ECONOMICS AND INDUSTRY STANDING COMMITTEE

FRANCHISING BILL 2010

TRANSCRIPT OF EVIDENCE
TAKEN AT PERTH
THURSDAY, 5 MAY 2011

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 11.08 am

UNDERDOWN, DR MICHAEL
Special Counsel, appearing on behalf of the Law Society of Western Australia, examined:

The CHAIRMAN: I will read an opening statement. Thank you for your appearance before the committee today. This committee hearing is a proceeding of Parliament and warrants the same respect that 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 contempt of Parliament. Before we commence, there are a number of procedural questions that I need to ask you. Have you completed the "Details of Witness" form?

Dr Underdown: Yes.

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

Dr Underdown: Yes, I do.

The CHAIRMAN: Did you receive and read the information for witnesses briefing sheet regarding giving evidence before a parliamentary committee?

Dr Underdown: Yes, I did.

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

Dr Underdown: No.

The CHAIRMAN: The committee has received the Law Society of Western Australia's submission; thank you for your contribution. Do you wish to propose any amendments to the submission?

Dr Underdown: No.

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

Dr Underdown: No. I think the submission is very plain. We have just addressed the three issues that were put to us to address.

The CHAIRMAN: Just to clear up my own ignorance, how does the Law Society of Western Australia fit in with the Law Council of Australia?

Dr Underdown: The Law Council is the federal body. Each state has its own law society.

The CHAIRMAN: Do the views of the Law Society of Western Australia filter up to the Law Council?

Dr Underdown: Yes, and vice versa; we get the council's views. I am actually a member of the commercial law committee of the Law Society of Western Australia, and we have addressed this issue. We received submissions from the council, and also from interested parties.

The CHAIRMAN: Have you been involved in this debate, because it has been an ongoing debate for some time?

Dr Underdown: Yes. I am also a lecturer in competition law at the University of Western Australia, and I have an advanced degree in competition law. So even though it is not the area that I am working in at Clayton Utz, I of course have to keep abreast of what is happening.

The CHAIRMAN: And the Law Society would have given submissions to the Bothams inquiry and the Ripoll inquiry and all the other inquiries that have examined this issue?

Dr Underdown: Yes. I have also spoken previously to the federal committee that is looking into the franchising code. I was supposed to give evidence to that committee, but in the end the committee as a whole did not come to Perth. But I did meet with the chairperson of the committee in Perth, on behalf of the society.

The CHAIRMAN: We have had evidence given to us by the Law Council and the Law Society of Queensland, because we want to see how it all fits together. Could the definition of "WA franchise agreement" in clause 4 of the bill, and the extraterritorial application of clause 6, be interpreted to include the interstate franchisees of franchisors based in Western Australia?

Dr Underdown: Well, that is the way it reads. The problem with extraterritorial application of laws, whether it is the Trade Practices Act, or whatever, is enforcement. Obviously, if the bill once passed applies extraterritorially, the burden of seeking to enforce the provisions of the act interstate is going to fall on somebody, whether it is the Western Australian government or the franchisee who is complaining. Someone is going to have to pay for that. Enforcement interstate is not without problems and without costs. It is often easier to deal with the local law and the local courts. But it is not impossible. It happens all the time in Australia; we are a multi-jurisdictional country.

The CHAIRMAN: Would the courts individually decide, in a precedent-setting manner, whether it had extraterritorial coverage?

Dr Underdown: No. I think in the first place the very first person who tried to enforce a provision in the legislation would come up against this, and either their lawyers will advise them that it is too complicated or too expensive or too time consuming; or, if they do proceed, there will be a court decision about it.

The CHAIRMAN: So the body that is given responsibility for administering that will have to make an administrative decision based on the advice of its lawyers?

Dr Underdown: The commissioner in Western Australia might decide to institute proceedings himself or herself, and obviously that will be a cost to the government. But, again, that is not without precedent either.

The CHAIRMAN: Are there similar cases in which you might have a franchisor in a state, and a state piece of legislation that is trying to guarantee or regulate aspects of their relationship with their franchisees in Western Australia, and that case might create a precedent for a huge number of franchisees all around the nation, and the cost could be very large?

Dr Underdown: That is the issue. For most big franchises, the franchisors are based interstate and not in Western Australia. There are a few that are based in Western Australia, but the majority are not. The national franchises will have franchisees in different states. So it gets a bit complicated. But overriding everything is the franchising code, which governs the operation of franchises.

Mr P. ABETZ: Clause 3(1) of the bill says —

> If a term is given a meaning in the Franchising Code of Conduct (WA), it has the same meaning in this Act, unless the contrary intention appears.

I was given to understand by the parliamentary counsel that assisted in putting the bill together that in the Franchising Code of Conduct, "business" is a term that is used exclusively for franchisees and not for franchisors, and therefore there is no extraterritoriality in the bill. Could you clarify that for us? There is no intention in the bill to make it extraterritorial. For me as a layman, when I read the bill when it came from parliamentary counsel, I thought that the term should be "franchisee business", but I was told that "business" is a franchisee business and never a franchisor business, and therefore that does not need to be done. Would you recommend that that be clarified in the wording of the bill to make it absolutely clear? What are your comments on that?

Dr Underdown: To say that only franchisees are businesses is a bit strange, because "business" has other general meanings in law; it does not refer just to a franchisee. To that extent, I think it is probably not wise to think that the term "business" applies just to a franchisee. You just said that it was not the intention that the Western Australian legislation would apply extraterritorially. I would make two comments on that. First, every state Parliament has the power to legislate extraterritorially, as does the commonwealth Parliament. The second point is that since most of the franchisors are based interstate, it will be very hard to apply the legislation if it does not apply extraterritorially. They are not going to just come and present themselves to the Western Australian courts if they have done something wrong or have been in breach of the legislation. So I think it is going to have to apply interstate. But of course we have arrangements between the states to apply decisions of the courts in the other jurisdictions.

Mr P. ABETZ: Can you clarify the term "extraterritoriality"? My understanding of the extraterritoriality issue is that it would apply to franchisor/franchisee relationships outside of WA, whereas the bill seeks to relate only to franchisor/franchisee relationships within WA; that is, where the franchisee's business is predominantly in WA.

[11.18 am]

Dr Underdown: I know that is the intention. It is very easy to apply the bill if both franchisor and franchisee in Western Australia are based or located in Western Australia. The problem arises if one party to the dispute is not based in Western Australia. That is when you have to have either the Western Australian courts decide after legal proceedings have been instituted, and then that decision is applied interstate under the arrangements between the states, or the Western Australian franchisee has to be able to litigate interstate, which of course adds to the cost. And there is also this issue of who actually does the litigation.

The CHAIRMAN: Let us say there is an extraterritorial aspect to this issue and one of the parties decides to, let us say, operate out of New South Wales. Could the New South Wales courts adjudicate under this bill, if it was an act?

Dr Underdown: They would not normally because it is Western Australian legislation. Most of the other states, I think with the exception of South Australia, are just relying, at this stage anyway, on the Franchising Code of Conduct. I think only South Australia and Western Australia have legislated in addition for the code, but that is permissible under the federal legislation. It specifically states that states can pass their own legislation.

The CHAIRMAN: One of the concerns we have is the costs to this issue: what are the cost implications for the state in this issue? Under the bill there is an assumption that a government body will act on behalf of franchisees; and, if it is extraterritorial, that might increase the cost significantly, particularly if the government agency acting on behalf of the franchisees has to act interstate. What are some of the cost aspects of that? Is it just the travel or getting lawyers to jurisdictions?

Dr Underdown: I do not think the travel is going to be a major component, but it is the legal costs. If I am not mistaken, the commerce commission here has acted on behalf of affected consumers in the past. I am not sure whether interstate, but if they have acted in court interstate, they probably have some knowledge of the cost implications. But, as I have mentioned before, there are two parties who could initiate proceedings under the legislation. There are commissions but also affected parties. Franchisees could, in which case, of course, they bear their own costs.

Mr W.J. JOHNSTON: Could I just clarify in respect of the action a party might take in another jurisdiction? What you are suggesting is that if this legislation is passed, it will create a right in the contract between those parties, and it is that right that the party might seek to enforce in another jurisdiction. Is that what you were saying?

Dr Underdown: Yes, but that is independent of the act. Under the individual franchise agreement, there will be some dispute-resolution mechanism. It is a contract; the franchise agreement is a contract at law, so there is nothing to stop an affected party that suffered loss or damage, or believes it has suffered loss or damage, from instituting legal proceedings to seek a remedy in the courts, and there is nothing to stop you doing that anywhere in the world if you can afford to and so on.

Mr W.J. JOHNSTON: Could I just clarify again that some agreements would say that they are interpreted in accordance with a particular jurisdiction?

Dr Underdown: Yes, that is true. There is normally a jurisdiction or choice-of-law clause in most contracts, and that means that that is your first forum or first place to institute proceedings. But proceedings can be transferred to the Federal Court perhaps, or even go as far as the High Court, by leave. So it might end up outside of this jurisdiction.

Mr W.J. JOHNSTON: Sure; but if that were to be the case, it would be for some reason.

Dr Underdown: Yes.

Mr W.J. JOHNSTON: There would be a decision made.

Dr Underdown: Yes, of course, but it would generally be on something like a public interest issue, and for the High Court it would generally only be on a constitutional or some state versus commonwealth issue. For example, if somebody challenged this legislation as being incompatible with the federal legislation or the Franchising Code of Conduct, that theoretically could go all the way to the High Court, but I do not see that happening.

Mr P. ABETZ: I am trying to understand the extraterritoriality. It seems to me that you have taken a different line from how I have understood it. With the federal situation with the Franchising Code of Conduct, if somebody from the United States makes a franchising agreement with somebody in Australia, then because we have the Franchising Code of Conduct, the way I have understood you to define extraterritoriality actually means that the Australian government's legislation has an extraterritorial effect because the franchisor is operating out of the United States or New Zealand or wherever. So, in effect, any law governing any kind of business contract immediately is extraterritorial. Is that right, or am I missing something?

Dr Underdown: No. In a contract between two parties—say you contract with the builder here to build a house for you—there is not going to be any extraterritorial application of that, unless, for example, the United States company—to use the US example—during the construction of your house fully takes over the Western Australian builder. Then there could be some application of US law. But the way this works internationally—say the franchisor in America has an issue with the franchisee in Perth, the way that would play itself out is that the American franchisor would initiate proceedings in the US court. The Department of Justice, which is one of the two bodies responsible for administering competition law—anti-trust law in the United States—would then seek the help of the ACCC under the comity agreement between Australia and the United States on enforcement of anti-trust law, and the ACCC would then get involved. They would look at, for example, whether there was a breach of the Franchising Code of Conduct. But ultimately the American court—if the matter went to trial and there was a judgement and, say, the franchisor won or was successful, there would be an attempt by them to have the court order from the United States court enforced in Australia. It has to be a decision by a superior court, so it cannot be a decision of the district court in New York state; that will not be enforced in Australia. But if it is a decision of a state Supreme Court in the US, it would be enforced by the Supreme Court of Western Australia. That is the way it works.

Mr W.J. JOHNSTON: Could I just explore this? How is this relevant?

Dr Underdown: I think we are getting off the track of it because the Law Society is not objecting to the extraterritorial application of this legislation. It is just an issue of cost; it just relates to the cost.

Mr W.J. JOHNSTON: Sure.

Dr Underdown: There is no issue with extraterritorial application because there are so many arrangements between the states and the federal government over the enforcement. Corporations law is a good example, but also the Franchising Code of Conduct. The states have just had to pass legislation implementing the federal legislation in many areas, so there is no real issue about extraterritoriality within Australia. Extraterritoriality overseas becomes a completely different ball game, but I do not think that is an issue for this bill.

The CHAIRMAN: Okay; let us move on to a different issue. We accept the Law Society's perspective on that, and we have all heard it. Could franchise agreements regulated by the oil code or fractional agreements that are otherwise exempted under clause 5(3)(a) and (b) of the code be caught under the bill's definition of WA's franchise agreement?

Dr Underdown: I have not looked at that issue, but I doubt it.

The CHAIRMAN: You can take it on notice.

Dr Underdown: Yes, I will have to. It is not something we have discussed as a society.

The CHAIRMAN: Just going through these issues as they turn up, are there issues with unilaterally adopting the code as a uniform national law into state-based law?

[11.30 am]

Dr Underdown: No. The code already is part of the law of Western Australia. Is that what you are asking?

The CHAIRMAN: Yes.

Dr Underdown: It is already part of the law of Western Australia. This is just supplementing—an addition to—the code to address some particular issues that this Parliament has observed.

The CHAIRMAN: Clause 9(1) of the bill reads —

> A person who proposes to be or is a party to a WA franchise agreement must not contravene the Franchising Code of Conduct (WA).

There have been suggestions that if one party has reneged on its obligation and, as a result, the agreement has been terminated, the parties would no longer be parties to the franchise agreement and therefore the bill would not apply. Can you comment on that?

Dr Underdown: To clarify, do you mean that if the parties to a franchise agreement breach the agreement, the agreement is no longer valid?

The CHAIRMAN: Yes.

Dr Underdown: It probably would depend on the nature of the breach. As in most contracts, there are breaches that are fundamental and breaches that are not fundamental. A contract does not normally terminate just because there has been a breach of it. It may terminate if there has been a fundamental breach, but not otherwise. That is just general contract law.

The CHAIRMAN: I turn to another issue. We are just going through these technical ones so that you can help us to address the issues that have been raised. What is your view of having a statutory duty of good faith as opposed to an implied obligation under common law? We understand, and we have received evidence, that under common law there is an implied duty of good faith. The bill is trying to create a statutory and defined duty of good faith.

Dr Underdown: The issue with having a statutory obligation to observe good faith is in defining what you mean by "good faith"—what the parameters of that are. You have to set the parameters. If you are within the parameters, there is no breach, but if you are outside the parameters, there is a breach, so you have to have some kind of boundary. That is the difficulty with these kinds of expressions. This is just one of the expressions. "Best endeavours" is another and so on. These are

commonly used in contracts, but often the courts have struggled with them. The Western Australian Supreme Court, for example, in one case—I cannot remember the name—actually said that "best endeavour" meant to give it a good shot or give it your best shot, and that it did not mean more than that because it is not a term that is legally defined. "Good faith" is another term that means different things to different people. The issue would be how you define it. I do not think the Law Society would have any issue with actually having a good faith requirement. We pointed out in our submission that there is no good faith obligation in the Trade Practices Act or the Franchising Code, but it is not inconsistent with either. If the bill is finally passed with an obligation to observe good faith, that will not be inconsistent, in our view, with the federal legislation or the code. The issue is how you define it. You can leave it up to the courts to interpret, but the courts around Australia have not interpreted "good faith", "best endeavours" or expressions like that in a uniform way.

The CHAIRMAN: As you know, the bill defines "good faith" with four words. We have heard evidence that the way it is worded could be interpreted as meaning these four terms exclusively, and that if we change the word from "meaning" to "including", it could include those but also others. That is the issue we have to look at about the definition. We have heard evidence that the common law has not come down to a clear definitive agreement, and that defining it in a statutory manner will remove the flexibility of the courts to interpret good faith in the context of the situation at hand.

Dr Underdown: Both those points are valid. From the parliamentary drafting point of view, it would be better to use the expression "including" because that does not exclude other possibilities. For example, in drafting agreements we always, as part of the definition or interpretation clause in a contract, say that "including" is not a limiting word. But the parliamentary draftspeople will be well aware of this. I think that is the way to get around this particular issue. If you just have four examples without using the word "including", it could be limited to just those examples. The other point—you are quite correct—is that the courts have not come down with a uniform definition of good faith. The disadvantage, of course, of leaving it up to the courts to decide is that a court in one state or one court in Western Australia may decide in a different way from another court, or this year the bench may decide a different way from how they decided two years ago.

The CHAIRMAN: Just a couple of things. We have been told that the four terms used in the bill are a distillation of the essential characteristics of the courts' interpretation of good faith. Do you have a comment on that?

Dr Underdown: That is probably correct, but, again, different courts have different interpretations and different judges have different interpretations, so I am not sure that you can actually encapsulate all the different decisions where good faith has been discussed in a judgement in just four expressions.

The CHAIRMAN: Does the Law Society have a view on this question; that is, if we were going to proceed with this bill and put in a statement of good faith, would it believe that we should define it with limiting terms—these terms—or including these terms?

Dr Underdown: Our submission does not actually say that. All we said in our submission was that we did not think any good faith provision in the final legislation would be struck down for incompatibility with the code or the federal legislation.

The CHAIRMAN: So you do not have a view on that question?

Dr Underdown: Well, the society does not. My view is that if you are going to define it, it would be better to use the word "including" so that you are not limiting the definition. That is just a drafting tool, which every parliamentary draftsman knows.

Mr P. ABETZ: Can I just ask a question on that? If it is defined in statute law, does that automatically exclude the common law aspect?

Dr Underdown: No.

Mr P. ABETZ: So the common law still continues alongside. If it is defined as four things in the statute, that would not exclude a judge from taking the implied law, as broad as whatever the case law may make it.

Dr Underdown: There are various rules of statutory interpretation. Normally a judge will look at the intention of Parliament. To use the same example, if Parliament says that good faith means A, B, C and D and does not use the word "including", the courts will generally interpret that as meaning that that is all Parliament wanted to include in the definition. If parliamentary draftspeople use the word "including", then of course that is not limiting the definition to those four points. That is when the judge has a bit of discretion. The more concrete the drafting is, the less scope there is for a judge to broaden the definition because they will say that Parliament must have intended that the definition only include these four points. That is the most fundamental way of interpreting statutes, but different judges can adopt a more expansive view.

The CHAIRMAN: As politicians, we sometimes have a hard time knowing what Parliament asks for, with clarity at least.

[11.40 am]

Dr Underdown: The judges can actually look at *Hansard*; they can look at bill memoranda and so forth to try to ascertain the intention of Parliament, and of course they can take a look at *Hansard* to see what was said in the second reading speech and so forth. But generally, in this case, if the act as passed says "good faith means a, b, c and d", then a judge would probably say, "Well, that was obviously the intention of Parliament, that good faith be limited to those four definitions."

The CHAIRMAN: Especially in the context of the debate in Parliament and the issue of whether "means" is included was discussed or debated. If the Parliament chose "means", they would say, "Well, they made a decision to restrict."

Dr Underdown: A judge would then look at that and say, "Well, obviously that is how the Western Australian Parliament wanted to define it."

The CHAIRMAN: One of the issues I have is that often politicians and laymen want to put things in law to clarify, to attempt to use words that clarify the intent of the law, but there often is a difference between the laymen's use of the word and the law's use of the word. Sometimes they can be minor; sometimes they can be significant. One of the intents of this bill is to provide a clear and concise statement of the norms of conduct required of franchisors and franchisees by reference to the four key concepts in the bill. The argument is that these terms can be used in case law and the legal literature in Australia and overseas. We have received evidence that, if you put these things in, it would define up front that both parties had to act in good faith in these terms, and they would be a combining area—"fairly" is one of them. Do you have any comments on that?

Dr Underdown: I think what you said is correct, but a word like "fairly" is open to so many different interpretations. What does "being fair" mean? In drafting—I do commercial drafting obviously, because Clayton Utz is a commercial law firm—we try to avoid those kinds of words which have a lay meaning. In the case of "fair", if you ask someone who has watched a football match, after the match, "Was the umpire fair?", or "Did this player behave fairly?", you will probably get 100 different views of what is fair and what is not fair. It is not a good idea to use words that do not have a very precise meaning in legislation.

The CHAIRMAN: What about "cooperatively"?

Dr Underdown: I think that is a bit narrower than "fairly". The parliamentary draftspeople of course are thinking about these kinds of issues when they are drafting. I have worked in two Parliaments, including the federal Parliament, so I know how the system works. Obviously the members of the committee also discuss their understanding of these words. If you are going to seek to define precisely expressions, you need to give very careful thought to whether the words you are

choosing in your definition can be ambiguous, because that is working against your desire to be precise in the definition.

The CHAIRMAN: The four terms are "honestly", "reasonably", "cooperatively" and "fairly". We have discussed "fairly".

Dr Underdown: "Fairly" is the most imprecise of the four terms; I think the others are more precise.

The CHAIRMAN: "Reasonably" is a very commonly used term.

Dr Underdown: But legally it does not really mean very much. Again, what is reasonable for one person may not be reasonable for another.

The CHAIRMAN: It is kind of like a word that allows a judge to make an expansive decision.

Dr Underdown: Yes. It comes down then to how the judge decides. The issue is that one judge may have one view and another judge may have another. At the same level of the same court, that is an issue. It is not an issue if it is a judge in a higher court, because then the judge in the lower court is going to follow that interpretation.

The CHAIRMAN: Do you think these terms that have been primarily chosen to communicate are an effective communication tool to the parties to the contract in a franchise arrangement? Will it affect their behaviour? That is, these four terms are put in there, and the aim of the bill is to provide guidance to the parties, recognising there is a contract between them already. This is the overriding guidance to the formation and operation of the contract between them. Do you think that is an effective communication, particularly as it transcends, if it does, from the contract to the courts?

Dr Underdown: Yes, I do. I am assuming that most people who enter into franchise agreements on both sides want to behave honourably and do the right thing. The franchisor wants to run a good franchise business; the franchisee wants to run their own business with the help of the franchisor—the advertising power and so on of the larger body. The problem is with the mavericks in the industry. They are not going to be influenced very much by your definitions, but the good people will be. The very fact that the Western Australian legislation will set out what we mean by "good faith" and "proper behaviour" in entering into the agreement, I think will influence both sides of the agreement.

The CHAIRMAN: Besides the rogues, from the evidence I have seen, most of the problems of disputes come up when something goes wrong with either party. The franchisor goes bankrupt, the franchisee's operation does not work, runs into cash flow problems and whatnot—the proverbial hits the fan, on either side. It is hard, from my reading of what the facts are; I am not across them. Would this help in resolving those disputes when they are tensions on one side, which is often the case, besides the few rogues?

Dr Underdown: There are dispute resolution mechanisms now in franchise agreements. I think these definitions are more useful in entering or the negotiating at the beginning of the franchise agreement, rather than when something goes wrong during the franchise. The things that go wrong—in my experience there are a lot of issues with exiting a franchise. Some of those issues relate to tying leases to the franchise agreement. That is something that the federal parliamentary inquiry into the franchising code looked at.

There are actually some franchisors who do not seem to be running franchises for genuine purposes, who do not seem to care whether the franchise does well or not. One of the indicators of this is that they are constantly trying to get rid of franchisees before the franchise term is completed, often on fairly minor grounds, and then they are just recycling a new franchisee into that particular business. That way they get more money up front—they keep getting money up front from the new franchisees. In my view, that is not running a genuine franchise business. That is a minority. That is not the way that most franchises are operated. I think in most cases, as in any business, there can be

disputes over payment or advertising or buying stock or something like that. I think in the last couple of years that has all been tightened. The dispute resolution procedures are quite well defined, but I do not think having this particular definition is important once the franchise is underway. It is more important when you are looking at entering into a franchise agreement and at the actual signing stage.

[11.50 am]

Mr W.J. JOHNSTON: I want to go to a new topic, if that is all right. The question of retrospective operation of the proposed bill: is the society's position that the bill means that the terms of the contract will now be different, and that is what you are saying is retrospective; or are you saying there is an enforceable right in respect of previous behaviour, because they are two slightly different things?

Dr Underdown: It is more the latter. The Law Society, and I think law societies around Australia, are totally opposed to any retrospective legislation. It is a fundamental issue—people should know the law they are supposed to have broken. Our thought is this bill, if it was passed as it is, could apply to conduct that just happened in the past rather than people knowing from the date the act enters into force that this is what is going to apply. That is really ideal.

Mr W.J. JOHNSTON: Would that be resolved by a provision that said, just as an example, that the rights—whatever the words would have to be—cannot apply to an act that occurred prior to the bill coming into operation?

Dr Underdown: When we discussed this in the commercial law committee of the Law Society, I said that I thought clause 4(2)(a) of the bill should be amended to read "when it is entered into after this Act commences". That covers the point I was just making.

Mr W.J. JOHNSTON: Could I just clarify that, because that would then say that a new franchise agreement would have these provisions apply, but not an agreement that is currently on foot?

Dr Underdown: Not a current agreement, but if the agreement came up for renewal, obviously the new provisions would apply, and it would apply to any agreement entered into after the commencement date.

The CHAIRMAN: To clarify this: let us say there is a simmering dispute under an existing franchise contract between parties. No legal action has been taken by either party in this case. We pass that bill with your suggested amendment—could those disputes or disagreements under the old franchise arrangement be looked at if this bill was passed?

Dr Underdown: They would have to be dealt with under the previous legislation, but that is the way the law applies in every other area too.

The CHAIRMAN: The Law Society's concern is that the way this is drafted might allow disputes that have not been brought to the courts—disputes between existing contracts—to be looked at under these changed laws?

Dr Underdown: That is the way we believe the bill can be interpreted.

Mr W.J. JOHNSTON: Can I clarify that? There are many examples of course where the Parliament confers additional rights on contracted parties. An example would be industrial law where there has regularly been changes and often the provisions say—take unfair dismissal as the classic example—on 1 May the unfair dismissal law changes. If you were terminated on 30 April you have no action, but if you were terminated on 2 May you have an action. We are currently dealing with commercial tenancy provisions where rights will be extended from the date. I can understand an argument that says—let us take the unfair dismissal case as an example—that you are not extending a right to somebody who was sacked the day before the bill came into power but you are still interfering in the contractual arrangement between the other parties from that moment forward. To that extent the contract is being interfered with.

Dr Underdown: There are two approaches to this. One is that it does not apply to any existing contracts, but when the contracts come up for renewal, or a new contract enters into force, the new legislation will apply. The other approach is that it will affect the previous or existing contract in the event that legal proceedings are initiated, which is the point you are making.

The CHAIRMAN: What is the Law Society's view on the choice between those two, in this case?

Dr Underdown: I think the Law Society would prefer the legislation did not apply retrospectively at all. There is certainly the possibility that you could have a provision that any legal proceedings currently on foot will be under the previous regime but any initiated after the commencement date will have to follow the new legislation. That picks up the point you just made.

The CHAIRMAN: The case that Bill makes relates to industrial law, but industrial law is different in some ways, maybe—I am starting to explore it to find out some precedent. The case that Bill just raised is clear. It is a major part. I would imagine other aspects of law would do the same thing—tax does.

Dr Underdown: Occupational health and safety, I suppose, is a little bit different to franchise disagreements in that it affects people's actual life or health. That may be why we are a bit stricter in those areas. Because I am a maritime lawyer, I am only familiar with how these issues apply to seafarers. That is very widespread in those kinds of areas—occupational health and safety areas—that the legislation applies from the day it commences to any proceedings which are started after that date.

The CHAIRMAN: In other areas, such as straight commercial law, it is usually the case in Australia where the law applies to new contracts.

Dr Underdown: Yes, the law applies to new contracts. Most disputes do not end up in legal proceedings. Perhaps 10 per cent of disputes actually go to court, but then probably 90 per cent of those either settle on the day of the trial or at the last minute. It is only a very small proportion of all disputes that actually end up in court.

Mr W.J. JOHNSTON: Indeed most of these franchise agreements would be on foot for the whole term without dispute —

Dr Underdown: Yes, the majority work out quite well. There are some particular franchise areas where there are more disputes than others, but that is the same as in some industries like the taxi industry or construction industry, which have more disputes too. The majority of franchises work reasonably well; both parties get what they want, I guess.

Mr P. ABETZ: With the requirement to act in good faith, it is actually about conduct rather than the contract. We have heard from a number of franchisors that they would not need to change anything in their contracts because nothing has changed with this, but it is about how they conduct themselves from here on in. Can you explain why that would still be regarded as retrospective in the sense that it is only from when that bill is enacted anybody who does not act in good faith after that date is actually in breach of the law; anybody who is not acting in good faith three months ago or 10 years ago is not in breach of the law because it was not enacted then? Can you just clarify that for me, please?

[12 noon]

Dr Underdown: Normally, "good faith" is an expression which is used in contractual negotiations; the actual negotiations. It is only fairly recently that financial institutions, like banks and other lenders, had to actually say to a client, "You should get independent financial advice before signing this contract or this loan agreement." That is a fairly recent change. Good faith in negotiations is a similar kind of approach; we both come to these negotiations with a view to being honest with each other and disclosing what we need to disclose. The franchisor will disclose what the franchisee needs to know to make a decision about whether to enter into the agreement; the franchisee will

disclose that it is bankrupt or whatever. Good faith applies normally at the beginning, or prior to the signing of the actual agreement, but also it applies to decisions made during the term of an agreement, such as decisions about opening new businesses under the franchise agreement. The franchisee may expect at the beginning that they will be the only franchisee in Perth, and they may discover, down the track, that suddenly they are competing with six other businesses in Perth, or, in a case I know about that has not gone to court but potentially could, the franchisor is actually competing against his own franchisee, contrary to the franchise agreement. There has to be good faith during the term of the franchise agreement as well as at the beginning, but it is at the negotiating stage when it is most crucial, because it affects the actual decision to sign the agreement. Did that answer your question?

Mr P. ABETZ: Yes.

Mr W.J. JOHNSTON: You said there has to be good faith.

Dr Underdown: I mean in a common law sense.

Mr W.J. JOHNSTON: Yes; that is what I am exploring. How does one go about knowing, firstly, that there is good faith and enforcing your obligation to be treated with good faith?

Dr Underdown: It is notoriously difficult. Basically, you are trusting each other—this is common law now—and generally you do not discover until later that somebody has not acted in good faith or they have not told you everything they knew, and then it comes down to whether you asked specific questions. If you are dealing, say, with a real estate agent and the real estate agent says, "This is the best house in the best street in town", the courts say that that does not mean too much. But if you ask the real estate agent whether any plumbing work has been done on this house in the last two years, and, if so, what work was done, and the real estate agent knows plumbing work has been done and does not disclose that, then the courts are likely to say, if the dispute goes to court, that the real estate agent has not acted in good faith because they have a duty to disclose. There are statutory duties in the real estate industry about disclosing, too, but generally people do not have to volunteer information, but if they are asked specific questions and it is within their knowledge, they have to answer truthfully. But it is notoriously difficult to litigate for breach of good faith because the burden of proof is quite difficult in that, how do you prove that somebody was acting without good faith? That is where this definition of good faith comes into it.

The CHAIRMAN: Would this definition help, in your view?

Dr Underdown: You could definitely argue in court that one of these four conditions was not met, but then if I was acting for the accused I would probably ask what "reasonably" means. That is the issue. Obviously, it helps to be able to point to these key indicators.

The CHAIRMAN: Could the wording of clause 12(2) on civil monetary penalties allow for double jeopardy? Opponents to the bill state that the wording allows for an order for payment to be made prior to the conclusion of an ACCC investigation that may also result in an order for payment being made, thus exposing the person to double jeopardy.

Dr Underdown: I do not think that would happen because the Federal Court would know that there was a previous order and would not impose a second order for the same offence. I just do not see that happening. If that has been raised with you, I think it is very unlikely that that would happen. In general, of course, the Law Society would be opposed to double jeopardy.

The CHAIRMAN: What about if a state commissioner with statutory powers under the state opposed a penalty on a party, and the ACCC then subsequently imposed a parallel penalty; is there a concern about that? Would the Federal Court also take the first —

Dr Underdown: Yes, I think the Federal Court would. The penalty is only imposed by order of the Federal Court, so obviously counsel for the defendant would say, "Well, the Western Australian

commissioner has already imposed a penalty of such and such an amount for this breach", and the Federal Court would not impose a parallel penalty.

The CHAIRMAN: Opponents of the bill state that exposure to fines of up to $100 000 for civil breach are unprecedented, particularly as no penalties exist under the Competition and Consumer Act for the more serious infractions of misleading and deceptive conduct. Are you able to comment on that?

Dr Underdown: I am not sure if those submissions were made in knowledge of the penalties that apply to cartel offences under the legislation. Individuals actually now face not only fines but also criminal sanctions of imprisonment for up to 10 years.

The CHAIRMAN: But I think they were comparing this one with misleading and deceptive conduct, which is kind of related to acting without good faith.

Dr Underdown: Yes, but cartel offences are acting without good faith, too. If you get fined, as in the Visy case, in the tens of millions of dollars and the directors can go to jail, I think, fines of $100 000 are not really excessive. Sorry, that is not a Law Society opinion; that is just my opinion.

The CHAIRMAN: The whole intent of this is to basically help franchisees who often are pretty small, and there is often a so-called imbalance of power between the franchisees and the franchisor. Franchisees often get into a franchise because it is an easier way to get into business without starting from scratch, and the evidence is that many of them do not have a great deal of experience in business. Also, the indication is that they are often heavily in debt—I do not have any data on that actually, but nonetheless—and so there is this imbalance. We have been told that one of the fundamental problems with these types of dispute is the lack of access to the courts because of the financial constraints faced by franchisees of accessing courts against a franchisor. Can you comment on that; and also, if you can, does this bill help?

Dr Underdown: On the first part of your question, in most cases there probably is an imbalance. There are some cases of some of the fast-food franchises where the franchisees are actually companies in their own rights with quite considerable strength, but in general—say it is a coffee shop or something like that, or a party supplies business—there often is this imbalance of power. But you do not want to be encouraging franchisees to think only in terms of going to court. There are plenty of other avenues open to them, and the first step is to go to the department for consumer affairs, or even to local legal services that exist in many suburbs.

[12.10 pm]

They will not necessarily have to face court without any assistance or at their own expense. I do not think the legislation should be driven by what it might cost somebody who is a weaker party to actually go to court, but more generally in Australia as a whole the more money you have, the better your chances are of getting good legal advice and paying for top counsel and so on and going to court. That is just the nature of our legal system. But that is not specific to franchises. That is the weaker party in general.

The CHAIRMAN: As I understand it, the bill envisages a state entity acting on behalf of a party, whether it is franchisee or franchisor, to take action on that complaint that you have.

Dr Underdown: That was the second part of your question, which I did not answer, and that is an example of how this legislation does help the weaker party.

The CHAIRMAN: So that is the intent. One issue from a state perspective: what would be the potential cost for that? Would it open a floodgate? Of course, on the ACCC, my understanding of the case is that they ration or they have the right to pick and choose, and the complaints are that they do not pick enough.

Dr Underdown: That has been my experience both with the Commerce Commission in New Zealand and with the ACCC here; that is, they very much pick and choose. One of the arguments of

insiders in Australia is that they pick cases that they think they are going to win for a start, but then so does the ATO and ASIC and every other government regulator too. But the argument also has been—under Allan Fels in particular, but also under Graeme Samuel—is that they have sort of favourite areas that they target and also that they support cases that they think will show the body in a good light or give them kudos with the government or help get them extra money in the budget. People say this about all areas of government too; that is not just confined to these. This is not a Law Society view, but, in my view, that is a reason for not having regulators also prosecuting. I believe very strongly that the two should be separated.

The CHAIRMAN: What you would do in this case?

Dr Underdown: I think that if the ACCC has a case—I am not talking about the commissioner in Western Australia but the ACCC—they should go to the DPP or the Commonwealth Director of Public Prosecutions and let me them make a decision on whether to proceed or not. I do not think the decision should be made by the regulators. That is just my personal view, but I think customs operates in a much fairer way by basically issuing infringement notices for breaches of the Customs Act. I think that is a much better way of getting compliance than prosecuting.

The CHAIRMAN: If a party gets an infringement notice from customs, they can go through the courts to challenge it.

Dr Underdown: They can challenge it if they want to—that is up to them—but in most cases people pay up because it is a fairer way of doing things. They have not been dragged through the court and customs has not had to spend a huge amount of money on enforcement and prosecution and so on. But I think the commissioner here—well, whether it opens the floodgates or not I do not know, because my view is that any problems that arise during a franchise agreement settlement can be negotiated between the parties. Again this is where good faith comes into resolving disputes too. You want to have good faith on both sides. We basically want this dispute to be settled so we can get on with our business. So that is another argument for why good faith does not apply just at the beginning. So I think that is how most disputes are settled, but obviously there are some that are intractable because the parties do not want to resolve amicably. I do not think it would open the floodgates, but it is very hard to say up-front what it would cost. Again, the Department of Commerce may have some figures on how many consumer disputes it gets and how much they cost to resolve, but I suspect in most cases that they are resolved again through negotiation.

The CHAIRMAN: Since this issue has come around, they have made changes to the code that came into place in July 2010, and then the Australian Consumer Law has been revised significantly and has been gazetted on 1 January this year. One argument is that before we do anything, we would like the dust to settle on these changes—that is, the changes to the code and the changes to the operation and interpretation of the Australian Consumer Law. Do you have any comment on that?

Dr Underdown: That sounds like a classic case of *Yes Minister*. It is the public service attitude of "Let's wait and see and not do anything". I do not think that is a reason for the Western Australian Parliament not to act. If you think that this legislation is the correct way forward, then I think you should proceed with it and not worry about giving the new consumer legislation or the replacement of the TPA six months—how long do you give it to operate? There might not be a lot of court cases for the next two years, so it could be quite a lengthy period before you build up enough case law or enough experience of how the new legislation is going to work. So I do not think that is a reason for not proceeding.

Mr P. ABETZ: On the imposing of penalties issue, the submission says, "which could prove to be difficult to enforce". That is on page 4. I am just wondering what the Law Council envisages as being difficult to enforce. What is the issue there?

Dr Underdown: That relates specifically to the extraterritoriality aspect. If a Western Australian court imposes a penalty on a franchisor in, say, Queensland, to enforce it you are going to have to apply to have it enforced in Queensland by the Queensland courts. There are additional costs there and so forth, and time as well. That is what that refers to.

The CHAIRMAN: We will close it there and make a closing statement. Thank you, Dr Underdown, for your evidence before the committee. There are a number of questions that we have not been able to ask you today, and Tim here will get in touch with you. Would you be willing to answer to a series of these further questions that the committee can provide by writing?

Dr Underdown: Yes.

The CHAIRMAN: A transcript of this hearing will be forwarded to you for the correction of minor errors. Please make these corrections and return the transcript within 10 working days of the date of the covering letter. If the transcript is not returned within this period, it is deemed to be correct. New material cannot be added via these corrections and the sense of your evidence cannot be altered. Should you wish to provide additional information or elaborate on a particular point, please include a supplementary submission for the committee's consideration when you return your corrected transcript. Thanks very much, and for your society's views—very helpful indeed.

Hearing concluded at 12.18 pm