



Signing on the Dotted Line: The Legal Side of Franchising Your Business

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Canadian Franchise Association

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Intro: Legal Needs

Franchisors.

- a) Legal obligations?**
- b) Cost?**

Franchisees.

- a) My rights? Protection?**
- b) Cost?**

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Legal Elements

A - Franchise Contracts

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B - Franchise specific laws

C - Other business laws

D – Laws of General Application

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A- Contracts: **The Franchise Agreement**

What are the elements of the franchise agreement?

- Grant of licence to use
(i) system and (ii) trade-marks
- Territory defined (exclusive?)
- Term, renewal terms if any
- Assignment and termination

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A- Contracts: **The Franchise Agreement**

- **Initial fees**
- **Ongoing royalties**
- **Advertising fund contributions**

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A- Contracts: **The Franchise Agreement**

Franchisee's covenants

- **Local advertising (eg. Yellow pages)**
- **Equipment and Inventory**
- **Update “look” as and when determined by franchisor at franchisee's cost**
- **Report sales**

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A- Contracts: The Franchise Agreement

Franchisee's covenants:

- **Devote full time attention**
- **Non-compete/solicit upon termination (enforceable?)**
- **Restrictions on assignment**
- **Must “defixture” location upon termination**

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A- Contracts: **The Franchise Agreement**

Franchisor's covenants:

- **Location assistance and site planning**
- **Location design**
- **Subletting of location**

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A- Contracts: **The Franchise Agreement**

Franchisor's covenants:

- **Opening assistance and supervision**
- **Training**
- **POS, Accounting software, etc**
- **Promotional material, manuals, etc**
- **Continuing assistance**

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A- Contracts: **The Franchise Agreement**

- **Term and Renewal issues (5+5 etc.)**
- **Assignment Issues**
- **Termination (rights and obligations)**
- **Non-compete/solicit**

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A- Contracts: **The Operations Manual**

- **“KEY” to franchise**
- **Essential trade secrets of system**
- **Usually “loaned” to franchisee**
- **Subject to confidentiality rights**
- **Not technically a contract**
- **Incorporated into franchise agreement by reference**

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A- Contracts: Guarantees

- **Given by principals of franchisee corporations, ie. Shareholders**
- **Spousal guarantee often requested**
- **Guarantee payment and performance of obligations under franchise agreements**
- **Coupled with indemnities**
- **Some obligations are personal, ie. Devotion to business, non-competition etc**

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A- Contracts: **Lease Arrangements**

- **Subleasing by franchisor is common**
- **Practice of having franchisee lease directly is also gaining prominence**
- **Franchisee will request a conditional assignment of lease or option to assignment**
- **Control of premises is key**

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A- Contracts: Other

- **Security agreements**
- **Promissory notes**
- **Signage agreements**
- **Site acceptance agreement**
- **Estoppel agreement/
acknowledgment of no prior
representations**

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B- Franchise Specific Laws

Why do they exist?

- **You have a scalable, successful business system and known trademarks**
- **You want to expand via franchise sales to individuals**
- **Prospects have varying degrees of sophistication and business savvy**
- **“Power imbalance”**



B- Franchise Specific Laws

- **Franchise legislation seeks to redress the imbalance**
- **Ontario, Alberta, PEI and New Brunswick have statutes in force**
- **Quebec (Civil Code generally)**

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B- Franchise Specific Laws

Overview of franchise legislation:

- a. Definition of “franchise”**
- b. Pre-sale disclosure**
- c. Right to rescission**
- d. Good faith and fair dealing**
- e. Rights to associate**

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B- Franchise Specific Laws

What is a “Franchise”?

- a) grant of right to engage in a business**
- b) requirement to make one or more direct or indirect payments**
- c) goods or services substantially associated with trade-mark; and**
- d) franchisor exercises significant control over, or offers significant assistance in the franchisee’s method of operation**

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B- Franchise Specific Laws

Is it a franchise?

- a) Bottler and reseller of *Coca-Cola*?**
- b) Fast food restaurant where methods of operation and décor are dictated?**
- c) Gas station?**

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B- Franchise Specific Laws

Disclosure Obligations:

- **franchisor must provide disclosure document in form prescribed**
- **14 days before any payment or the signing of any document**
- **payment includes refundable deposit (Ontario, not Alberta)**
- **agreement includes confidentiality (Ontario, not Alberta)**

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B- Franchise Specific Laws

Disclosure Obligations (Contents):

- **document must contain all “material facts” including those prescribed**
- **Financial statements as prescribed**
- **Copies of franchise agreements and all other agreements relating to the franchised business (sublease, ops manual etc.)**
- **Prescribed statements**
- **Such other documents/info prescribed**

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B- Franchise Specific Laws

Disclosure Obligations (Contents):

- **“material facts” include all facts that would or could significantly influence value of purchased franchise**
- **Alberta legislation: info that could reasonably be expected to have a significant effect on the value or price of the franchise to be granted or the decision to acquire the franchise**

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B- Franchise Specific Laws

Disclosure Obligations (Contents):

- **Business background of franchisor and principals**
- **convictions against franchisor or principals for fraud or deceptive business practices or violations of laws regulating a franchise or business**
- **Administrative orders or penalties under laws regulating a franchise or business**
- **Liability for civil misrepresentation, unfair or deceptive business practices or laws that regulate a franchise or business**

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B- Franchise Specific Laws

Disclosure Obligations (Contents):

- **Bankruptcy or insolvency proceedings in the last 6 years**
- **Financial statements for most recent fiscal year**
- **List of costs for establishment of franchise**
- **Estimates of annual operating costs and earnings projections can be provided**

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B- Franchise Specific Laws

Disclosure Obligations (Contents):

- **Description of financing arrangements**
- **Training**
- **Advertising fund contributions**
- **Restrictions or requirements respecting suppliers or clients**
- **Policies respecting volume rebates**
- **Rights to trade-marks**

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B- Franchise Specific Laws

Disclosure Obligations (Contents):

- **Licences, permits etc. needed to operate the franchise**
- **Requirement for personal participation**
- **Encroachment policy**
- **Details of franchise terminations**
- **List of all franchises in Ontario**
- **Certificate as to disclosure**

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B- Franchise Specific Laws

Disclosure Obligations (Remedies):

- **Failure to provide disclosure document gives franchisee right to rescind agreement 2 yrs from date of signature**
- **Defect in disclosure gives franchisee right to rescind within 60 days of receiving document**

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B- Franchise Specific Laws

Disclosure Obligations (Remedies):

The franchisor has within 60 days of the date of rescission

- **to refund money received other than money for inventory supplies or equipment**
- **to purchase from the franchisee inventory, supplies and equipment purchased under the Agreement**
- **compensate for losses incurred in acquiring, setting up and operating the franchise**

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B- Franchise Specific Laws

Duty of Good Faith and Fair Dealing:

- **Franchisor has a duty to act in “good faith” in the performance and enforcement of the franchise agreement**
- **Standard of commercial reasonableness**
- **Do not exercise discretion arbitrarily**
- **Keep interests of F’ee in mind**

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B- Franchise Specific Laws

Right to Associate

- **Franchisor cannot restrict rights of franchisees to form associations**

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C- Business Specific Statutes

Trade-Marks Act

- Permits registration and licensing of trade-marks
- Allows franchisor right to require that marks be used in accordance with system standards

Competition Act

- Regulates multi-level marketing schemes and prohibits pyramid selling
- Prohibits franchisors from requiring higher sale prices or putting floors on prices

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C- Business Specific Statutes

Privacy Laws.

- Federal and provincial (B.C., Alta, and QC) laws regulate the use, collection and disclosure of personal information.
- PIN is collected in surveys, contests, promos, gift cards, online sales, etc.
- Data is transferred to franchisor for use in marketing.
- Data is outsourced for order processing, technical support, payroll.
- PIN is transferred when system is sold.

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C- Business Specific Statutes

Privacy Laws

- Franchisor must have own privacy policy and web policy and should recommend system-wide policy
- Consents to all uses must be obtained
- Ensure that agreements have consents of franchisees to use of their personal information

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C- Business Specific Statutes

Other regulated areas

- Alcohol and gaming
- Contests
- Personal property security
- Municipal permits (restaurants, etc.)
- Specific regulation (ie. Day nurseries)
- Consumer protection – internet contracts, remote contracts, personal services contracts

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D- Laws of General Application and Other Legal Issues

- **Tax and corporate laws
(structuring issues)**
- **GST, RST, EHT, EI, CPP, WSIB**
- **Employment laws**
- **Health and safety laws**
- **Occupier's liability**
- **Bankruptcy and insolvency laws**

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D- Laws of General Application and Other Legal Issues

- **Dispute resolution and litigation**
- **Purchase and lease of capital assets**
- **Commercial agreements (supply agreements, custom software, consulting, etc.)**
- **Bank financing**
- **Purchase and sale of unit franchises or whole system**

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Conclusion

- **This has been a brief overview of legal considerations**
- **Qualified franchise counsel can assist you with essential structuring and documentation**
- **Proper legal advice can streamline your system and steer you around obstacles as your franchise grows**

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Thank You.

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