ECONOMICS AND INDUSTRY STANDING COMMITTEE

FRANCHISING BILL 2010

TRANSCRIPT OF EVIDENCE
TAKEN AT PERTH
MONDAY, 4 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 11.18 am

KEANE, MR WILLIAM ARIE SCOTT
Member, Competition and Consumer Committee of the Business Law Section of the Law Council of Australia, examined:

RUSSELL, MS SARAH ELIZABETH
Deputy Chair, Competition and Consumer Committee of the Business Law Section of the Law Council of Australia, examined:

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

The Witnesses: Yes.

The CHAIRMAN: Do you understand the notes at the bottom of the form? I should not need to ask two lawyers about that!

The Witnesses: Yes.

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

The Witnesses: Yes.

The CHAIRMAN: Do you have any questions regarding your appearance here today?

The Witnesses: No.

The CHAIRMAN: The committee has received your submissions; thank you for your contributions. Do you wish to propose any amendments to your submission?

The Witnesses: No.

The CHAIRMAN: Before we ask any questions, do you wish to make an opening statement?

The Witnesses: No.

The CHAIRMAN: Just a question: your organisation is a national one with local, state and territory branches, but you are representing the national organisation?

The Witnesses: That is correct.

The CHAIRMAN: You understand that the focus of this committee is the proposed bill to regulate or change the regulation relating to the franchisees–franchisors. I presume that you have gone through the bill. Could you give a synopsis of whether the bill is appropriate; and, if so, why; if not, why not; and where?

Mr Keane: The first thing to point out is that as a large organisation comprised of a considerable membership, it is important that when we are responding to your questions today on behalf the committee, we do not exceed the scope of what the committee is committed to provide a contribution on. To that extent, we are a bit limited, and I apologise if that sounds somewhat lawyerly, but I think the word "appropriate" takes us a little bit outside the scope of what we looked

at. We looked specifically, and the committee looked specifically, at the terms of reference of this body and responded to the specific questions that were asked. But if I could perhaps interpret your question in a way that more directly reflects the terms of reference, the committee was of the view that the bill does not promote the policy aims that it purports to address; it would not be effective to promote the policy outcome that is explained in the explanatory memorandum.

Mr P. ABETZ: In your submission on page 4, it says that the bill does nothing more than provide two new different bases for enforcing obligations that franchising parties already owe and introduces new obligations, the duty to act in good faith. My question is that on the previous page, on page 3, you believe that the good-faith provision of the bill would create confusion amongst franchisors and franchisees. Could you explain how you envisage that confusion occurring given that franchisors and franchisees, according to your own paper, actually already have a common-law obligation to act in good faith? Justice Rein, in New South Wales I think it was, has ruled in two cases now and I quote from his ruling. It states —

> … I summarised the submissions made on behalf of the franchisee in that matter, which I accepted as to the content of the duty of good faith. In short, and relevantly, the franchisor is required to act reasonably and honestly —

These are the two terms that we put in our definition in the bill. The ruling continues —

> (to an objective standard), not to act for ulterior motive, —

Which I guess we could say means fairly. The quote continues —

> to recognise and have regard to the legitimate interest of both parties in the enjoyment of the fruits of the contact, and to avoid rendering the franchisee's interest under the agreement nugatory or worthless or seriously undermining it …

Which in common language means cooperatively. So, the four adjectives that we use in the bill would seem to summarise what Justice Rein says is the common-law obligation. My question is: why do you not envisage using the definition that Justice Rein has ruled is the common-law obligation into law so there is no confusion? You are saying that it would create confusion. Could you just clarify your thinking on that?

Mr Keane: Yes, and it is a legal answer. The difference lies in the distinction between the application of a concept in mandatory statutory terms and the application of a concept by a judge when applying common law in a decision on the facts of a particular case. Legislation applies, to an extent, in the abstract. A judge applies the common law to the particular facts of the case. When there is a blunt application of words that might have been used in case law, without qualification, in statute, and where consequence of contravention is a pecuniary penalty, as in this case, the legislation operates—these are my terms not the committee's—I would describe that as acting as a bit of a blunt instrument, whereas the judge uses the law more like a scalpel. Given the consequences and given the existing law, the committee felt that the application of these concepts in a statute in this manner would create confusion and create an environment for dispute.

Mr P. ABETZ: Excuse me, Mr Chairman; can I explore this a little further? Putting myself in the position of the franchisee or franchisor, if I know that I have, by statute law, the obligation to act fairly, honestly, reasonably and cooperatively, that is clearly stated, then I know that the everyday language of what that means and the opinion that Daryl Williams QC has provided, which is on the website, in the submissions, indicates that that is a—I cannot remember the exact words that are used now—but basically he says it is a good summary of the terminology and it actually clarifies it. So, I am struggling to understand why it creates confusion when every time a franchisor or a franchisee goes to court and has some sort litigation, if the franchisee or the franchisor wants to say that good faith does apply in this case, every time, there has to be some significant time taken of the court in legal arguments as to whether good faith applies in this case, yes or no. In the Trade Practices Act, in the unconscionable conduct area, it says that it may take into account good faith.

So, the litigants are never sure whether good faith actually applies; when they are out in the marketplace they are never sure whether it applies. By putting it into statute law, we would make it absolutely clear and there would be no confusion and no need for litigants to argue and take up more time. They can simply say, "This is the standard of conduct that we expect in a franchisor–franchisee relationship." Can you explain why that should be confusing for a franchisee and why that should lead to more litigation rather than less?

Mr Keane: I would imagine that there are lot of responses to that. The first one that leaps to my mind is that already we have an unconscionability provision that has a pretty important consequence of breach. In fact, as a result of the Australian Consumer Law, it now gives rise to pecuniary penalties. Just as I could imagine a layperson looking at the word "unconscionable" and saying, "Well, I know what that means; I understand what I can't do", you might just as easily look at the elements of the good faith concept and reach the same view and say, "Well, I know what those things mean." But as we all know, business has not necessarily responded to the unconscionable conduct provision in quite the same way. A lot of people would say that they are confused by that concept as well. I should clarify that the committee's submission does not address unconscionability, so when I am speaking to unconscionability I do so in my own capacity as a solicitor. I think you can always make an argument that that particular kind of law, a particular word used in law, might give rise to confusion. In this case, I think we are looking at a concept where if you look at—you have cited one particular case—but if you look at many of the cases there is no great uniformity through the cases of precisely how to apply these concepts in practice. The beauty, I think, of case law, of common law, is that a judge is able to apply those concepts with nuance.

[11.30 am]

Yes, that means that people engaging in conduct where there is a dispute might need to litigate in order to settle the dispute. But there is a predictive analysis that people make as well, and that is where in fact you would argue most of the law is in fact administered. It is in the predictive process of people looking at their conduct, looking at the law, taking advice if they need it and deciding on a course of conduct accordingly. Parliament tends to need to balance, I suppose, the certainty of the terms of legislation it uses and the flexibility of those concepts. If you choose a concept which is very flexible, then it can be argued that it could lead to confusion or misunderstanding and therefore needs resolution by a court. If it is very prescriptive and precise about what would contravene it, then you have to consider whether it might catch conduct that should not appropriately be the subject of a contravention.

If you look at the Garry Rogers case—the Subaru dealership case—that was a case in which Justice Finkelstein looked at both unconscionability and good faith and found that in fact the conduct would not in that case be regarded as not being in good faith. It defended the application of a concept in the common law, but when you read the judgement, what he does is engage in a much more nuanced application of those words and concepts that you have quoted than a piece of legislation would allow. There is a serial list of adjectives of conduct. You find yourself not having acted in accordance with one of those adjectives and, bang, you are in breach and a pecuniary penalty is the consequence. That is different from a judge looking at the conduct and also considering, for example, whether a party is acting in accordance with their own commercial self-interest. There are no balancing factors in the proposed legislation. The common law provides for balancing factors. So a court will use the concepts in a much more nuanced way. I suppose that resolves the dilemma that you have suggested. That resolves the dilemma in favour of justice. Speaking for myself, I think that is an appropriate balance of things, to allow a court to do that rather than to provide concepts which, your characterisation is, are clear and certain. I think our submission makes clear we do not necessarily agree with that.

The CHAIRMAN: Let us take an issue and explore whether a term to a layman might be clear, to a court of law it might be open to interpretation: "cooperation". In business you compete and you cooperate. In a franchise, you do both—there is always a bit of competitive tension between the franchisee and franchisor, but there is also obviously some cooperation. Could you explore, if there is some case law or otherwise, where a judge is trying to interpret that, where if we had this good-faith clause and it said that you have to cooperate and you could basically say that they were more competitively cooperative, as opposed to, let us say, as in place now under common law where you can nuance all these things. Could you explore that a bit, because to most laymen " cooperation" appears to be understood?

Mr Keane: Yes, and if it is understood in very simple terms, you might say that is in direct conflict with ordinary commercial relationships. Some commercial relationships are zero-sum games, so there will always be a degree of conflict between the interests of people contracting. In fact the basis of law of contract is in fact to resolve those conflicts. What you have described is a balancing process between the cooperative elements of contract and the elements of contract that are all about resolving conflict.

Perhaps it is worth going back to where the common law duty, at least on my research, first came substantially into our law, which is the Butt and McDonald case, which is referred to in the submission. I think in those cases the idea is that cooperation is one of the things you look at to work out whether a party has acted in good faith, but it is considered against other factors. It is not as you suggest and it is not as this legislation, I think, would apply the concept. A judge is able to balance the kind of cooperation that you might regard as the parties pursuing to share the fruits of the contract, and that is the origin of the concept that cooperation has an origin in the idea that contracts are cooperative contracts; they are about sharing the fruits of the contract. But, as you pointed out, there is a tension between that and what each party in their own self-interest seeks to obtain through the contract. If you simply place an unqualified obligation to cooperate in circumstances where there will necessarily be, in commercial relationships, conflicts, that is a recipe for dispute.

Mr P. ABETZ: Is that not something that a judge, weighing up the situation, would determine—to what degree cooperation is appropriate, particularly given that franchising is very different to normal contracts in that it is an ongoing relationship? It is based on trust, and I do not think I have ever come across in business any contract which has within it that the franchisor, the one party, can vary the terms of the contract at any time at their total discretion, which is part of just about every franchising contract. A franchisee signing up to a franchise contract has a contract where the franchisor has that total disproportionate power. That is what every inquiry going back from 1974—I have a whole list there that the CCI has put together—pointed out, that this anomaly in franchising has given rise to this huge problem that we have. Therefore, because the franchisor has that enormous power, there must be a legal obligation to act cooperatively, because otherwise it cannot work.

Mr Keane: We are not here to comment on the bargaining power between franchisees or franchisors or in fact on the policy problem itself. What, I think, the submission says is that if you take those problems with franchisees as read, the question is: does this legislation advance or not advance them? Our view is that, if one agrees and accepts the policy objective of this legislation, an examination of its actual terms suggests to us as lawyers that those objectives are not advanced by this legislation. When you described what a judge would do when faced with a particular situation, that is exactly why the common law performs such an essential function in Australian business. There are things legislation is not well adapted to doing—concepts that legislation is not well adapted to putting into practice. Speaking for myself entirely, I think sometimes we have a tendency to see a problem and assume that legislation is always the way to deal with that problem. Sometimes it is; sometimes it is not. Speaking for the committee in relation to this particular legislation, the committee looked at these concepts, looked at the manner in which they were put in

place by the legislation and concluded, as in fact did the commonwealth, that these concepts are not well adapted to being applied directly by statute in this way.

Mr P. ABETZ: Did you do any research at all on how the legal requirement to act in good faith is working in the United States and Canada, where it is has been legislated? There is a paper by Peter Macrae Dillon, who, according to Evan Carmichael's website, is one US's most respected franchise attorneys. It appears to be working extremely well, and it has actually afforded significant extra protection. He makes the interesting point in this paper. Because people say it is difficult to define what "good faith" actually is, he makes the point that the courts in the United States and Canada have never tried to define exactly what good faith is. He says:

> In fact, most cases dealing with breaches of the good faith requirement involve the plaintiff party trying to establish an act of bad faith …

From what I have been told—there is no research data I can use to support this but certainly the anecdotal evidence from my contacts in the United States and Canada in franchising indicate—that has been a very useful addition to the legislative regime and that it has actually strengthened franchising because it gives the franchisee a very clear basis on which to go to court on if the franchisor is doing the wrong thing. Have you done any research on the US, Canada issue?

Ms Russell: Perhaps I could answer that one, and please, Bill, chip in if you have something to add. We did not do any research outside of the franchising bill and the terms of reference. We very much focused on that, so just to clarify that point. Perhaps if I could also just echo some of the things that Bill has said with regard to your earlier point about certainty and the words. Whilst I appreciate—and I say this on my own behalf, although it is reflected in the submission of the committee—that whilst certainly there are ingredients in various decisions that the courts have made about what is good faith or when someone acts in bad faith then you do have those words of "fairly", "honestly", "reasonably" and "cooperatively", by no means is that the end of the matter. I also consider that it is too prescriptive to try to confine good faith as a concept, which indeed is still evolving certainly in Australia. When you look at all of the case law, particularly in relation to franchise agreements—and it has been considered often together with unconscionability; the two do generally go hand in hand—it is not a one size fits all. Very much, as Bill has said, it is a case of the judge looking at the particular circumstances of the case and the facts of that case but also the terms of the agreement between those particular parties and what they have actually bargained for. Again, I appreciate that with franchise agreements there is perhaps a power on the part of the franchisor to be able to terminate or vary terms somewhat unilaterally, although there are generally provisions in agreements that counter that to a degree, but there is of course also the commonwealth code of conduct for franchisors which already applies Australia-wide and does seek to address that to a degree.

I think there is a problem in trying to confine good faith to a statutory obligation that imposes on a mandatory basis obligations using those particular words. I do not think it is necessarily a problem with changing the definition or looking at what other words you might introduce. For example, we spoke briefly about the word "cooperatively", but particularly not just in franchise or commercial contracts but in a whole area of the law there is huge uncertainty around being able to just say definitively what is reasonable. What is reasonable in one case may be unreasonable in another, and it always depends very much on the particular circumstances of the case. Whilst it might seek to give some certainty by allowing a franchisor or a franchisee to understand that they have to act fairly, honestly, reasonably and cooperatively—and the way that is worded suggests it has to be all four—it may be that in determining what in any particular case is fair, honest, reasonable and cooperative is not so straightforward. I think that may give rise to some confusion during the term of the franchise agreement as to whether in fact there has been a breach of the good-faith obligation, because obviously people are in dispute because one party might think the other has acted unfairly or unreasonably but the other party certainly does not agree with that. I think you would still find

that the parties end up going off to court to get a determination as to whether one party or the other has acted in any of these ways.

Mr W.J. JOHNSTON: Can I just clarify that particular answer? What your submission is and, as I understand it, your commentary today is that that can happen today. What is the difference between defining the term and not defining the term if it applies anyway?

[11.45 am]

Ms Russell: I think the problem with seeking to define the term —

Mr W.J. JOHNSTON: Sorry, and it is dealt with in other legislation; for example, industrial laws already have the concept of good faith included.

Ms Russell: It is. I think the difficulty with being prescriptive with an obligation of good faith is that—it is certainly my view, and I think this is reflected in the view of the committee and in the submission—it is not a one-size-fits-all approach. It will not necessarily apply to every circumstance. Bill touched on this before —

Mr W.J. JOHNSTON: Sorry, I do not understand that. I thought you said that by implication the good faith provision applies to the common law.

Ms Russell: It does, but whether someone acts in good faith or not —

Mr W.J. JOHNSTON: Will need to be determined.

Ms Russell: —is a matter for determination.

Mr W.J. JOHNSTON: Sure, but the obligation sits there, regardless.

Ms Russell: Yes. My point is whether it is enough to just have a defined term—that "good faith" means to act fairly, honestly, reasonably and cooperatively—or whether there may be more or less to it in a particular case, depending on the circumstances. The other issue that touches on this, which Bill also raised, is the franchising cases that have an implied obligation of good faith built into the franchise agreement, or that are open to do that, at least, but for which a breach of the good-faith obligation has not necessarily been found. We have also recognised that, in a commercial contract, a party may act in its own self-interest or commercial interest, which the other party may conceive as unfair to it but which that party is fully entitled to do in that particular situation, whereas in another situation that may not be the case.

Mr W.J. JOHNSTON: I appreciate that. As you rightly said, the contracts are necessarily about conflict. I can understand why you say you should not define "good faith" but I do not understand what the issue is if it is implied anyway. Either it is part of the process or it is not. If it was to be written into the Franchising Code of Conduct, would that make it good?

Ms Russell: I think when the commonwealth looked at that they decided against writing it in.

Mr W.J. JOHNSTON: Yes, but let us assume they change their mind. This is hypothetical; we are just discussing matters. The fact that they have rejected it does not mean that they will not accept it in the future. Are you saying that if it were included in the commonwealth code it would be a bad decision?

Ms Russell: I am not sure I would go so far as to say it would be a bad decision, but I do not think it would achieve the objectives of what the code seeks to address in terms of the relationships between franchisors and franchisees. It needs to be dealt with depending on the circumstances of each agreement.

Mr Keane: If I can just add to that, the committee does not necessarily oppose the good faith concept. It points out that the concept is evolving and there is not unanimity among the Australian courts about how exactly it is to be applied. When you look, for example, at clause 11 of this legislation, you can see that a number of choices are being made about the expression of the

concept. First of all, you are making a choice that you will apply the elements that have evolved over time of a good-faith concept in not an inclusive list but an exhaustive list, and you apply them serially so that all of them must be present. You do not provide for any balancing of that requirement against any other kinds of considerations. If you look at other examples of recent legislation, such as various provisions of the Competition and Consumer Act, you see that sometimes they say "the following factors". A legislator might decide that factors will be applied or weighed against each other to determine whether a particular standard has or has not been crossed. That is not the case here. The committee's response in its submission, and our response on behalf of the committee today, is very much about this particular application. Members of the committee might well agree or disagree about whether good faith as a concept in a particular way might be appropriately introduced to a legislative scheme, but that is not really what we were asked to address, and it is not what we have addressed today. Where you have an evolving concept that is somewhat controversial and you have a commonwealth scheme that does not apply it, and where you have the application of pecuniary penalties as a consequence of the contravention of that concept, we think that what arises from that is dispute, confusion and compliance costs for corporations seeking to adhere to the standards of conduct that are required by legislators around the country. All that tends to suggest to us that even people who have great sympathy for the interests of franchisees may blanch at the potential consequences of applying these concepts so bluntly and so directly.

Mr W.J. JOHNSTON: Could I just follow that up? A number of the submissions that are all published are from franchisors complaining about the behaviour of franchisees; for example, taking intellectual property and moving to another business. Clearly that is bad faith. Surely a franchisor would want the protection to enforce good faith on the franchisee. Is that not something that, as public policy—we are interested in public policy—is an important public policy outcome?

Mr Keane: I cannot speak for the interests of franchisors or franchisees, but, speaking for myself, if I were a franchisor or was advising a franchisor, I would be looking at balancing the potential benefits such as that against the potential detriments. I would be looking at the other legal remedies I had if someone misused my IP, and they are substantial. I would consider whether the benefits outweigh the detriments. At least from a legal analysis, we see sufficient problems in the way these concepts are applied in this legislation to make me speculate as an individual that if I were doing that analysis, I would come out against including the changes, regardless of which side I was on.

The CHAIRMAN: Let us change the topic away from good faith; we might come back to it. This is state legislation. Over the last 20 years we have been trying to push commercial law to a national basis. That is a very important concept. A lot of progress has been made and most of the regulation is under the commonwealth's domain. Do you see deficiencies in the way the commonwealth regulates or legislates on this so that a state needs to have its own—not parallel, but perpendicular—regulations? Are you aware of any trends that would ameliorate, or otherwise, this legislation along the way, such as new legislation and changes to the acts at the commonwealth level?

Ms Russell: With regard to that, it is not something that we are able to comment on on behalf of the Competition and Consumer Committee or the Law Council of Australia because we have a mandate to provide this submission based on the terms of reference.

The CHAIRMAN: If I wrote you a letter expanding on that, could you respond?

Mr Keane: We would go back to the committee. Certainly the first part about whether there are deficiencies in the commonwealth law could be the subject of a further response.

The CHAIRMAN: Okay. Are you aware of major changes in the commonwealth competition and consumer law that are under way? I was told anecdotally that over a number of years people have been looking at the laws and trying to unify, simplify, reduce and clarify them. Hopefully that is coming towards an end, I understand.

Ms Russell: Certainly with regard to that the Trade Practices Act was recently amended and is now the Competition and Consumer Act, as you would be aware. As part of that, the fair trading and consumer legislation has been harmonised Australia-wide and adopted by all states and territories, so that all the laws relating to fair trading, including business-to-business and consumers, are harmonised and uniform across Australia. As part of the Australian Consumer Law, the unconscionable conduct provisions that used to be in the Trade Practices Act have continued through on an Australia-wide basis. Bill referred to the pecuniary penalties that are in place that were not in place before in relation to unconscionable conduct, including business transactions.

The CHAIRMAN: Did those changes to the commonwealth legislation consider the issues of good faith and franchising? Was that part of the debate?

Mr Keane: I am not aware whether or not they did.

Ms Russell: Nor am I.

Mr Keane: The committee's submission at 3.1 addresses the role of how the Australian Consumer Law might be regarded as one of a number of harmonisation projects that the commonwealth and state governments have been engaged in. I suspect many of you will be much more informed about that than I am. The point made by the committee's submission is that this legislation appears to be swimming against that tide.

Mr P. ABETZ: Can I ask a question on costs? Are you happy to move on? On costs, in your submission at paragraph 2(b)(ii) on page 3 you assert that the bill would result in increased compliance costs for businesses involved in franchising. Given that all franchisors and franchisees are obligated to adhere to and conform with the Franchising Code of Conduct, and because, as you state, franchisors and franchisees already have the obligation to act in good faith to one another under common law, why would it increase the costs of compliance? I note that Jim Penman, who is the largest franchisor in the country, has put in writing and made a public statement that this bill would not cost him one cent in compliance costs because his contracts comply with the Franchising Code of Conduct and he already conducts himself according to good faith and therefore it would not cost him one cent. Is not the implication that there would be significant compliance costs an admission on the part of the franchising industry that there are many franchising contracts out there that do not conform to the Franchising Code of Conduct?

Mr Keane: I would not interpret it in that way. If I were advising a franchisor or franchisee in the context of the termination of an agreement, for example, and I was given a draft letter that my client was sending to the other party and I was asked to advise on that letter, I would, I would hope, consider the application of the common law concept of good faith to that conduct. I would also, as a result of this legislation, look at whether my understanding of the common law differs from the attempted encapsulation of the common law in this statute. That is a distinct legal question. I would look at whether or not this statute requires me to do something in addition to or differently from the way that I would have done it. Does it expose me to more or less risk? Does this legislation, as has been suggested by you, simply introduce the common law concepts directly through statute law? I would not assume that that was the case because the words of this statute differ from the words that some judges have used to describe the concept of good faith. So I now have to look in two places. Therefore, it is more complex and expensive advice, and I imagine that that kind of advice would be required to be given quite regularly if this law were introduced in not only Western Australia, but I imagine that kind of advice would have to be given pretty well nationally because a lot of franchisors would be national. Also, the provisions of the act apply to the conduct in so far as it relates to Western Australia. There are a whole range of reasons why I imagine it is a more complex analysis to advise a client, whether the client is a franchisee or a franchisor, in order to determine the risks under these provisions.

Mr P. ABETZ: Would it only be when it comes to the end time —

Mr Keane: That is just one example. I imagine there would be many circumstances in which you would be looking at two sources of law—statute law and common law. It is commonly the case that the analysis is different under each.

[12 noon]

Mr W.J. JOHNSTON: But, with respect, perhaps in other issues the common law covers hundreds and hundreds of different issues that are also covered by statutory law, and that is your job, is it not?

Mr Keane: It is, and we are happy to be paid for it. As a solicitor, I am quite happy to be paid for the additional expense. The fact that it happens already does not necessarily mean that there is a good case for making it happen here.

Mr W.J. JOHNSTON: When you say "additional expense", let us take another concept that is already in the code. You are already providing advice on that issue that is in the code where there is a common law interpretation anyway, are you not? It is just another —

The CHAIRMAN: Another expense.

Mr Keane: It is another expense.

Mr W.J. JOHNSTON: — another couple of minutes' work.

Mr Keane: Obviously I cannot quantify it. If asked to comment on legislation that moves the law in a particular direction, it seems to me that advice on more stuff means more cost.

The CHAIRMAN: Did you want to comment on that?

Ms Russell: I was just going to add another cost concept, which is referred to in the submission. In addition to the example of giving and receiving legal advice and the costs incurred in relation to addressing different legislation, there is also the potential cost of either bringing actions under different grounds, which may or may not make the costs significantly more—I think that is again a case-by-case basis depending on the circumstances—but also the potential cost of being exposed to potentially a number of actions. There may be an action by the commissioner under the state legislation or an investigation. Even if it does not lead to a proceeding as such, there would still be the costs of dealing with that. Similarly, there may at the same time be an investigation by the Australian Competition and Consumer Commission in relation to potential breaches of the commonwealth code. Along with that, there may be individual actions brought by one or more franchisees if you were a franchisor, for example. There are probably a few connotations to that.

Mr W.J. JOHNSTON: Sure, but are you not saying that if you extend a new right, there are also new enforcement arrangements? That is pretty straightforward.

Ms Russell: It is, but my point is fairly similar; it is just that it does introduce an additional cost. I guess the question leading on from that is whether it is necessary, given there is already a regime that addresses conduct between franchisees and franchisors.

The CHAIRMAN: As Bill said, it gives a right, does it not?

Mr Keane: I guess you might say it gives a slightly different form of an old right. The problem for lawyers in doing that is you ask yourself: how much substantively are we moving the ball forward; how much are we changing things? Then you look at how much it costs to move the ball forward that far? I am not just using a gridiron analogy because I hear an American accent! But if you are making that analysis, what we point out as lawyers is that "different" is inherent in this, because the common law is a more subtle and nuanced expression of these concepts, so it is necessarily different. Whilst it is seeking to apply a concept that in substance is actually there, words matter. And when you change words and make these legislative decisions about the order of the words and the connections between them, you do change the law. When you change the law, even if you do not change it much, there is a cost for companies that must predict the outcome of that; and that cost, I imagine, is relatively substantial. If you look at that cost and you imagine whether it justifies

the further amount, you move the concept by implementing this. At least it was the committee's analysis that it does not seem to stack up.

The CHAIRMAN: Do you think it skews the legislation in favour of smaller franchisees? I think one of the arguments for this legislation will be that the franchisors are big enough and can take care of themselves, but many of the franchisees are very small. Does this legislation close the gap and clarify good faith to enable them even to avoid legal action or make legal action clear?

Mr Keane: I think the answer to that question is unclear. One problem is—this is not addressed in the submissions; this is me speaking for myself—I would be concerned that big companies that are big and ugly enough to look after themselves are capable of using uncertain concepts to their advantage more than small companies, as a general observation, but either party might find themselves with an unintended consequence from this legislation. Proceedings with this kind of uncertainty could be threatened with some confidence, with the other party in a situation where the one thing they know they have to do is go and get legal advice. So you now have another new plank that can be put under any dispute, and that new plank is going to require some legal advice. I think it is difficult to predict whether it is necessarily advantaging one kind of franchisee or another. There is plenty of legislation where there have been unintended consequences that in fact have moved things in the opposite direction to what was intended.

Mr P. ABETZ: Given that the intent and consequence in the United States and Canada have proved to be extremely positive for franchisees, on what basis do you envisage negative impacts here? The second question I still do not understand is that the common law understanding of good faith is still evolving et cetera. That means there is uncertainty around that. People going into litigation do not really know what that means at the moment because it just depends on how the judge interprets things. Justice Rein has come out and said, "Boom, boom, boom, boom". He has given us all terms that we have put into the bill. That would provide clarity to me. If I was a franchisee thinking of taking on a franchisor about an issue, I would have much greater confidence having legislation in front of me that says, "This is what the franchisor needs to do and also what I need to do as a franchisee", rather than some vague concept that is floating out there called common law that everybody is telling me is still evolving. Surely it is the role of Parliament to clarify the law and to make it as simple as possible for people and help reduce the cost of litigation.

Mr Keane: There are three or four things in there; perhaps you can break them up. I cannot accept the premise of your first point about the evidence in the United States because, as we told you, we have not looked at it, so I do not know whether that is correct or not. I would have to take your word for that, in which case what I say is not going to help you very much. The point that we have not addressed, and continue to, is the fact that there is a difference between what the common law says about these concepts and how it applies them, and what this legislation does with those concepts. If there is a difference between those two things, and we think that there is—the state of the common law which is evolving and this expression of the concept—what we have not perhaps talked about is whether this expression of the concept is a good expression of the good-faith concept. Does it actually achieve the object that the common law seeks to achieve in implying into it that some commercial contracts have an obligation on good faith? The reason why I do not think it does is because it lacks the capability to balance these concepts against things like the legitimate self-interest of the individual parties. There is no capability to do this. If you do not act cooperatively, you are liable to a pecuniary penalty. A court applying common law and the lawyer's advice most likely looking at the common-law concept would be balancing those things and you would get advice from your lawyer that would say, "Balancing those two things, I think you have or have not got a problem with your obligation on good faith." With this legislation there is no balancing. So you are just saying, "I do not know whether a court would say that", because a court taking this legislation will not apply the same concept in the same way as a court applying the common law. They will not. They will look at the legislation, they will look at the explanatory memorandum and they will apply the formal words of the statute, and the dominant thing will be

the words of the statute. So, I would draft a pleading for a client and I would be saying, "By doing these things, they had not acted cooperatively." And a lawyer advising the other party would say, "Well, I don't know what a court is going to do with that. I simply don't know." If the allegation of breach of good faith were made under the common law, I would be able to look at a whole lot of evolving legal cases and provide more precise advice on what my client's likely outcome would be.

Mr P. ABETZ: But after a short time you would have case law on how judges apply this law, which you could then refer to. So, initially there is, I guess, a little bit of uncertainty because we are not quite sure how a judge would interpret it. But after a few court cases, it would be like unconscionable conduct, which is a term in the Trade Practices Act. That is a term that in that legislation was not defined, and as some court cases have emerged that is becoming clearer.

Mr Keane: To comment on this piece of legislation on the scenario that you have just outlined, now you have two parallel evolving forms of law, two parallel forms of good faith—one under the common law and one under the statute—and they are independent of each other. What tends to happen over time is that these things will diverge. We do not actually know whether they will diverge or whether they will converge; we just do not know. But you are now talking about two parallel concepts of good faith that you have to explain to people, many of whom will not be sophisticated in business or law. I suggest to you that that is problematic.

Mr W.J. JOHNSTON: I just want to ask a question directly on the question of the terms of reference. Do you think the legislation is inconsistent with the Trade Practices Act or the other instruments from the commonwealth? Has the commonwealth covered the field on this issue or not?

Mr Keane: Those are two distinct concepts, I think. Inconsistent with or covering the field: we did not see any direct inconsistency with the commonwealth law.

Mr W.J. JOHNSTON: And do you think they covered the field?

The CHAIRMAN: The commonwealth has?

Mr W.J. JOHNSTON: Yes. Has the commonwealth covered the field? Can we legislate on this issue?

Mr Keane: We cannot comment on that issue, I do not think.

The CHAIRMAN: There is one issue: is this bill potentially retrospective in its action?

Mr Keane: Again, I think that is something the committee did not comment upon.

Ms Russell: It is not something that the committee commented on. I have not really spent a lot of time considering it but my initial view of it was that it would not be, but I have not spent any amount of time analysing that.

Mr Keane: I would agree with that. Speaking for myself, I would agree with that.

The CHAIRMAN: Certain parties who are against the enactment of the bill maintain that clause 14 on redress orders creates an automatic or de facto right of renewal of a franchisee. How does the council interpret this section? Is the ability for the courts to grant a renewal order problematic in terms of freedom of contract?

Mr Keane: We cannot represent the views of the committee on that issue because that was not an issue that was put to the wider committee, I am sorry.

The CHAIRMAN: So, if we put it to you, you could perhaps potentially respond?

Mr Keane: Yes.

The CHAIRMAN: You are not billing us for this time, are you? That was a joke!

There are two questions in respect of these redress orders that I will send to you for the committee to consider. What is the timing of the reconsideration of the committee? I assume it does not sit every week.

Ms Russell: Depending on the timing, obviously, the more notice we can receive the better, because it is such a large committee and there is generally a consultation process amongst the members and then some coordination to try to get as wide a view as possible. We have been known to turn things around pretty quickly, but the more notice we can receive is obviously going to produce a more comprehensive submission.

Mr Keane: Perhaps to describe the process will assist. Typically a request is received, a working group is comprised of members of the committee, and that working group comes up with a draft, which is then circulated to the entire committee and comments come back. The committee is quite large; I think probably around 100 solicitors nationwide, perhaps more. In relation to this submission, for example, there was a discussion involving solicitors in South Australia, New South Wales and Victoria. At each of our monthly meetings, if there is a draft submission outstanding when the monthly meeting is held, it is typically discussed at that meeting.

The CHAIRMAN: How do you meet; electronically?

Mr Keane: We meet as state groups and then we report by minutes through to the national executive.

Mr I.C. BLAYNEY: I am sorry I was not here earlier, so my question might be redundant, I suppose. I was just curious to know whether you are a group that looks at all laws objectively and then gives people like us an answer back. Is that right, so that you are not appearing here on someone's behalf?

[12.15 pm]

Mr Keane: No.

Ms Russell: Perhaps if I could expand on that. We represent one committee of the business law unit of the Law Council of Australia. That committee is the Competition and Consumer Committee, which was formerly known as the Trade Practices Committee. Our focus is very much on matters relating to competition and consumers.

Mr Keane: Typically, the committee does not regard its business as including speaking to the merits of the policy objective of legislation. Because one can differ about the policy objective, we tend to confine ourselves to commenting upon whether the legislation enacted would promote those objectives.

Mr P. ABETZ: Do you see any problem with the provision in the bill to have pecuniary penalties for breaches of the code? At the moment there seems to be ample evidence, so we presented a Ripoll inquiry and various other inquiries of franchisors not adhering to the code, but it costs the franchisee too much to take them to court. Some rogue franchisors simply thumb their nose at the code, with very little reaction from anybody. Do you see any issues relating to the introduction of pecuniary penalties?

Mr Keane: Yes. I think if you combine the nature of the good-faith concept with a pecuniary penalty, you amplify the error. Some concepts you can imagine, some standards of conduct—there is quite a spectrum of conduct that might fall within that standard. The example we use in the submission is misleading or deceptive conduct. Everybody could agree that misleading or deceptive conduct is undesirable. The question is whether the breadth of conduct that might be regarded as misleading or deceptive ought to be the subject of a sanction. In many cases conduct can be misleading or deceptive when it was not intended to be and it was of a very minor or trifling nature and its consequences were not great. Equally, misleading or deceptive conduct can be extremely egregious and lead to substantial consequences. When you have a spectrum that big that is covered by the same concept, applying pecuniary penalties can have some really serious unanticipated effects, particularly if you look at franchises, where you might have breach of a good-faith standard—particularly one expressed in the way it is in this legislation—that applies to a franchisee that is used by a franchisor as a bludgeon. The introduction of this concept is not without risk to

franchisees. I might suggest that in fact the people in the best position to make good use of some of these concepts that may well be applied in this way might be franchisors. There might be substantial unintended consequences for franchisees. I do not know, I have not researched it, but I would be concerned. Just as misleading or deceptive conduct is a broad spectrum, good faith is a very broad concept, particularly where you have not got the sensitivity of the common law and judge the application of that law the way that you have here; that is, as a prescriptive application. Applying a pecuniary penalty regime to that breadth of conduct seems to me to be problematic.

Mr P. ABETZ: What about if we take the "good faith" out; just the existing franchising code of conduct?

Mr Keane: I think that is beyond the scope of what the committee has addressed in the submission, I am sorry.

The CHAIRMAN: Thank you for your evidence before the committee today. There are a number of questions that we have not been able to ask today. If you are willing, we have to follow up those questions. We will put them in quickly so you can get through your processes.

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, it will be deemed to be correct. New material cannot be added or introduced 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. If you have any doubts, call Tim. Thank you for your efforts.

Hearing concluded at 12.20 pm