unreasonably rejects all potential transferees. As such, there is no reason to include a provision requiring that a franchisor not act capriciously in assessing a transfer when the duty of fair dealing already imposes such a duty.

Although Iowa boasts an extensive transfer provision, detailing the process in full, it lacks the extensive duty of good faith demanding such a duty in the exercise of rights under the agreement. Thus, whereas Iowa needs transfer provisions because of the limited duty of good faith, once it adopts the more extensive duty, Manitoba will not. Consequently, Manitoba should not adopt transfer provisions.

#### **iv. Sale of Franchise by Franchisee**

The issue under this heading arises out of the following series of events. Typically, if a franchisee sells his franchise and assigns that agreement and/or sublease to the purchaser, the original franchisee remains liable for all obligations contained in the agreements. This is a typical provision of commercial leases. However, some agreements contain further obligations by providing that if the purchaser subsequently renews the agreements for another term, the original franchisee continues to be liable for all obligations of the purchaser under the renewed agreements, despite having had no input into their terms. It was suggested to the Manitoba Law Reform Commission that franchise legislation provide that, in this situation, the obligations of the franchisee do not extend beyond the terms of the original agreements and any renewals signed by that franchisee.<sup>125</sup>

In order to understand this issue better, it is necessary to consider the steps involved in a transfer of a franchise or sublease. Usually, if a franchisee sells his franchise, the franchisor will make the final decision with regard to the new party's suitability. If the franchisor does not approve of a potential franchisee, it will not be sold. Once sold, the new franchisee will often be required to complete training and pay a transfer fee.<sup>126</sup>

Forcing a former franchisee to remain liable under a contract they are not a party to is counterintuitive. Since the franchisor has approved of the new franchisee, and the former franchisee has had no part in

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<sup>125</sup> Manitoba Law Reform Commission, *supra* note 13 at 53.

<sup>126</sup> Frank Zaid, *supra* note 65 at 19.

drafting the new agreement, there is no reason why the former franchisee should remain attached to a subsequent contract. Thus, Manitoba should correct this unfair practice. In doing so, the following requirements ought to be included in a provision: (1) the franchisor must approve of the incoming franchisee, only rejecting potential franchisees with good cause; (2) upon transfer of a franchise, the incoming franchisee should receive all adequate disclosure documents and training; (3) the section in a subsequent contract that aims to attach liability to a former franchisee shall be deemed null and void.

Including such a section in Manitoba's franchise legislation would achieve several goals. First, the franchisor will be able to ensure that the proposed transferee meets the standards of the franchisor for new franchisees to preserve the goodwill and image of the entire franchise system.<sup>127</sup> Second, the incoming party will be in the same position and possess the same knowledge as the outgoing party. Last, the former franchisee will not be held liable under the new contract, upon approval of the new franchisee by the franchisor.

#### **4. Franchise Regulatory Body**

The latest possible development to franchise legislation in Ontario has emerged in the same context as did the idea to incorporate franchise legislation. As was the case in the 1990s, where media attention to **887574 Ontario Inc. v. Pizza Pizza Ltd.**<sup>128</sup> drew the public's focus to the need for franchise legislation, a new series of cases is currently directing Ontario's franchise community to consider introducing franchise regulators. The Toronto Star has recently focused on the **3 for 1 Pizza & Wings** litigation as the basis for proposing the appointment of some kind of franchise regulator for the province.<sup>129</sup> The question facing Manitoba is the same. In introducing franchise legislation, should Manitoba implement a franchise regulatory body?

Although a regulatory office could be structured in a number of ways,<sup>130</sup> its functions would not vary. A regulator would review the quality of disclosure given to franchisees, provide an inexpensive system to resolve disputes, rules to govern contractual relationships and

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<sup>127</sup> *Ibid.* at 190.

<sup>128</sup> 23 B.L.R. (2d) 239, 23 C.P.C. (3d) 323.

<sup>129</sup> Peter Macrae Dillon, "Ontario Franchise Developments in 2005: Welcome to the Tween Years," (Paper Presented to The Six Minute Business Lawyer, The Law Society of Upper Canada, June 2006), online: Siskinds Resources, Articles of Interest <<http://www.franchiselaw.ca/pdf/6MBLArt.pdf>> at 1.

<sup>130</sup> Manitoba Law Reform Commission, *supra* note 13 at 54.

penalties for breaking franchise law.<sup>131</sup> Ben Hanuka, chairman of the joint subcommittee on franchising for the Ontario Bar Association, supports the introduction of a regulatory body. He argues that some franchisors do not give out proper disclosure, and franchisees who have already invested a life's savings are having to spend a lot of money to enforce their rights under franchise law. He further states:

[W]e should upgrade the teeth of the statute, and bring in a regulatory body to deal with the situation where there is an utter breach of providing a disclosure document.[...] People should not be forced to locate a franchise lawyer and litigate this, but should have the benefit of a regulatory body.<sup>132</sup>

Such a tribunal would save franchisees millions of dollars in legal fees,<sup>133</sup> allowing them to pursue their rights even after being abused by unscrupulous franchisors. A regulator should not only go after rogue franchisors, and require them to post a bond to compensate potential victims, and ensure access to justice, but also protect compliant franchisors from rogue franchisees.<sup>134</sup> Such a body would not be unique to Canada, as the United States has already implemented it through the Federal Trade Commission.

The United States Federal Trade Commission (FTC), a federal agency with power to regulate interstate commerce, investigate business activities and issue enforcement orders, regulates federal franchise law in the United States.<sup>135</sup> The FTC may commence an enforcement action against a franchisor if an investigation determines that the franchisor has not complied with the FTC Rule. The enforcement action sought or commenced by the FTC can either be administrative, wherein the FTC may negotiate an order or a consent decree in which the franchisor will be enjoined from certain actions, or the enforcement action may be judicial, wherein the FTC can commence a lawsuit against the franchisor for their breach or non-compliance, in a court of law. Penalties for noncompliance are serious and may include the impounding of company

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<sup>131</sup> James Daw, "Regulator Could Help Franchise Feuds: Province Awaiting Report from Committee," *The Toronto Star*, (16 March 2006), online: Toronto Star Online

<<http://www.anthonysfranchiseinformation.com/Star16March2006.htm>>.

<sup>132</sup> *Ibid.*

<sup>133</sup> *Ibid.*

<sup>134</sup> *Ibid.*

<sup>135</sup> Daniel F. So, *supra* note 69 at 86.

assets, cease and desist orders, injunctions, and mandated rescission or restitution for injured franchisees.<sup>136</sup>

Complementing the FTC, all states have incorporated, in one form or another, consumer fraud or deceptive trade practice acts, commonly referred to as “Little FTC Acts.” These little FTC Acts independently create a private cause of action, wherein a violation of the FTC Act will give rise to an independent cause of action in state law.<sup>137</sup> If Manitoba chooses to instate a regulatory body, the FTC model would certainly be one to follow. Since franchisors are not required to register with the FTC and the FTC does not review or approve of the initial disclosure documents,<sup>138</sup> the regulatory body would not play an invasive or cumbersome role in the purchase process. Furthermore, franchisors coming to Manitoba from the United States, already accustomed to such a system, would not see it as a deterrent from establishing franchises in the province.

Although implementing a regulatory body would give more “teeth” to any franchise legislation, several lawyers, primarily those representing franchisors, oppose such a change. Mr. Joseph Adler, an Ontario based lawyer, argues that such cumbersome laws will only dissuade honest franchisors from conducting business in that province and increase the cost of doing business for franchisors and franchisees.<sup>139</sup> Mr. Dillon, who also opposes such a body, blames the amount of media attention the 3 for 1 Pizza cases have received. He states:

When one considers the number of franchises operating in the province [of Ontario] at any time, it should not come as a surprise that a certain number of systems will operate below the accepted community standard in the enforcement and performance of their franchise rights and obligations.<sup>140</sup>

Mr. Dillon argues that instead of introducing a regulator, it should be franchisees’ responsibility to inform themselves and become acquainted with all disclosure documents prior to purchasing a

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<sup>136</sup> *Ibid.* at 94.

<sup>137</sup> *Ibid.*

<sup>138</sup> Manitoba Law Reform Commission, *supra* note 13 at 55.

<sup>139</sup> James Daw, *supra* note 131.

<sup>140</sup> Peter M. Dillon, *supra* note 129.

franchise, in order to avoid being abused.<sup>141</sup> A franchisee may become informed by using the large variety of resources made available by the CFA at <<http://www.cfa.ca/Page.aspx?URL=EventsEducation.html>>, the Ministry of Government Services web site at <[http://www.gov.on.ca/MGS/en/Home/STEL01\\_039054.html](http://www.gov.on.ca/MGS/en/Home/STEL01_039054.html)> or a number of franchise magazines and publications that would empower a franchise prospect to avoid many of the situations in which these people find themselves. After all, an individual must be expected to take some responsibility for his own welfare. Mr. Dillon then adds that the direct costs of administering such a regime, and the indirect cost to the industry sector as a whole of being subject to further regulation are incalculable. He closes by pointing out that Alberta abandoned its regulatory system after 24 years in favour of a presale disclosure regime.<sup>142</sup> At this point it is important to note that in 1992 Manitoba's Legislature refused to adopt franchise legislation based on Alberta's old model.

Last, Richard Cunningham, president of the CFA in 2006, opposes the establishment of such a body on the grounds that there is no need for regulators. Instead, he suggests that franchisees should inform themselves properly or consult specialists in franchise law before entering into a deal.<sup>143</sup> Consequently, the CFA offers workshops to its members, such as the "Franchise Excellence Series: Franchisee Training Program," hoping to educate franchisees entering or already in the business.<sup>144</sup>

The first matter to be decided is not what type of a regulatory body Manitoba needs, but if it needs one. First, Manitoba cannot follow Ontario's argument for adopting such a body because the same problems have not arisen in the former due to its smaller size. Whereas in Ontario several franchisees have suffered at the hands of 3 for 1 Pizza & Wings, there has only been one such case in Manitoba.<sup>145</sup> Therefore, if there is a need for a regulator in Manitoba, it is certainly not as imminent as in Ontario.

Second, Manitoba has not had the chance to determine what effect franchise legislation will have on the franchise community. Given

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<sup>141</sup> *Ibid.* at 2.

<sup>142</sup> *Ibid.*

<sup>143</sup> James Daw, *supra* note 131.

<sup>144</sup> Canadian Franchise Association, "Upcoming Events by Region," online: Already in Franchising, Events Education <<http://www.cfa.ca/Page.aspx?URL=EventsEducation.html>>.

<sup>145</sup> Please refer to the following articles: Alexandra Paul, *supra* note 11; Paul Turenne, *supra* note 11.



its unique size, perhaps the issue of improper disclosure will also be in a relatively small scale and thus be solved more easily than in Ontario. It may be wise to wait until after franchise legislation is introduced to assess the true need of a regulator in Manitoba. Thus, the necessity for a regulator has yet to arise in Manitoba.

Although Manitoba may not need a regulator, it does not mean that the situation should be ignored until so much abuse takes place that one is needed. To avoid such a situation, the provincial government may want to prepare an instructional pamphlet directing franchisees to different resources they can employ to become better informed prior to purchasing a franchise. This would be very similar to the CFA's approach of providing its members with the opportunity to educate themselves. It would then become a franchisor's responsibility to attach the pamphlet to the disclosure documents. In doing so, Manitoba would be following the advice of those who oppose the introduction of a regulatory body while still leaving the possibility of introducing one if need be.

Overall, it is too premature for Manitoba to adopt a regulatory body to overlook franchise disclosure. Instead, it should be the Province's aim to educate franchisees to make well-informed decisions, allowing them to detect franchisors whose intentions may be ill-conceived.

## **5. Alternative Dispute Resolution**

In the franchise industry in particular, the use of ADR is growing in marked popularity. From a franchisor's perspective, this is due to the disclosure requirements of franchise legislation, which requires franchisors to provide details concerning litigation commenced against them, or pending litigation against them. A disclosure document that contains numerous lawsuits commenced against the franchisor may dissuade prospective franchisees from acquiring the franchise. Consequently, franchisors have commenced to utilize mandatory arbitration or ADR clauses in their franchise agreements, mandating that disputes must first be resolved through ADR instead of through litigation, with the goal of having a smaller number of disputes to disclose.<sup>146</sup> In doing so, the franchise may appear more appealing to a prospective franchisee.

From a franchisee's perspective, ADR offers a less expensive means of dispute resolution than litigation, removing barriers associated to justice such as cost, location and duration.<sup>147</sup> For instance, although

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<sup>146</sup> Daniel F. So, *supra* note 69 at 266.

<sup>147</sup> *Ibid.* at 261.

the length of a mediation varies with the complexity of the dispute, mediation of a typical franchise dispute may take 10-15 hours and involve two or three sessions.<sup>148</sup> ADR will also allow a franchisee to avoid the combative nature of litigation, fostering the preservation of commercial relationships while parties attempt to resolve a dispute.<sup>149</sup> Furthermore, the franchise relationship presents some particular aspects which make it critical that the courts have special tools to deal effectively with their disputes.<sup>150</sup> Some of the concerns that franchisors and franchisees have to address when a dispute arises between them include:

- It is very difficult for all parties to continue working together on a daily basis while pursuing a court case between them;
- In many cases, a franchisee who decides to sue his franchisor is not, at that time, in a good financial position;
- Where the amounts paid to franchisors by the franchisee are the only, or main, source of income, franchisors have found themselves in problematic positions toward their franchisees by reason of the slowness of the court system; and
- Another problem encountered by franchisors and franchisees when disputes arise is the uncertainty in regard of their contractual relationship during the time when litigation has taken place, most specifically in the event where the franchisor has terminated the agreement by reason of one or several defaults committed by the franchisee while the franchisee pleads that these defaults are non-existent, are not sufficient to justify the termination of the franchise agreement or that the franchisor has improperly terminated same.

These examples demonstrate the need to provide for particular mechanisms and means in order to deal with issues encountered in franchisors/franchisees disputes.<sup>151</sup> Due to the importance of ADR to both franchisors and franchisees, it is necessary to determine how Manitoba will address the subject in its franchise legislation. The questions facing Manitoba with regard to ADR are twofold. First, what should be disclosed to the franchisee in pre-contract documents?

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<sup>148</sup> International Institute for Conflict Prevention and Resolution (CPR), "National Franchise Mediation Program: A dispute Resolution Process for Franchising," online: <<http://www.cpradr.org/pdfs/5/franchise.pdf>> at 4.

<sup>149</sup> Daniel F. So, *supra* note 69 at 264.

<sup>150</sup> Jean H. Gagnon, "Some Considerations Regarding the Judicial and Non-Judicial Resolution of Franchisors/Franchisees Disputes" (1 April 2003), online: Jean H. Gagnon Consulting Services <<http://www.jeanhgagnon.com/site/jhg/files/documents/someconsiderationsjudicialandnonjudicialresolution.pdf>> at 7.

<sup>151</sup> *Ibid.* at 7-12.

Second, should ADR be mandatory? Prior to addressing either issue, it may be helpful to consider how the various legislated Canadian jurisdictions and the UFA deal with ADR.

### **a. Dispute Resolution Provisions in Canada and the ULCC**

#### **i. Ontario**

Ontario addresses the issue of ADR in section 5 of the *Regulations Made Under the Arthur Wishart Act (Franchise Disclosure), 2000*.<sup>152</sup> The section requires that where a franchisor will use an internal or external alternative dispute resolution process, a disclosure document shall include a description of the mediation or other ADR process and the circumstances when the process may be invoked. Furthermore, as per s. 5(2), every disclosure document shall state:

Mediation is a voluntary process to resolve disputes with the assistance of an independent third party. Any party may propose mediation or other dispute resolution process in regard to a dispute under the franchise agreement, and the process may be used to resolve the dispute if agreed by all parties.

In other words, Ontario requires that a franchisor who chooses to use ADR disclose all elements to the franchisee in the disclosure document. Franchise legislation in Manitoba should adopt a similar provision to ensure that franchisees are aware of what action a franchisor may or may not pursue.

In **Toronto Truck Centre Ltd. v. Volvo Trucks Canada Inc.**,<sup>153</sup> an agreement included a dispute resolution process that provided for binding mediation of any dispute, including a dispute for termination of the agreement. The manufacturer purported to terminate the agreement without notice, and the dealer applied for an interlocutory order compelling the manufacturer to submit to mediation and to continue the dealership until completion of the mediation. The court held that the order should be granted, since the clear intent of the agreement was that disputes should be submitted to the dispute resolution process.<sup>154</sup> This

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<sup>152</sup> O.REG 581/00.

<sup>153</sup> (1998), 163 D.L.R. (4th) 740 (Ont. Ct. Gen. Div).

<sup>154</sup> Frank Zaid, *supra* note 65 at 339.

is a clear example of the necessity to disclose what, if any, ADR methods will be pursued.

In **Ellis v. Subway Franchise Systems of Canada Ltd. (2000)**,<sup>155</sup> the franchise agreement contained a clause stating that any claim arising out of the agreement would be settled by arbitration in accordance with rules of the American Arbitration Association at a hearing in Connecticut. After the franchisee failed to cure alleged defaults, the franchisor filed a demand for arbitration. The franchisee brought an application for stay of proceedings on the grounds that the arbitration clause in the Franchise Agreement was unenforceable on the basis that it was unconscionable. The court, finding no evidence of fraud, duress or inequality of bargaining power upheld the clause and arbitration proceeded. Had the franchisee not been difficult, the dispute could have been resolved promptly and economically.

#### ii. New Brunswick

A unique feature of New Brunswick's proposed *Franchises Act*, Bill 32 is the ability of one party to a franchise agreement to deliver a notice to the other party requiring that a dispute be mediated. Although the proposed legislation permits one party to a franchise agreement to require that the other party mediate a dispute, the proposed legislation confirms that this procedure does not preclude either party from taking other steps in relation to the dispute.<sup>156</sup>

Bill 32 thus requires that any party to a franchise agreement who has a dispute with the other party may deliver a notice of dispute setting out the nature of the dispute and its desired outcome. The parties must then attempt to resolve the dispute within 15 days after delivery of the notice of dispute. If the parties fail to resolve the issue, any party to the dispute may then deliver a notice to mediate within 30 days after delivery of the notice of dispute but not before the expiry of the 15 days for resolving the dispute. Section 8(6) of the Bill addresses the issue of confidentiality by stating that no person shall disclose or be compelled to disclose in any proceeding before a court, tribunal or arbitrator any information acquired, any opinion disclosed or any document, offer or admission made in anticipation of, during or in connection with the

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<sup>155</sup> B.L.R. (3d) 55.

<sup>156</sup> Blaire Rebane, Karen Carteri and James M. Bond, "Recent Developments in Franchise Law," (Paper presented to the Western Franchise Summit, 2007) online: Lang Michener LLP Publications, Articles <[http://www.langmichener.ca/uploads/content/2007%20Western\\_Franchise\\_Summit\\_Handout.pdf](http://www.langmichener.ca/uploads/content/2007%20Western_Franchise_Summit_Handout.pdf)> at 4.

mediation of a dispute under this section. Section 8(7) restricts 8(6) by stating that no confidentiality will apply to anything that the parties agree in writing may be disclosed, an agreement to mediate, a document respecting the cost of mediation, a settlement agreement made in resolution of all or some of the issues in dispute or any information that does not directly or indirectly identify the parties or the dispute and that is disclosed for research or statistical purposes.

### iii. Prince Edward Island & Alberta

Schedule I, Part III, section 16 of PEI's *Franchises Act Regulations*<sup>157</sup> requires that a franchisor disclose a description of any restrictions or requirements imposed by the franchise agreement with respect to arbitration, mediation, or other alternative dispute resolution process, including any requirements relating to the location or venue of such a process.

In contrast to all other legislated jurisdictions in Canada, Alberta has yet to incorporate an ADR provision.

### iv. ULCC

In contrast to all existing Canadian franchise legislation, Section 8 of the UFA contains the most extensive description of a dispute resolution process to be adopted by parties to a franchise agreement. It is important to note, however, that, when passed, New Brunswick's *Franchises Act* will closely resemble the UFA, with the only difference being that the UFA does not contain a provision stating that the delivery of a notice of dispute or notice to mediate does not preclude a party to a franchise agreement from taking any other measure in relation to the subject matter of the dispute.<sup>158</sup>

In composing such provisions, the ULCC considered at great length whether franchise disputes would be resolved more advantageously through a form of alternative dispute resolution. Recognizing that in certain provinces the rules of practice in civil proceedings mandate a form of pre-trial mediation, the Committee determined that it would be beneficial to provide for mediation to be invoked by any party to a franchise agreement.<sup>159</sup> In support of mediation, the ULCC states:

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<sup>157</sup> R.S.P.E.I. 1988, Chapter F-14.1.

<sup>158</sup> Bill 32, *Franchises Act*, 1st Sess., 56th Legislature, New Brunswick, 2007, s. 8(10) (Received First Reading on 23 February 2007).

<sup>159</sup> Uniform Law Conference of Canada, *supra* note 71 at 22.

The Committee believes based on its own experiences and those brought to the attention of the Committee that party initiated mediation will be of significant benefit to resolve franchise disputes prior to the commencement of, as well as after the commencement of, litigation proceedings.<sup>160</sup>

Where the UFA differs even from New Brunswick's Bill 32 is in its regulations. In dealing with the issue of mediation, rather than including further provisions in the regulations, the ULCC created mediation specific regulation.<sup>161</sup> These Regulations establish general rules for appointment of a mediator and for mediation as well as specific rules for pre-litigation mediation and post-litigation mediation. Some of the topics covered include:

- Pre-mediation conference;
- Exchange of information;
- Costs of mediation;
- Timing of mediation;
- Time limits on mediation; and
- Defaults.

These Regulations apply to the mediation of a dispute that is initiated by notice to mediate delivered before or after a legal proceeding or arbitration in respect of the dispute has been commenced. In essence the proposed mediation process is mandatory. It is elective on the part of either party that wishes to mediate, so long as the parties have attempted to resolve the dispute. Once the election to mediate has been made by one party, it becomes mandatory on the other.<sup>162</sup>

It is clear that the ULCC has created the most complete provisions with regard to mediation. If a province were to adopt the UFA's Mediation Regulations, all parties to a franchise would know what to

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<sup>160</sup> *Ibid.*

<sup>161</sup> Uniform Law Conference of Canada, *Regulation Made under the Uniform Franchises Act – Mediation*, online: Selected Uniform Statutes <[http://www.ulcc.ca/en/us/UFA\\_Mediation\\_Reg\\_En.pdf](http://www.ulcc.ca/en/us/UFA_Mediation_Reg_En.pdf)>.

<sup>162</sup> Larry Weinberg and Peter Henein, "Annual Franchise Law: Legislative Update," (Paper presented to the 5th Annual Franchise Law Conference, 2005) [Toronto: OBA Continuing Legal Education, 2005] at 6; online: Publications by Cassels Brock Lawyers – Lawrence M. Weinberg <[http://www.casselsbrock.com/publications/Henein\\_FranchiseUpdate1005.pdf](http://www.casselsbrock.com/publications/Henein_FranchiseUpdate1005.pdf)> at 7.

expect if mediation is chosen as a dispute resolution method. It is important to note, however, that the UFA regulations only apply to mediation. This is key because, although mediation may be quite effective in the context of franchising, the parties must share a genuine desire to resolve the dispute promptly in an equitable manner.<sup>163</sup> Otherwise, any attempts at mediation will be futile.

#### **b. What Should Manitoba Do?**

The first question under this heading is whether Manitoba should address the prospect of mediation or ADR in its franchise legislation. An ADR provision would require a franchisor to disclose to the franchisee if there are any ADR methods that will be employed to resolve a dispute and, if so, to provide further details. Since it might be important for a prospective franchisee to be properly informed of the ways by which the franchisor resolves its agreements and disputes with franchisees,<sup>164</sup> franchise legislation in Manitoba should incorporate a dispute resolution provision.

In doing so, Manitoba should adopt a different approach than the ULCC and focus on both mediation and arbitration. Although the former is a useful tool for franchise dispute resolution, franchise legislation should also address an ADR method that does not rely on a party's willingness to participate for success. Franchisors may have more resources to pursue litigation than franchisees and may thus not cooperate throughout the mediation process. Therefore, a binding method of resolving disputes, such as arbitration, will be necessary.

Ontario and PEI have adopted dispute resolution provisions that focus on what must be disclosed, whereas New Brunswick, by following the UFA, has adopted dispute resolution provisions that outline the process to be followed. Manitoba should adopt a provision similar to Ontario and PEI and not New Brunswick, as the latter forces the parties to mediate, even when they may not have mutually agreed to do so. Therefore, Manitoba's provision will not dictate what process ought to be followed, only stating what must be disclosed.

Attempting to preserve clarity, Manitoba's provision should require more detail than both Ontario and PEI's. Whereas section 5(1) of Ontario's franchise regulations only requires a description of the mediation or alternative dispute resolution process, Part III, section 16 of PEI's regulations adds the disclosure of any requirements relating to the

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<sup>163</sup> CPR, *supra* note 148 at 2.

<sup>164</sup> Jean H. Gagnon, *supra* note 150 at 13.

location or venue of such a process. Although PEI was on the right track by requiring more detailed disclosure, it still maintains Ontario's vagueness. Thus, Manitoba should adopt more detailed provisions, allowing a franchisee to know exactly what will take place in case of a dispute.

If a franchisor chooses to resolve matters through mediation or arbitration, Manitoba franchise legislation should require that the disclosure document outline all elements. For example, an arbitration provision should explain the methods for selecting an arbitrator, governing rules for arbitration, special characteristics or experience of the arbitrator, costs of arbitration, governing law of arbitration, venue of arbitration, and confidentiality.<sup>165</sup>

In contrast, a mediation provision must cover elements such as the matters accepted for mediation, that mediation is to proceed prior to the matter being brought before a court, other tribunal or arbitrator, the mechanics for appointing the mediator, place of mediation, special experience factors for the mediator, confidentiality, costs and expenses of mediation, inability to resolve the matter, and procedures for mediation.<sup>166</sup> Manitoba's provision should still adopt the open-ended requirement that a general description be provided, while also enforcing a non-exhaustive list of requirements, to encourage a franchisor to disclose certain details that the franchisee should know and are not required by the provision.

Overall, Manitoba should incorporate dispute resolution provisions that require franchisors to disclose what method of ADR they will employ in case of a dispute, together with two lists of what must be disclosed in the case where mediation or arbitration are the ADR methods of choice.

### **c. Should Manitoba Adopt a Mandatory ADR Process?**

While primarily a voluntary process, the use of ADR can be mandatory in certain instances. As a result, even parties that want to litigate, who do not wish to mediate, or arbitrate a dispute, may be required by law to use alternative dispute resolution methods prior to

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<sup>165</sup> Joseph Adler and Frank Zaid, "Drafting Franchise Agreements in the 21st Century," (Paper Presented to the Ontario Bar Association's Third Annual Franchise Law Conference: Franchising in a New World of Disclosure, 2003), [Toronto: OBA Continuing Legal Education, 2003] at 26.

<sup>166</sup> *Ibid.* at 25.



having their cases heard in a court of law.<sup>167</sup> To date, two Canadian provinces, British Columbia and Ontario, have introduced some form of mandatory pre-trial mediation into the civil court process, meaning that mediation is or can be required after an action has been commenced, but before it reaches trial.<sup>168</sup>

Adopting a mandatory mediation process for franchise disputes would have both positive and negative aspects. One of the advantages of mediation is that it is less adversarial than arbitration, and therefore, less disruptive of business relationships. Furthermore, since there are other options available if mediation should fail, entering into a mediation process is essentially without risk.<sup>169</sup> The International Institute for Conflict Prevention and Resolution (CPR) supports the use of mediation to resolve franchise disputes:

In fact, failure is the exception. [...] with the assistance of a skillful mediator, parties to a great variety of business disputes have succeeded in bridging wide gaps in their positions and often in developing creative, mutually advantageous business solutions.

However, CPR clearly states that the principal pre-condition to mediation is that the parties share a genuine desire to resolve the dispute promptly in an equitable manner.<sup>170</sup> Mediation will fail if the parties are not willing to partake in the process and resolve the dispute. Consequently, forcing parties to mediate through a mandatory mediation program may very well be a waste of time and money in such instances. A mandatory mediation program should therefore not be adopted in Manitoba.

A mandatory arbitration scheme lacks many of the disadvantages of mandatory mediation. Since arbitration is a binding method of solving disputes, it means that, once agreed upon, it will resolve the dispute between the parties, and absent some specific circumstance, the parties will have no further recourse or appeal rights after a decision is reached.<sup>171</sup> However, even many supporters of ADR fear the ramifications of mandatory arbitration. Mr. Jean H. Gagnon, Vice-President of the

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<sup>167</sup> Daniel F. So, *supra* note 69 at 263.

<sup>168</sup> Peter Snell and Larry Weinberg, ed., "Fundamentals of Franchising – Canada," (Forum on Franchising, American Bar Association, 2005) at 327.

<sup>169</sup> CPR, *supra* note 148 at 2.

<sup>170</sup> *Ibid.*

<sup>171</sup> Daniel F. So, *supra* note 69 at 261.

Alternative Dispute Resolution Section of the Quebec Division of the Canadian Bar Association and member of the Mediation and ADR Committee of the Quebec Bar, argues that it is too delicate and dangerous to, by law, force the parties to a franchise dispute to resort to arbitration or any other ADR process.<sup>172</sup>

When considering arbitration as a mandatory means of conflict resolution, it is necessary to realize that a dispute resolved through arbitration can be as costly in terms of fees and costs as a case going before a court. Furthermore, if one of the parties is litigious in nature or is drawn to arbitration against its will, arbitration can also be a slow process which may take months and, sometimes, years before a final decision is reached and enforced.<sup>173</sup> Therefore, a mandatory arbitration scheme would also fail to provide a desired alternative method to litigation.

In conclusion, Manitoba should adopt neither mandatory mediation nor mandatory arbitration and should only introduce provisions dealing with a franchisor's disclosure requirements with regard to what ADR means it will adopt when a dispute arises.

This concludes the list of issues for consultation suggested by the Manitoba Law Reform Commission in the Consultation Paper on Franchise Legislation.

## **6. Additional Suggestions**

### **a. Exclusions on Oral Representations During the Franchise Sale Process**

In order to prevent a franchisor abusing a franchisee by making oral representations that will not be enforced, Manitoba should follow the *UFA*, PEI's Act and New Brunswick's Bill and incorporate an exclusion for oral arrangements. Section 2(3) of the *UFA*, the *Arthur Wishart Act (Franchise Disclosure)*, 2000, PEI's *Franchises Act*, and section 2(4) of New Brunswick's Bill 32 states:

This Act does not apply to [...] a relationship or arrangement arising out of

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<sup>172</sup> Jean H. Gagnon, *supra* note 150 at 13.

<sup>173</sup> Jean H. Gagnon, "There Must be a Better Way to Resolve Franchise Disputes!" (2006), online: Jean H. Gagnon Consulting Services <<http://www.jeanhgagnon.com/site/jhg/files/documents/theremustbeabetterwaytoresolvefranchisedisputes.pdf>> at 2.

an oral agreement where there is no writing that evidences any material term or aspect of the relationship or arrangement.

This will in turn deter franchisees from entering into oral arrangements with franchisors and require that all promises be made in writing. Furthermore, since Manitoba has repealed its Statute of Frauds<sup>174</sup> dictating that a written agreement will override any alleged oral contract,<sup>175</sup> it is necessary to say so through franchise legislation.

In conclusion, Manitoba ought to include Ontario's exclusion on oral representations made during the sale process to encourage potential franchisees to require franchisors to reduce all agreements to writing.

#### **b. Cooling-Off Period**

All Canadian franchise legislation allows for a 14-day period between the issuance of disclosure documents and the signing by the prospective franchisee of any agreement relating to the franchise or the payment of any consideration relating to the franchise. In addition to adopting such a provision, Manitoba should consider incorporating a cooling-off period.

Although the two-week period grants franchisees with ample time to acquaint themselves with all disclosure documents, a cooling-off period would allow them a final interlude during which to assess the purchase. Considering that, for the most part, franchise agreements last as long as 10 years and may be difficult to transfer, a potential franchisee will be investing a significant amount of time and money. Thus, once the agreement is signed, a seven-day period would allow them to analyze the purchase with a "cooler head" and cancel it if so desired. In doing so, neither party would suffer a loss.

To incorporate such a provision, Manitoba could emulate section 13 of Australia's *Trade Practices Act 1974*. The section states that a franchisee may terminate an agreement (being either a franchise agreement or an agreement to enter into a franchise agreement) within seven days after the earlier of entering into the agreement or making any payment under the agreement. A cooling-off period will not be granted to a franchisee renewing, extending, or transferring an existing franchise

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<sup>174</sup> *An Act to Repeal The Statute of Frauds*, C.C.S.M. c. F158, Enacted as: R.S.M. 1987, c. F158.

<sup>175</sup> Frank Zaid, "Franchising and The Law," online: Online Publications, <<http://www.osler.com/resources.aspx?id=8402>>.

agreement. In addition, if the franchisee decides to terminate the agreement during the cooling-off period, the franchisor must, within 14 days, return all payments made by the franchisee to the franchisor under the agreement. However, the franchisor may deduct from this amount paid the franchisor's reasonable expenses if the expenses or their method of calculation have been set out in the agreement.<sup>176</sup>

As an alternative, Manitoba could follow section 8 of *The Condominium Act*.<sup>177</sup> The Act allows a prospective purchaser who has signed an agreement to purchase to cancel the agreement within 48 hours. The prospective franchisee would be able to cancel the agreement by personally giving a written notice of cancellation to the franchisor or franchisor's agent or by sending a written notice of cancellation by registered mail, fax or any other method, except e-mail, that provides proof that it was sent, to the address or fax number given by the franchisor or the franchisor's agent for this purpose.

### **c. Independent Legal Advice (ILA)**

The power and information imbalance separating franchisees from franchisors could be reduced, in addition to providing disclosure documents, by introducing an independent legal advice clause in Manitoba's franchise legislation. Ideally, all franchisees should be forced to consult a lawyer to achieve an insight into the franchise agreement that they may not be able to attain on their own due to the document's complexity and length. Furthermore, such a clause would reduce litigation between parties to a franchise, as the franchisee will be well aware of all that the franchise agreement entails. Thus, Manitoba should seriously consider addressing the matter through legislation.

Currently, there is no legislation in existence in Manitoba that enforces seeking independent legal advice. However, the *Reverse Mortgage Regulation* encourages doing so.<sup>178</sup> The disclosure form provided under the Regulation's schedule in section L pertains to seeking advice. It states:

It is strongly recommended that you talk to  
your lawyer about this reverse mortgage  
before you sign the mortgage or any other

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<sup>176</sup> Australia, Trade Practices (Industry Codes – Franchising) Regulations 1998, *supra* note 48 at s. 13.

<sup>177</sup> R.S.M. 1987, c. C170.

<sup>178</sup> Man. Reg. 65/2002.

document that requires you to sign the mortgage.<sup>179</sup>

Because reverse mortgages are complicated, and many borrowers lack the background and expertise to evaluate both the suitability of the mortgage for them and the terms of the mortgage offered to them, independent advice and counseling should be sought by most prospective borrowers.<sup>180</sup> This argument could also be applied to franchising.

In contrast to all Canadian franchise legislation, Australia's legislation requires that a franchisee attain independent legal advice prior to entering into a franchise agreement. Under section 11(2) of the *Trade Practices Act 1974*, a franchisor must receive from the prospective franchisee prior to entering into the franchise agreement the following:

- (a) Signed statements, that the prospective franchisee has been given advice about the proposed franchise agreement or franchise business, by any of: (i) an independent legal adviser; (ii) an independent business adviser; (iii) an independent accountant; or
- (b) For each kind of statement not received under paragraph (a), a signed statement by the prospective franchisee that the prospective franchisee: (i) has been given that kind of advice about the proposed franchise agreement or franchised business; or (ii) has been told that that kind of advice should be sought but has decided not to seek it.<sup>181</sup>

The subsequent section qualifies subsection 2 by stating that it does not apply to the renewal or extension of a franchise agreement and that it does not prevent that franchisor from requiring any or all of the statements mentioned in paragraph 2(a).<sup>182</sup>

In formulating its own independent legal advice provision, Manitoba should follow Australia's example. A similar provision to the *Reverse Mortgage Regulation* would not go far enough to ensure that franchisees seek legal advice. In contrast, Australia's Act, by forcing franchisees to either seek advice or waive it, ensures that franchisees seriously consider the possibility of consulting an expert. In adopting the

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<sup>179</sup> *Ibid.*

<sup>180</sup> (2006) "Manitoba Law Reform Commission Review of the Garnishment Act," Commonwealth Law Bulletin, 32:1 103-139 online: <<http://dx.doi.org/10.1080/03050710600850280>> at 137.

<sup>181</sup> Australia, Trade Practices (Industry Codes – Franchising) Regulations 1998, *supra* note 48 at s. 11(2).

<sup>182</sup> *Ibid.* at s. 11(3).

Australian clause, Manitoba should limit the qualified experts for consultation to lawyers and accountants, since these are the two parties who are better suited to provide the necessary advice.

In addition, Manitoba should introduce a cooling-off period (in case the general cooling-off period is not adopted) that applies only to those franchisees that waived attaining professional consultation. Doing so will allow more time for franchisees left with the task of understanding the franchise agreement on their own to actually do so.

Overall, Manitoba should introduce a provision forcing franchisees to seek independent legal advice prior to signing the franchise agreement to ensure that they make a well-informed decision. This will counter the power imbalance between franchisors and franchisees as well as reduce litigation arising out of misunderstandings. This requirement will however be limited by a waiver, with which franchisees will be able to forego attaining independent legal advice. Furthermore, a cooling-off period should be granted to those franchisees who waive the independent legal advice clause, granting them an extended period of time to become acquainted with the agreement.

#### **d. Layout of Disclosure Document**

The main goal of adopting franchise legislation in Manitoba should be to help franchisees make well-informed decisions when purchasing a franchise. Requiring franchisors to provide clear and accurate disclosure documents is a necessity to accomplish this worthy goal. To ensure greater ease in reading a disclosure document, Manitoba's franchise legislation should require franchisors to provide a table of contents, indicating all headings and subheadings, together with page numbers.

Australia's *Trade Practices Act 1974* incorporates very thorough layout requirements. For instance, under s. 7, the Act requires franchisors to include a table of contents, as well as indicating the page number on which each item begins.<sup>183</sup> In addition, Annexures 1 and 2 describe the specific manner in which the disclosure document must be laid out. For instance, Annexure 1 sets out what the first page of every disclosure document must include: the franchisor's name, signature of the franchisor, officer or authorized agent of the franchisor and the preparation date of the disclosure document.<sup>184</sup>

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<sup>183</sup> Australia, Trade Practices (Industry Codes – Franchising) Regulations 1998, *supra* note 48 at s. 7.

<sup>184</sup> *Ibid.* at Annexure 1, s. 1.1.

Manitoba should only follow Australia's requirement to include a table of contents. Requiring franchisors to adopt a specific template may be too onerous for some franchisors coming from foreign jurisdictions and employing a wrap-around. Furthermore, including a table of contents will suffice to make the disclosure document clear to navigate, accomplishing the goal of franchise legislation. Thus, Manitoba's franchise legislation should incorporate the requirement that disclosure documents include a table of contents with page numbers.

## **CONCLUSION**

**F**ollowing a failed attempt to introduce franchise legislation in 1992, Manitoba once again faces the opportunity to adopt a franchise act. Unlike then, franchise legislation has become widely accepted in Canada and is currently in force in Alberta, Ontario and PEI; New Brunswick has recently completed the first reading of its own franchise bill. The need for franchise legislation in Manitoba is clear. With a business population comprised predominantly of franchisees rather than franchisors, the former must be protected from abuse at the hands of the latter without unduly impeding fair commercial practices. In adopting franchise legislation, Manitoba ought to consider other Acts in force in Canada together with the Uniform Law Conference of Canada's UFA, molding them into one to form the most progressive version. This is an opportunity Manitoba cannot afford to pass.

