ECONOMICS AND INDUSTRY STANDING COMMITTEE

FRANCHISING BILL 2010

TRANSCRIPT OF EVIDENCE
TAKEN AT PERTH
WEDNESDAY, 13 APRIL 2011

SESSION ONE

Members

Dr M.D. Nahan (Chairman)
Mr W.J. Johnston (Deputy Chairman)
Mr I.C. Blayney
Ms A.R. Mitchell
Mr M.P. Murray
Mr P. Abetz (Co-opted member)

Hearing commenced at 9.17 am

SPENCER, MR WAYNE
Executive Director, Retail Traders' Association of Western Australia, examined:

TSAKNIS, MR LEO ANTHONY
Barrister, Francis Burt Chambers, examined:

The DEPUTY CHAIRMAN: Thanks for your appearance before the committee today. This committee hearing is a proceeding of Parliament and warrants the same respect the proceedings in the house itself demand. Even though you are not required to give evidence on oath, any deliberate misleading of the committee may be regarded as a contempt of Parliament. Before we commence, there are a number of procedural questions I need you to answer. Have you completed the "Details of Witness" form?

The Witnesses: Yes.

The DEPUTY CHAIRMAN: Do you understand the notes at the bottom of the form?

The Witnesses: Yes.

The DEPUTY CHAIRMAN: Did you receive and read an information for witnesses briefing sheet regarding giving evidence before parliamentary committees?

The Witnesses: Yes.

The DEPUTY CHAIRMAN: Do you have any questions relating to your appearance before the committee today?

The Witnesses: No.

The DEPUTY CHAIRMAN: The committee has received your submission. Thank you for your contribution. Do you wish to propose any amendments to your submission?

Mr Spencer: I believe it is more context and discussion around it.

The DEPUTY CHAIRMAN: So you do not have any amendments?

Mr Spencer: No.

The DEPUTY CHAIRMAN: Before we ask you any questions, do you wish to make a brief opening statement that directly addresses your submission and the terms of reference?

Mr Spencer: Yes, please.

The DEPUTY CHAIRMAN: Please go ahead.

Mr Spencer: Representing the Retail Traders' Association of WA here today, we are the state's peak industry body representing the retail industry of WA. The RTA represents about 4 000 shopfronts throughout Western Australia. Some 98 per cent of those would be considered small to medium-sized businesses. The RTA most probably represents about 25 per cent of the retail industry, but, through our association members, we would most probably extend to 85 or 95 per cent of the industry. We would state up front that the RTA is an unequivocal supporter of the Franchising Bill 2010. To just give a statistic, 40 per cent of Australian retailers are involved in franchising, which translates to approximately 10 000 to 12 000 franchise businesses in Western Australia.

The franchising concept was developed some time back. Quite honestly, it was developed to further or progress business programs when capital was short and experience was required. We initially saw contracts of around 25 to 30 years being put in place, which gave adequate time to recoup capital and run systems and programs. The franchisor program was actually built to survive taking percentages or recouping from that. Today we see franchise programs down to five years or less. Quite honestly, with the cost involved with leasing, labour et cetera, there is very little chance of a rate of return on those types of investments. I would note that the Commercial Tenancy (Retail Shops) Agreements Act states a minimum of five years. We have been listening to and attending something where it was indicated that it was a statutory right of five years. That is correct, but a minimum can be negotiated for far longer terms. Because of this pressure on franchise models, services offered are somewhat limited and somewhat restricted, but in many cases we see in the actual franchise agreements wording to the effect that full service is being given. We have also noted—this is our concern—that the initial franchise fee being paid can be considerable; half a million dollars or $1 million is not out of the question. In a number of cases, there is a far higher return on that fee than there is from running and operating the franchise business; hence, the challenge of churning evolves. You also have enforced direct purchasing and many other issues that can arise.

Unfortunately, from our perspective, we have a number of members who are both franchisors and franchisees. We do see a trend from some of these "rogue franchises", which I guess is the terminology, whereby franchisees are bled dry, forced into a corner and basically cannot undertake a legal battle or challenge. They are also frightened or prohibited by contractual agreement to voice anything publicly. We could note that that is why you really have not seen too many franchisees here but have been bombarded by members of the FCA. We make the point that we hope that you can see through this and focus on the evidence, not the numbers. The RTA has a long history of advocacy for good faith reform in the franchise industry dating back prior to the Bothams inquiry, the South Australian franchise inquiry and also the federal Ripoll inquiry. From all these inquiries, the inclusion of good faith and penalties has arisen as a recommended strategy. It would be prudent to note here that all these inquiries did not happen just to fill the time of the various committees; there was strong angst and concern about the continuing abuses inflicted by rogue franchisors that caused these inquiries. Evidence was presented to all these inquiries; it is all on the record. But it goes back even further than this. There are concerns that have been questioned by inquiries as far back as 1976. The damning fact is that nothing has been done to make amends to prevent this type of unscrupulous behaviour. As a responsible industry association, we would not support any legislation that we considered would seriously disadvantage the interests of business or, in this case, small business in Western Australia. We have received nothing but support from our members, as well as a steady increase of discussions with non-member franchisees within our community.

I think it is prudent that you understand my background just a little. I have had experience in retail, merchant banking, all forms of retail, development, recreational and also finance. I have lived and worked throughout Australia, but also in the USA, UK, Europe and Asia. My personal involvement, unfortunately, was with a rogue franchisor in Kleenmaid. Unfortunately, the end result is that the two responsible parties are going to walk away. In Kleenmaid, we literally saw people led to slaughter. If they had money and blood in their veins, they were done; it was a very classy act. But the fact is that they were misled; they were misinformed, sometimes by silence; and, definitely, if they did not come near the standards that were wanted to be achieved, they were bullied and beaten. We wish to strenuously point out that the financial ruin, marriage breakdowns and suicides brought about by opportunistic and predatory franchise has been well documented and cannot be glibly dismissed as inconclusive evidence. These stories, these real facts, are about real people and real families who have been left destitute and ruined in many cases. But if you listen to FCA, these issues are rendered completely invisible. We believe it is now time for the Parliament to make a stand against this type of conduct and to make note that it is just not acceptable, and that this

Parliament will take measures necessary to support its citizens who have risked their financial future in the franchise industry. To this point, we bring your attention to the WA Bothams inquiry. There were some 90 franchisee submissions. It was closed down because of the content of some of those submissions, which were horrific. I strongly stress that this committee should open those and read them personally. We also have a book of a few instances for you that have been in the media and we would like to offer that. There are also some in-confidence situations that I would like to run through with you now. I will not mention names. You can understand the seriousness of this and the position that I would put some players in if I did.

The DEPUTY CHAIRMAN: Just to clarify that, this is an open hearing so whatever you say will be recorded.

Mr Spencer: I understand that. I will just give you some instances that are happening right now.

In one case, a state franchise was purchased for $1.2 million. An agreement was signed with a letter of comfort to support certain clauses in that agreement. Twelve months into that agreement, the franchisor sold to another party, who basically wanted to take over the state as a corporate scenario. He read the franchise agreement and realised he had full control over the KPIs and quadrupled those, which were unachievable. He started litigation against the franchisee and at the same time offered him $150 000 to take off.

In another one, the franchisor has opened company-owned stores in direct opposition to franchisees, offering far cheaper pricing and deals to the public. He put pressure on existing franchisees to quit, leaving them with lease commitments but no business or possibility of income.

In another one, the franchisee wants out of an agreement as he can acquire goods far cheaper than obligated under his franchise agreement. The franchisor is price gouging.

In another one, the franchisor refuses to renew longstanding franchise agreements and has offered 60 per cent in the dollar value. Another party is available who will pay 100 cents in the dollar. In that same case, they are now refusing to implement a marketing program to support WA franchisees to lower the value of the franchisees.

In another one, the franchisee has a rent review renewal of franchise agreement arising. Franchisee initiates negotiations with landlord to settle the figure. The franchisor sends the bill for the franchisee fee, the franchisee pays, and the landlord sells out prior to formalising the new lease. The new owner reneges and offers an 88 per cent rent increase, plus shop fit-out of $200 000. It is just absolutely not commercial. The franchisor goes to ground.

[9.30 am]

Franchisee just happens to be the oldest franchisee in WA, with over 15 years experience. So we are not talking about people who are completely naive to the situation. Franchisor takes marketing fees and does no marketing; bleeds franchisees dry. Four out of 11 franchisees in the state lose their home. The rest have now combined, luckily, with a new franchisor, constructed a new franchise agreement, built on the terms of the good faith and are now working the business to success.

I also draw your attention to a class action for Wendy's. I would like to read just a couple of items. This is to do with Therese Evans, who you have most probably heard of in the news —

> Wendy's ended a six-year relationship and locked Mr and Mrs Evans out of their business for a debt Mrs Evans puts at $7000.
>
> ...
>
> The Evans' experiences are far from unique in a sector credited with contributing $130 billion to the economy annually.
>
> A Federal parliamentary committee inquiry into franchising in December 2008 noted franchisors necessarily held more power than franchisees.

This is from press —

> In August, BusinessDay exposed complaints from disenchanted Wendy's franchisees, who asked whether their businesses were being set up to fail. One franchisee Therese E vans, 48, died of a suspected heart attack days after being locked out of her shop in the Hunter Valley.

If you read the Botham inquiry, you will read like situations. There is also a possible class action developing with Baker's Delight. If you go to the website bakersdelightlies.com.au, you can read all the horror stories. I think it is important that you realise that this is still going on and it is big and small. The rogue not just the little fly-by-nighter.

I would also like to point out that—I can actually remember this; I give some of my age away—back in the late 1960s, early 1970s franchisees in the petroleum industry were being inflicted with huge personal and financial pressure because the franchisors wanted their petrol stations back. The Petroleum Retailing Marketing Franchise Act 1980 was introduced to prevent the power abuse by franchisors. Once this was introduced, it stopped that type of behaviour, that conduct, immediately. So that introduced a "good cause" clause and that was supposed to be carried across commercial leasing et cetera, but it was never done.

Overseas we have explored to some extent what others around the world have done with regards to instituting "good faith" into law, especially within the franchise arena. We have noted actions taken in Malaysia, Canada and especially the USA where individual states have taken unprecedented action to stop this type of predatory opportunistic behaviour by franchisors. I raise this specifically as we understand that this legislation within the USA was largely the result of the likes of Yum, who I note has made a submission and will present after ourselves today. Their type of activity cannot be allowed to be predicated here in Australia and especially here in WA.

I would like to just read a couple of items and this is from Mr Bryden, who is the representative of Yum. This is recorded in the Hansard —

> We are not opposed to regulation of franchising at all. But we believe it should be directed towards preventing abhorrent behaviour and also at ensuring that parties are informed of the nature of the agreements they are entering into. Of course, that is the thrust of the regulation and intervention so far. We are interested in good faith ... We believe an appropriate definition could provide clarity.

The DEPUTY CHAIRMAN: What is the reference there?

Mr Spencer: I will hand this to you if that is all right.

The DEPUTY CHAIRMAN: That would be great, thank you

Mr Spencer: The Chair says —

> You have this issue with good faith in the sense that you do not want it in the code.
>
> **Mr Bryden**—That is not our position.
>
> ...
>
> **CHAIR**—Just so we have it on the record, you are clearly saying that you do not have an issue with good faith being in the code?
>
> **Mr Bryden**—That is fine.
>
> ...
>
> We would say that it has to be in good faith. We are saying that whatever good faith is, it is something we would be comfortable with ... but we are not against good faith.

I also bring you to the Ripoll committee. They have outlined a few points, which I think are relevant —

> Franchisee opportunism may take the form of free riding, unauthorised use of franchisors' intellectual property rights, underperformance, or failure to accurately disclose income.

> However, the franchisor's control over the provisions in the contract enables franchisors to address opportunistic behaviour of this kind by enforcing the terms of the franchise agreement.
>
> ...
>
> There is an inherent and necessary imbalance of power in franchise agreements in favour of the franchisor, but abuse of this power can lead to opportunistic practices including encroachment, kickbacks, churning, non-renewal, transfer, termination at will, and unreasonable unilateral variations to the agreement.
>
> ...
>
> The imbalance of power in franchise agreements is not something that should be changed, but what does need to be checked is any abuse of this power.
>
> ...
>
> Although there is no clear definition of 'good faith', it would be generally understood to mean acting fairly, reasonably and honestly, encapsulating the concept of 'a fair go'.

The DEPUTY CHAIRMAN: Do you want to table those two bits of paper? The transcripts from the Ripoll inquiry, Mr Spencer—is that how you describe them?

Mr Spencer: Yes, there is one from the Ripoll. There is one from the joint committee of corporations and financial service and there is also a download on the Wendy's case.

The DEPUTY CHAIRMAN: Great. Thank you very much.

Mr Spencer: In response to terms of reference for this inquiry, this association has sought to satisfy ourselves that the Franchising Bill 2010 does indeed meet our expectations and that of the committee and the WA Parliament. To do so we sought the opinion of Mr Malcolm McCusker, QC, also AO, who is soon to be the Governor of Western Australia and will be in charge of looking after the constitution of WA. Mr McCusker is one of Western Australia's most distinguished and respected legal practitioners. We believe that all aspects relating to part (a) of the terms of reference are answered by his opinion. Unfortunately, Malcolm McCusker could not be with us today because of visiting the Queen or whatever. Mr McCusker's opinion is more ably supported by former commonwealth Attorney-General Mr Daryl Williams, QC, jointly written with Leo Tsaknis. Mr Alan Robertson, SC, is now appointed as a Judge of the Federal Court. We submit that you have now before you no better clarity and certainty than presented by these three outstanding members of our legal fraternity. They all concur that the bill passes all legal tests required. Furthermore, and perhaps more importantly, the bill outlines a concise and legally workable definition of "good faith" that is specific to the franchise relationship. As Mr Williams aptly put it, this bill fills a void in the Australian franchising law. Few if any inquiries into this issue have had this benefit or privilege or whatever you would like to call it, because it is but one step away from a court determination. These opinions give you legal certainty and justification in your determination to recommend the bill to the WA Parliament. I would like to now pass to Leo for him to add comment.

The DEPUTY CHAIRMAN: Okay. I would appreciate it if you could because we do have a few questions and I do not want to keep you too long today.

Mr Tsaknis: Did you want to ask questions of Mr Spencer first?

The DEPUTY CHAIRMAN: No, I am happy for you to proceed, but I am just making the point that the longer the opening the less opportunity for exploration.

Mr Tsaknis: I will try to be as brief as possible. Very briefly my background: I commenced independent bar in 1996 in Perth. I specialise in commercial advice and litigation and government advice and litigation not only both for and against federal and a state governments, but also statutory authorities and agencies. Prior to that, between 1982 and 1984 I was a legal officer in the federal Attorney-General's department. When I left in 1994 I was the principal general counsel in the Attorney-General's department. I had a heavy involvement in legislation in that capacity.

I am here as a witness, not as an advocate. I am not here to persuade any particular policy viewpoint. I am here really to try to clarify and set down, perhaps affirm, some of the matters in the Franchising Bill. One matter I will say, it does seem to me that the enormous number of submissions that have been put to the committee—I have not obviously read them all; the numbers have been quite staggering—have to be assessed against the prism of what the bill will actually do. There are from all parties—I do not cast aspersions on any of them—assumptions as to what the bill will do or what it is intended to do, which I think need to be clarified or at least form the starting point. I think when that is done in effect the committee's job will be a lot easier because one will be able to assess the policy viewpoints and the policy desirability from that prism of what the bill actually does.

The question insofar as the formal questions, it seems to me, having regard to the opinions that have been put, that it ought to accepted there is no direct inconsistency with the five terms of reference that the committee is tasked to investigate and report on in so far as the committee is considering whether or not the bill will enhance the purpose of the Franchising Code of Conduct. I cannot say anything more than expand on what is put in the joint opinion that it will, in our submission, fill a gap that exists in the current franchising code. Effectively, there is no enforcement mechanism of the code and that is what the bill seeks to do. Whether as a policy perspective that is desirable or not I will leave to the committee to determine. In so far as the third formal reference—that is, the cost impact—it is not possible to say what the cost impact on the state or participants in franchising will be. It does seem that the model which has been adopted is the least expensive model that could be envisaged; that is, there is already an existing state commissioner under the Consumer Affairs Act who will be tasked with this exercise. Litigation disputes are going to be governed by what the individual litigants seek to pursue, so effectively the costs are going to be privatised in the litigation. As I said, I cannot envisage a more cost-effective mechanism, but whether or not the real costs are going to be positive or negative in that scheme which you have heard much argument about, I am sure, hidden costs and real costs and business efficiencies, I am certainly in no position to comment on that and I have not seen anything that would, with respect, allow any formal clear decision to be made in respect of that or for me to be able to comment on that.

They are the formal matters, it seems to me, before the committee. I am aware that a number of other matters have been considered. Retrospectivity—it is clear that the bill is not retrospective. That is uniformly agreed by all the opinions. In fact, I do not think I have seen any serious argument that the bill is retrospective.

The DEPUTY CHAIRMAN: Can I just interrupt on that and seek clarification, because what you are saying there by that submission is it is not retrospective because it relates to enforcement, so it is about when you enforce your rights, it is not about when the right existed; is that what you are saying?

[9.44 am]

Mr Tsaknis: It is not retrospective because it does not affect rights or liabilities by reference to past events. This bill speaks only as to the future by placing an obligation to negotiate in good faith from a future time, and it is for that reason that it is not retrospective.

The DEPUTY CHAIRMAN: And in respect of the enforcement procedures?

Mr Tsaknis: They are only in the future as well, of course. They only apply from the time after the bill comes into operation as a result of what may be claimed or real breaches as a result not claimed.

The DEPUTY CHAIRMAN: Thank you very much.

Mr Tsaknis: So, it is a simple concept, but it is conceptually sometimes difficult to grasp what retrospectivity actually means, because in one sense, all laws are retrospective, because you are always prohibited from doing what before the law you were not prohibited from doing. So, that is obviously not the test.

The aspect I wanted to focus on is this duty to act in good faith, which is in cause of 11 of the bill. Clause 11(1) exhaustively defines the meaning of the term "good faith". It means to act fairly, honestly, reasonably and cooperatively, but, and this is an important qualification, I put it in terms of qualification because the argument, seems to me, from many submissions that the good-faith requirement will have particular effect or results, but the qualification is that the obligation to act in good faith applies only in respect of any dealing or negotiation in connection with a franchise agreement, whether that is the entering or renewing. So, the good faith is that dealing or negotiating in good faith; that is, it is concerned with procedures, it is not concerned with outcomes. The best analogy one can give, it is not entirely apt, but it is really a measure of procedural fairness, or natural justice as that was called in dealings; it is not a provision that mandates an outcome or indeed any particular outcome.

The DEPUTY CHAIRMAN: Just to summarise that, are you saying that you could have a capricious outcome so long as he did in a fair way?

Mr Tsaknis: I think that you can; my view is that you can.

The DEPUTY CHAIRMAN: So, is your suggestion that the court is not going to be testing the outcome of the discussions, but rather the procedures that are used to find the outcome?

Mr Tsaknis: That is so. I can see a very limited avenue for challenging it, very limited. I think it will be awfully difficult to rise, but I can see as the last stepping stone—perhaps I can give you the steps that I think will happen. The court is not able to determine whether a particular proposal or outcome is objectively reasonable under this proposal. That is all it can determine under reasonableness, and I picked that term because that seems to me, perhaps the one that allows more value judgement if you are going to argue, "What is reasonable?" The only reasonableness required is in the dealing or negotiation, so one might say, to give an example, "Well it is not reasonable for you to say to me, 'You are only going to negotiate for a week, between the hours of midnight and 2.00 am and, because it is the busy time of your season as a franchisor or a franchisee.'" Now, that is not reasonable negotiation. As to what the particular terms of the negotiation are, whether you are offering more or less money or not enough money, that is not something that goes to the reasonableness of the negotiation. In fact, the courts have made that clear; the most recent case that we have cited in our opinion is the 2010 Supreme Court decision. The provision does not import a consideration of the offer that is actually being made. It will be unlikely that the offer will be a matter that goes to reasonableness, except, as I say, there may be an extreme case, which I will come to. The process does not mandate any outcome at all, whether it be a renewal of a franchise agreement or indeed any other outcome.

But I think one might say, "What is the whole point of this bill?" It struck me when I looked at it: why is it that the parties or the proponents dislike it so much and what is it that the proponents like it so much for? Putting aside whether any of the parties seem to either have exaggerated or minimised the effect, what might it do? It struck me from my experience that what does happen in practice is that when you get people around the table, outcomes are effected. Getting people to talk—I have been involved in the most intransigent litigation when no-one would deal with anyone at all and the court forces you to sit around a table and talk, and the impossible does happen, people talk, outcomes get reached, compromises get reached. That does happen with the most intransigent parties in the world if they are forced to look at each other and deal with each other.

The DEPUTY CHAIRMAN: Settle on the last day of trial!

Mr Tsaknis: What reasonableness does do, or does not prevent, is self-interested behaviour. So long as you act honestly in negotiations; that is, you put forth proposals and you are prepared to listen to proposals, you can act as self interested, it seems to me under this bill, as you wish to act. Merely putting a proposal, which the other party considers unreasonable, is not acting unreasonably in negotiations or in connection with negotiations. Now, whether one gets to the stage where a proposal may be so unreasonable that indicates in effect that you are not prepared to negotiate in

connection with it, one could think perhaps of a very extreme example of a very small franchisee, a business maybe worth $100 000 or $50 000. First step, multi-million dollar business, "I will give you $100 for the business." One could say, "Well, look this really goes so far below; you're not attempting to negotiate." But having made that qualification, I would say, if I was acting for the party offering the $100, "Well, that is an opening gambit. If you are prepared to hear someone out and put in a counterproposal, that is not unreasonable." Indeed, one does not see as strange or unusual in multi-million dollar litigation where a party says—it has happened to me—"I want $20 million to settle this dispute; that is my bottom line", and you end up settling for something like $200 000 or $300 000. The bottom line is that it is movable; it is $20 million and you walk away with $200 000, provided you are prepared to negotiate in connection with that dispute. This will be, of course, determined by judges who are familiar with that. They are experienced commercial lawyers; they are used to the argy-bargy. So, that is what will happen. I suppose in a nutshell, unreasonable or capricious offers will only be relevant insofar as they may provide evidence from which it can be inferred that the party is not negotiating or dealing in good faith. The offers themselves, other than that, can be put in one's self-interest to the extent that the party wishes to.

The next aspect, perhaps, is what might be called the definition of good faith. There is not obviously an inclusive definition as distinct from an "includes" definition of good faith. The terminology that has been chosen does represent terminology consistent with terminology adopted in the decided cases. However, what the decided cases do not do here is to use the terminology uniformly. Some cases pick up one word, some cases pick up others and some cases pick two in combination.

The DEPUTY CHAIRMAN: Can I just stop you? I just want to clarify because this is a very interesting issue and it has been raised by a number of parties. What is your view about whether it should be a "means" or "includes" in respect of this definition of "act in good faith"?

Mr Tsaknis: There are obviously two different—"means" gives certainty; "includes" gives potentially more flexibility.

The DEPUTY CHAIRMAN: So, which do you think is preferable for the Parliament to look at?

Mr Tsaknis: Having regard to this particular legislation, in my view, a "means" definition provides greater certainty and is to be preferred. The reason I say that in this context flows from the bill and I explain this: a "means" definition, because the bill, in clause 10, allows additional rights or obligations, does not exclude the common law. The common law has its uncertainty, I can put it that way, I am speaking generally, but this bill is designed to reduce the uncertainty. The common law has the uncertainty; if one wants to go away and argue the common law and say that this should include this, and good faith now also includes that, you have got that under clause 10. Now, to include that in clause 11, whilst one might say, "Well, it gives you flexibility", you may get the case where, "fairly, honestly, reasonably and cooperatively" is not enough and maybe we do not want to compromise that and we want to change it to inclusive. But it seems to me that having the protection in clause 10 we can still argue the common law with the certainty of clause 11 and what that brings. The best balance that the bill provides is to have the certainty in clause 11 so that parties can use that. But it does seem to me that the vast circumstances, the vast variety, will be either "fairly", "honestly", "reasonably" or "cooperatively" issues. So, it is difficult to envisage what will not fall in there. Keeping that certainty with the flexibility that clause 10 creates, if one thinks that clause 11 is not certain enough, provides the best balance of this bill, because ultimately, one should not underestimate, from a business point of view, the value of certainty. I think the certainty by "means", given that the protection is still there in clause 10, is a desirable way to go, given the structure of the bill. So, it is my opinion that "means" is preferable.

Mr P. ABETZ: Some of the people who have appeared before us, and some of the submissions, claim that the words "fairly, honestly, reasonably and cooperatively" do not give certainty. Can you just elaborate on how a court would use those words? Are they common words?

Mr Tsaknis: The court will refer to what might be called the dictionary definition of those words; they will use it in the way that the ordinary person understands them to mean. They will not apply technical or legal meaning to those words, which means that anyone reading the bill will fall back on what they understand the words to mean as distinct from what may be some external meaning. That seems to be, given the target market, a desirable feature. It also underscores the educative value of the bill and I think that one should not underestimate the educative value of legislation, because whilst we have heard it said that people go to lawyers and lawyers can advise them of their rights and whatever, lawyers are not omnipotent. You will find many, many lawyers who are not really aware of developments of good faith in commercial litigation, and in particular franchising. Without any disrespect, I think that a lot of individuals who went to pick the lawyer would probably go to lawyers who would not have a clue about what the law of good faith is or what it means. Even experienced lawyers disagree as to what the common law means. So, it does seem to me that the educative value—the reality is if you went to a lawyer as a franchisee and knowledge of the legislation was known, that is what most lawyers will go to instinctively, and most lawyers would do so whether or not they knew about the common law. So, I think the importance of having words that have a well-understood or common meaning is important as distinct from trying to create some new formulation. And of course, those lawyers who are familiar and have a background will be instantly aware that those words have been used before and can draw on that as well, so it does have that dual benefit.

The other aspect of good faith is the nexus with unconscionable behaviour. They are not synonymous concepts. Unconscionable conduct imposes different standards to a good faith conduct. Unconscionable conduct will show a lack of good faith, but lack of good faith is not unconscionable conduct. That is probably the simplest way I can put it and I am sure the committee somewhere has been referred to the High Court's decision in Australian Competition and Consumer Commission v CG Berbatis Holdings Pty Ltd (2003) 214 CLR 51, where the concept of unconscionability was applied in that case by a lessee. What occurred in that case was that the lessee was in dispute with the landlord about a considerable sum of money related to his lease, but his lease had now come to an end and he wanted to renew it and assign it to a third party. The landlord said, "I will let you pass on that lease, but I want you to let me off all my liability dispute that we have got about it", and the attendant said, "This is unconscionable; I have a right to give that up, to negotiate on this other issue about passing my lease on to a third party." The High Court said in that case, "It is hard bargaining, but it is not unconscionable; you have no rights to have that lease renewed and the landlord is entitled to impose any condition on it that he likes, so it is not unconscionable. Whether it is bad faith is the $64 question but it certainly was not unconscionable in that particular case."

[10.00 am]

Mr Spencer: I might add that with unconscionable conduct, we have now been sitting here for 15 years and we still do not have a definition. This bill sets out the concise definition with flexibility and it is a very important point to understand.

Mr Tsaknis: The reality is that no-one is arguing unconscionable conduct in any franchise case. Since Berbatis, I do not know that it has ever been argued before a court that conduct is unconscionable. I suspect that you have had huge legal minds input into that question. The fact that legal actions are not being brought probably says something about the prospects amongst the legal community.

The DEPUTY CHAIRMAN: Do you mind if we turn to some questions? If there are additional matters that you think are important, I will make some comments about how you might let us know. I am sorry to cut you off; it is just that we have limited time. I found your submissions very informative. I think they have been very accurate and to the point of the bill. I am very pleased to have heard them. If I have cut you off and if there are things that you need to submit, I will suggest a way you can give us that information at the end.

Mr Spencer: We will find a way.

The DEPUTY CHAIRMAN: Mr Spencer, you made the point that you have both franchisees and franchisors as members of the association. How do you handle potential conflict of interest within your organisation?

Mr Spencer: We meet individually with those people, understand —

The DEPUTY CHAIRMAN: Sorry; in the context of preparing a submission for us.

Mr Spencer: Sometimes we go against it. We have principles that we will not succumb to. Those principles stand. If someone comes with an argument that conflicts with that principle, the principle wins. They understand that.

The DEPUTY CHAIRMAN: Do you have a committee that makes that decision?

Mr Spencer: Correct.

Mr P. ABETZ: One of the things that various people brought before us is that their good faith is vague and it is not definable. Can you give us an indication of how many pieces of legislation have good faith in them? I am probably putting you on the spot.

Mr Tsaknis: No, you are not putting me on the spot; I actually looked at this question. I kept figures on it. There are excluding regulations. I checked the database on Friday, 11 April. There are 610 pieces of commonwealth legislation—that is, acts of Parliament—excluding subsidiary legislation. There are 610 acts—found in a search of the AustLII database—as of 11 April 2011 that impose obligations, create liabilities or impose a norm of conduct by reference to the obligation of good faith. There are 610 in the commonwealth sphere. A search on the same day shows that there are 400 acts of the Western Australian Parliament in the same category.

Mr P. ABETZ: Would you agree with the assertion that the concept of good faith is too vague for people to be able to work with is a furphy? If 400 pieces of WA legislation have the term in it, and 610 federal, surely it is a very well-known concept.

Mr Spencer: The Premier should know it is; he is bound to good faith!

Mr Tsaknis: It is certainly one of the most ubiquitous terms used in legislation. I would have thought whatever may be the merits or demerits of the legislation, the use of the term "good faith" is not one of them. It is a very commonly resorted to determination. To give two very quick examples, in the field of director's duties, in section 181, I think of the Corporations Law the obligation is raised in terms that directors must do what they do in good faith. That is the touchstone of liability. In the criminal law there are all sorts of exclusions for things done in good faith. They are very commonly used words not only in general legislation but also under the common law when one talks of equity in common law. They are certainly not uncertain words. The last agreement on the AustLII database was the Iron Ore Beneficiation (BHP) Agreement Act 1996. I randomly pulled that out. It was an agreement between Hon Richard Fairfax Court as Premier of Western Australia and BHP Direct Reduced Iron Pty Ltd and related to the iron ore development at Port Hedland. It is a very significant facility. Section 27 deals with what happens at the end of the iron ore agreement. It simply states —

> In the year 2044 the parties to this Agreement shall meet and consider in good faith the extension of the term of this Agreement.

That is how the interest in the bill arose. It is certainly very common.

Ms A.R. MITCHELL: Mr Spencer, on page 7 of your submission you refer to the "current unrestrained bullying culture encouraged by the lack of regulation to enforce minimum standards of conduct". What evidence can the RTA provide to the committee to support this claim? Can you give us a bit more information about this culture? Is it as pervasive as the statement implies?

Mr Spencer: I have already given the committee a whole bundle of media reports and also stated on the record a number of current situations that have been expressed in confidence to us very recently. The Franchising Code covers requirements prior to an agreement, in the delivery of physical facts and data. In the recent amendments it is starting to talk about requirements at the end of the situation. It does not cover the conduct of the parties—I stress, both parties—before, during and after. That is the real challenge that needs to be met. There is a very strong imbalance of power because of the actual business model of franchising. That in itself is good but the abuse of power inside that contract is the reason we are here today. I have given about a dozen instances that are current. I have handed to the committee a book that contains about 200 pages. You are welcome to read it.

The DEPUTY CHAIRMAN: You talked about a franchise agreement, saying they were originally for 25 years and now you are saying some of them are for only five years. If you are going to get back your franchise payment over five years, you are going to have a 20 per cent return on top of all your other returns. Are these the sorts of things that should be disclosed by the franchisor to the franchisee, such as what your minimum rate of return has to be to make your money back?

Mr Spencer: The full gambit of what is involved in that business should be presented—the good, bad and the ugly.

The DEPUTY CHAIRMAN: Do you not believe that that is currently happening?

Mr Spencer: I have been in a situation personally in which I have been told not to say certain things. I have had information in front of me relating to a renewal situation of a franchise in which another franchisee prospect was coming into place, and none of the current trading terms was divulged. In fact, it was encouraged that people do a business plan and make their own strategy. When they came in with figures that were totally preposterous, the only comment that was made to that franchisee was, "Are you comfortable with that?" That is the type of thing that can happen because people are not being honest. Twenty-five years ago I used to shake hands with a person and you knew you had a contract. Now you count your fingers.

The DEPUTY CHAIRMAN: I wish to address the question of renewal orders. Does the RTA have any comment to make? It has been submitted to us that a renewal order is an extraordinary power because if the relationship is broken down for whatever reason, it is an extraordinary power to give to a court the right to reinstate a business relationship. Does the RTA have any views on that?

Mr Spencer: Yes, we do have a comment. Most people perceive that at the end of a situation. Therefore, if a franchise agreement is reliant on a property lease and that has expired, the court will not give something that is uncertain. You have to put yourself in a position in which you have some churning motion. In the case of Wendy's, they were locked out. In that case the courts could have stepped in and said, "You must continue business while we continue discussions." I could put many instances to you. I have been in situations in which I have taken people to court and they are still good friends. We still keep discussions going. Yes, they might be more on a professional and civil level rather than a friendship level but the fact is that they still continue. I think that there is a lot of furphy around this—a lot of mischievous-type intent. The fact is that the whole bill is tailored to the franchise industry. There are peculiarities in that industry that need to be recognised by this committee. I hope that answers your question. Would you like to add to that?

Mr Tsaknis: I would. Again, this flows from a misunderstanding of how clause 11 and clause 14 dovetail. One talks about a complete breakdown of the relationship. As I see it, the renewal order is to effectuate the duty of good faith. For example, one would see a renewal order operating in that circumstance when one is coming to the end of an agreement and the franchisor may say, "I'm not dealing with you at all; I'm going to let this expire in a week's time. You're going to be finished and that's it." I would see the renewal order dovetailing if the court says, for example, "We've got an application here for an urgent injunction to terminate the agreement. Under the renewal order power we will extend the term of the agreement for three months to enable the parties to undertake

their obligations under clause 11 to cooperatively, honestly and reasonably negotiate in connection with that renewal." If that occurs during those three months, parties can be as obstinate as they like as clause 11 has been complied with and the agreement terminates. There is a misconception that the way the renewal order operates is there is a complete breakdown and therefore why should I be forced to be someone's employer? It really relates to the limited obligation under clause 11, and the renewal order is to give effect to that. The policy decision really is not whether we should force parties that do not get together or force a potential remedy; the issue is whether we should have a remedy whereby if a party does not abide by the requirement to negotiate or deal in good faith, there should be some remedy in respect of that to enable that good faith negotiation to occur. There is a misconception of the width those orders are directed to.

The DEPUTY CHAIRMAN: Do you think that there is a risk that the legislation will be seen to provide more rights than it is granting? I direct that question to you, Mr Spencer, because your members will be coming to talk to you about this. The submission is that it is not a right for a good faith outcome but a right to a good faith process.

Mr Spencer: The process is the important issue both before, during and after. It is a damning effect—that we have to bring this to law to enforce people to act civilly, honestly and responsibly with people. I would say that in 90 per cent of the cases out there, they do it already but there is always that element that disrupts society in some way, shape or form.

The DEPUTY CHAIRMAN: Do you think this question of the length of the agreements is something that Parliament should consider in the framing of the legislation?

Mr Spencer: As far as the length of a franchise agreement is concerned?

The DEPUTY CHAIRMAN: Yes.

Mr Spencer: If people are dealing honestly, the franchisor should be able to demonstrate that the facts and figures all stack up, and that is supported by the franchisee's business plan otherwise that franchisor should not be in business. I think it should be considered, encapsulated, in this bill.

[10.15 am]

I also stress—it was said before—that people have stated that five years is the maximum lease. With a commercial lease, the minimum that must be provided is a five-year lease. There are provisions that allow for less, and of course negotiation can get you far more. Let us face it, leases range from a temporary casual lease right through to 30 years.

The DEPUTY CHAIRMAN: We are nearly out of time.

Mr P. ABETZ: May I ask one more quick question?

The DEPUTY CHAIRMAN: Certainly.

Mr P. ABETZ: Clause 13(2) states —

> If a franchisee under a WA franchise agreement or the Commissioner makes an application under subsection (1), the court cannot require the applicant to give an undertaking as to damages.

Perhaps I can address this question to you, Leo? Leo is easier to say than Mr Tsaknis!

Mr Tsaknis: Leo is fine.

Mr P. ABETZ: Can you comment on that? Some people who have come before the committee have said that this is a most unusual clause to have in a bill. Can you comment on that?

Mr Tsaknis: It is not an unusual clause to have in a bill; it is being inserted with increasing regularity. It is inserted where there is perceived to be an imbalance in the resources of the one party versus the other party; for example, conservation legislation or employee–employer legislation. Indeed, I think the normal employee–employer legislation one looks at and the various

industrial relations acts do require employees to give an undertaking. The best example is probably the Family Law Act, which I think contains provisions about not giving undertakings in damages as well. So it is predicated on an imbalance in bargaining power between one party and another party. The other matter I notice in the bill is that whilst it does not require an undertaking, it does not instruct the court that the absence of the undertaking is irrelevant. It may very well be that the court may take the view that, in a particular case, the absence of an undertaking, even though a party is not required to give it, may be a relevant consideration in its deliberations. And it does not stop there; for example, parties may be prepared to give an undertaking even though they are not required to—the court cannot require them to; that is, a party off its own bat, can give an undertaking. I think there is a flexibility in the sense—with all due respect to my client—that if an organisation such as Hungry Jack's wanted it, I would expect that the fact that they were not prepared to offer an undertaking may be significant. If I were a mum-and-dad operator, I do not think any adverse consequences would flow from me, as a mum-and-dad operator, not offering an undertaking.

Mr P. ABETZ: Thank you.

The DEPUTY CHAIRMAN: This will be the last question unless other members of the committee want to ask you something: it is about the renewal of an agreement. If you do not renew a lease, it still continues as you pay your rent. If you are an employee on a fixed-term contract and you continue to work and continue to be paid, the contract continues. Is there some unique nature about franchising arrangement that there is not an expectation that the contract will continue after the end of its term so long as the parties continue to abide by it? Is there some view about that?

Mr Spencer: As to whether there should an addition of that continuation clause?

The DEPUTY CHAIRMAN: There is an expectation with other contracts that they will continue.

Mr Spencer: I do not have a problem with that: do you?

The DEPUTY CHAIRMAN: It does seem a little unusual that when this contract comes to an end, everyone expects the contract to disappear, whereas other contracts continue the relationship.

Mr Spencer: It is normally a renewal factor that is entered into well and truly beforehand. That is what the change to the Franchise Code is insisting; that six to 12 months before, the franchisor says it is going ahead with the contract so that people can be prepared and can adjust their stock levels and finance et cetera.

Mr Tsaknis: There is no legal impediment, if I can put it that way. Whether there is an expectation, I think you are better able to say than I. But there is no legal impediment to having, for example, a provision that states "the agreement shall be renewed unless" or that provides for a time of renewal or a set number of renewals. There is no legal impediment for that.

The DEPUTY CHAIRMAN: And indeed many other contracts for which those sorts of arrangements —

Mr Tsaknis: That do operate on that basis.

The DEPUTY CHAIRMAN: Yes.

Mr Spencer: I believe that if the franchisee or the lessee has done absolutely nothing wrong, has performed and has a good active business, which is relevant to their market wherever they may be, the franchisor or the landlord is nuts not to renew—and renew on commercial terms.

The DEPUTY CHAIRMAN: Thank you. If there are no further questions, I will read the formal closing statement.

Thank you for your evidence before the committee. There are a number of questions that we have not been able to ask you today. Would you be willing to answer a series of written questions that the committee will provide when it sends you a copy of today's transcript?

Mr Spencer: Sure.

The DEPUTY CHAIRMAN: Thank you.

A transcript of the hearing will be forwarded to you for correction of minor errors. Please make these corrections and return the transcript within 10 days from the date of the covering letter. If the transcript is not returned within this period, it will be deemed to be correct. New material cannot be introduced via these corrections and the sense of your evidence cannot be altered. Should you wish to provide additional information or elaborate on particular points, please include a supplementary submission for the committee's consideration when you return your corrected transcript of evidence. Once again, thank you very much.

Mr Spencer: Would that be an opportunity to include some closing comments?

The DEPUTY CHAIRMAN: Yes.

Hearing concluded at 10.20 am