Parliamentary Joint Committee on Corporations and Financial Services

Fairness in Franchising

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Chapter 15

Dispute resolution

Introduction

15.1 Accessible, affordable and effective dispute resolution under the Franchising Code of Conduct (the Franchising Code) is of fundamental importance to franchisors and franchisees, particularly given the power imbalance between the respective parties. An effective dispute resolution process should have a sufficient range of mechanisms in place to enable the parties to resolve disputes in the most timely, cost-effective, flexible and fair way, without the need to resort to the court system except in rare cases.[1]

15.2 Evidence from a range of submitters and witnesses to this inquiry, including franchisees, franchisors, mediators, ombudsmen, academics, and regulators, highlighted the need for changes to the current dispute resolution arrangements in the franchising sector.

15.3 This chapter sets out the dispute resolution arrangements currently available under the Franchising Code and the issues identified during the inquiry. This is followed by a comparison of the dispute resolution arrangements for franchising with the dispute resolution arrangements for small business generally, as well as for the food and grocery supply sector and the financial services sector.

15.4 At the outset, however, the committee points out that not all disagreements between franchisors and franchisees proceed to formal dispute resolution. For example, Mr Andrew Gregory, Chief Executive Officer of McDonald's Australia, acknowledged that the franchisor has 'robust discussions debating the importance and priorities of our plans, and we disagree with our franchisees regularly'. Mr Gregory pointed out that McDonald's 'engage our franchisees through a range of committees and decision-making bodies that cover nearly every aspect of our business'. According to Mr Gregory, this collaborative approach meant that even serious disagreements about major business decisions were typically resolved in discussions between the franchisor and its franchisees.[2]

Current arrangements and outcomes

15.5 The Franchising Code provides for parties to a franchise agreement to resolve disputes through two mechanisms: mediation and legal action through the court system. Part 4 of the Franchising Code outlines the procedures to be followed for disputes between parties to a franchise agreement. Parties are required to resolve a

1 See Office of the NSW Small Business Commissioner, *Submission 49*, pp. 12–14; Office of the Franchising Mediation Adviser, *Submission 37*, pp. 17–18; Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, pp. 13–21.

2 Mr Andrew Gregory, Managing Director and Chief Executive Officer, McDonald's Australia Ltd, *Committee Hansard*, 21 September 2018, pp. 1 and 6.

dispute in a 'reconciliatory manner'. If the parties are unable to agree how to resolve a dispute within three weeks, either party may refer the matter for mediation.[3]

Mediation

15.6 Once the mediation process begins, 'the parties must attend the mediation'.[4] Should the parties be unable to agree on a mediator, either party may approach the Office of the Franchising Mediation Adviser (OFMA) and request the appointment of a mediator.[5]

15.7 OFMA informed the committee that for the 21 month period from 1 January 2017 to 30 September 2018, it referred 477 disputes to panel mediators. These disputes involved 202 different franchisors.[6]

15.8 OFMA also reported:

- four per cent of franchise systems generated 10 or more disputes (representing 45 per cent of all matters lodged);
- 27 per cent of franchise systems were reported as having 2 or more but less than 10 disputes (representing 29 per cent of all matters lodged); and
- 69 per cent of franchise systems had only 1 dispute with a franchisee that was mediated (representing 26 per cent of all matters lodged).[7]

15.9 OFMA cautioned that the results set out above may not necessarily represent the complete picture of franchising in Australia, as the records only include disputes referred to OFMA. Further, the statistics do not include 70 separate disputes relating to franchising operations lodged separately under the Oil Code of Conduct with the Office of the Oil Code Dispute Resolution Adviser.[8]

Multi-party mediation

15.10 Multi-party mediation in the context of franchising would generally involve a number of franchisees with similar issues all mediating with the franchisor at the same time. The ACCC observed that multi-party mediation has benefits such as:

- assisting to shift the imbalance of bargaining power that exists between the franchisor and franchisee when resolving disputes; and
- creating a more efficient process and use of resources.[9]

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3 Competition and Consumer (Industry Codes—Franchising) Regulation 2014, cl. 34–45.

4 Competition and Consumer (Industry Codes—Franchising) Regulation 2014, sub cl. 39(3).

5 Competition and Consumer (Industry Codes—Franchising) Regulation 2014, sub cl. 38(4).

6 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 9.

7 Office of the Franchising Mediation Adviser, *Submission 37*, p. 8.

8 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 9.

9 Australian Competition and Consumer Commission, *Submission 45*, p. 15.

15.11 However, the Franchising Code 'does not expressly state that mediators may undertake multi-franchisee mediation when disputes of a similar nature arise within a franchise system'.[10]

15.12 More problematically, the ACCC 'is aware of franchisors refusing to attend multi-party mediation on this basis and insisting on addressing disputes on an individual basis'.[11]

15.13 OFMA has been involved in trying to assist multiple franchisees from the same franchise network who have similar complaints about the franchise system or the franchisor. OFMA noted that multi-party mediations have successfully resolved disputes that have involved over 20 franchisees.[12]

Relative success and outcomes of mediation

15.14 OFMA noted that the settlement rate for mediations conducted by OFMA in 2017 was 80 per cent, and in the first quarter of 2018 it was reported as 85 per cent. While these results appear to indicate a high level of success, OFMA advised circumspection in interpreting the success through these statistics alone. Rather, OFMA preferred to delve deeper and obtain information about the extent to which settled matters were in fact 'totally resolved'. Viewed through this lens, about 68 per cent of matters are 'totally resolved' to the satisfaction of both parties.[13]

15.15 The statistics show that while about two thirds of all disputes referred to mediation have a successful outcome, about one third do not. This means a substantial proportion of disputes do not reach a mutually satisfactory outcome. Indeed, OFMA notes that while successful mediation does not rely on the collaboration and cooperation of the parties because a skilled mediator can help achieve an agreed outcome, it does require mutual good faith on behalf of the participants:

> …a necessary condition is that the parties be willing to negotiate in good faith and try to achieve an outcome. Where this condition is missing the mediation process will fail by design.[14]

15.16 Evidence to the committee from a range of submitters and witnesses appeared to bear out OFMA's conclusions about the relative success of mediation and the reasons for that. For example, Professor Andrew Terry noted that even though there is 'a very high settlement rate at very low cost and in a very short time, a lot of those settlements are reluctant settlements on the part of a franchisee, whose only alternative at present is to go to court'.[15]

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10 Australian Competition and Consumer Commission, *Submission 45*, p. 15.

11 Australian Competition and Consumer Commission, *Submission 45*, p. 15.

12 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 11.

13 Office of the Franchising Mediation Adviser, *Submission 37*, p. 9.

14 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 20.

15 Professor Andrew Terry, Private capacity, *Committee Hansard*, 24 August 2018, p. 18.

15.17 The Australian Small Business and Family Enterprise Ombudsman (ASBFEO) noted that one of the challenges for franchisees in going to court is the way cost orders operate. If a franchisee pursues litigation, but runs out of money to continue, it is possible for courts to order the franchisee to pay the franchisor's costs.[16]

15.18 Mr Faheem Mirza, a franchisee, noted that his mediation was counted as successfully resolved in the mediation statistics. From his perspective, however, it was not at all successful:

> I took this dispute to the OFMA… However, OFMA could not even get enough money out of Foodco to enable me to pay their [Foodco's] fee. I signed a deed. I walked out with $100. I was in debt with CBA and I had to fail my ATO liabilities to pay for my living costs. For the record, OFMA marks this result as a successful outcome.[17]

15.19 Another franchisee, Mr Anthony McVilly, described the challenges of mediation when there is an imbalance of power:

> So we went to mediation. That is a total waste of time, effort, money—whatever you want to call it—because they hold the gun at your head. They say what you're going to do. And if they don't like it—and they keep changing the goalposts—it gets too hard. You can't go anywhere else because they are a multinational company.[18]

15.20 Franchisee Mr Sanjeev Bajaj relayed his experience of mediation under the Oil Code of Conduct (Oil Code):

> We had a mediation under the Oil Code. We walked in there and they told us what we'd done wrong. We said, 'No problem; how can we fix it? We'll fix it.' They gave us 30 days to sell the site. We said, 'We can't sell it in 30 days. It's a freehold business. We'll do our best and we will change the colours and put your colours in.' We would take their card and their fees and put their branding in tomorrow morning and paint it all over. They went out of the room and didn't come back for five hours. Then they said, 'There is no deal.' So we had to go to court. We lost about five or six hundred thousand dollars in the court case. In the end the court appointed a mediation.[19]

15.21 Likewise, another franchisee, Mr Robert Whittet, highlighted the problems of the current situation where mediation or court are the only options:

> We spent well over $5000 on going to mediation. After our spending $5000, the other side got up from the table and walked away and said: 'We're not doing anything. We're too big. Take us to court.' We outlaid what

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16 Dr Craig Latham, Deputy Ombudsman, Australian Small Business and Family Enterprise Ombudsman, *Committee Hansard*, 21 September 2018, p. 41.

17 Mr Faheem Mirza, Private capacity, *Committee Hansard, 29 June 2018*, p. 39.

18 Mt Anthony McVilly, Member, Victorian Automobile Chamber of Commerce, *Committee Hansard*, 22 June 2018, p. 10.

19 Mr Sanjeev Bajaj, Private capacity, *Committee Hansard*, 22 June 2018, p. 15.

> we had left to try to go through the mediation process, and then you end up at the point where you've spent so much money—in our case, it's basically cost us over $2½ million to fight, which we have lost, over seven years. This is where they pull you. Even in the last few days, they've said to us: 'Sell what you've got. Try and go another week.'[20]

15.22 The Franchisee Federation of Australia (FFA) summed up the position of many franchisees by submitting that the mediation process under the Franchising Code is ineffective because it allows franchisors to just go through the motions or, on occasion, to actively impede it. The FFA argued that the current dispute resolution process via the OFMA has been useful in minor disputes but does not have the requisite authority to bring about the resolution of disputes arising from the power imbalances identified during the inquiry.[21]

Arbitration as an addition to the dispute resolution process

15.23 As noted above, in many cases mediation is a desirable and effective dispute resolution mechanism. However, the absence of a determinative mechanism as another constituent part of the dispute resolution process is a serious shortcoming. Several submitters and witnesses supported the addition of a determinative system to the current dispute resolution process under the Franchising Code. Many of these submitters drew the committee's attention to the existence of such a mechanism under other codes, such as the Food and Grocery Code of Conduct.

15.24 In explaining the difference between mediation, conciliation and arbitration, ASBFEO noted:

- A mediator is more like a facilitator and will raise questions that lead people to consider the range of options.
- A conciliator will guide and direct the parties, while acknowledging that the parties need to agree on an answer.
- An arbitrator can act much like a conciliator, but has the capacity to make a contractually binding ruling on the parties.[22]

15.25 The arguments set out in favour of some form of mandatory determination in circumstances where a resolution is not reached through mediation included:

- the lower cost of arbitration compared to a court process;[23] and

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20 Mr Robert Whittet, Private capacity, *Committee Hansard*, 8 June 2018, p. 69.

21 Franchise Federation of Australia, *Supplementary Submission 113.1*, p. 4; see also Mrs Maria Varkevisser, Private capacity, *Committee Hansard*, 8 June 2018, pp. 42–43.

22 Dr Craig Latham, Deputy Ombudsman, Australian Small Business and Family Enterprise Ombudsman, *Committee Hansard*, 21 September 2018, p. 41.

23 Professor Andrew Terry, *Submission 108*, p. 8; Mr Brian Keen, Founder and Chief Executive, Franchise Simply, *Committee Hansard*, 8 June 2018, p. 62; Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 21.

- the ability to secure a determination in circumstances where one party has declined to participate in mediation in good faith.[24]

15.26 The committee's 2008 report, *Opportunity not opportunism: improving conduct in Australian franchising*, concluded that a Commonwealth tribunal for the franchising sector would most likely add another layer of complexity and expense to the process without achieving improved outcomes. In addition, the committee argued that many of the issues which lead to franchising disputes might be mitigated by the introduction of an explicit obligation into the Franchising Code for all parties to a franchise agreement to act in, and approach mediation in, good faith.[25]

15.27 However, the committee acknowledges that much has changed over the last ten years. As the evidence on mediation in the previous section attests, the shortcomings of the processes currently available under the Franchising Code (including the good faith provisions) have become much more apparent. As the evidence below shows, substantial progress in arbitration has occurred since 2008.

15.28 OFMA drew attention to significant changes in dispute resolution procedures. OFMA pointed out that since the committee's 2008 inquiry into franchising, the state based Commercial Arbitration Act has been completely revised and updated in line with an amended International Arbitration Act and has been adopted nationally as a uniform Act in all states. OFMA also drew the committee's attention to the use of arbitration in every administrative tribunal in Australia.[26]

15.29 Further, OFMA also noted that the Franchising Code lacks the range of determinative dispute resolution procedures, such as arbitration, used in more recent codes such as the Food and Grocery Code of Conduct introduced in 2015.[27]

15.30 Likewise, Professor Andrew Terry commented on the growing trend towards establishing tribunals and ombudsmen as an avenue for consumers to invoke legal rights, thereby avoiding costly and time consuming court action.[28] He also drew the committee's attention to various industry ombudsman schemes which showed a precedent for ombudsmen making binding decisions. One example, the Financial Ombudsman Service, provided a range of remedies including the '…payment of money, compensation for financial or non-financial loss, and in some cases variation of contract terms'.[29]

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24 See, for example, Office of the Franchising Mediation Adviser, *Supplementary Submission* 37.1, pp. 13–21;Australian Small Business and Family Enterprise Ombudsman, *Submission 130*, p. 2; Dr Craig Latham, Deputy Ombudsman, Australian Small Business and Family Enterprise Ombudsman, *Committee Hansard*, 21 September 2018, p. 39; Franchisee Federation of Australia, *Supplementary Submission 113.1*, p. 4.

25 Parliamentary Joint Committee on Corporations and Financial Services, *Opportunity not opportunism: improving conduct in Australian franchising*, 2008, p. 99.

26 Office of the Franchising Mediation Adviser, *Submission 37*, pp. 14, 18.

27 Office of the Franchising Mediation Adviser, *Submission 37*, pp. 14, 16, 17.

28 Professor Andrew Terry, *Submission 108*, p. 8;

29 Professor Andrew Terry, *Submission 108*, p. 8.

15.31 OFMA drew a further distinction between the conduct and functions of a court and arbitration, namely the ability to undertake an investigation in the arbitration process followed by the determination of the dispute by an expert or arbitrator:

> …courts are umpires, and what's really required by small businesspeople is a determination by an expert or an arbitrator—by somebody who can actually do more than simply be an umpire, by somebody who can investigate. In other words, they can call for the records, they can see the prices that were paid, they can see the amount of the discount and they can calculate what a fair outcome should be.[30]

15.32 Several submitters highlighted the importance of arbitration as a backstop to the mediation process. Both Dr Tess Hardy and the ASBFEO argued that the ability to direct parties to arbitration where a resolution is not reached through mediation would level the playing field between franchisors and franchisees in the dispute resolution process.[31]

Differing perspectives on arbitration

15.33 Despite widespread support for the inclusion of a determinative process in the dispute resolution process for franchising, there was opposition to the proposal including from the Franchise Council of Australia (FCA). This section sets out the FCA's six key reasons why it did not support suggestions to supplement mediation with any form of arbitration or any new Tribunal, and OFMA's responses to those views.

15.34 First, the FCA argued that arbitration would immediately create an adversarial environment, which runs entirely contrary to the principles of mediation. Fewer disputes would proceed to mediation, the parties would be less open to negotiated settlements and access to justice would be significantly reduced.[32]

15.35 With respect to the FCA's concern that arbitration would create an adversarial environment, OFMA responded:

> Mediation processes are born out of the adversarial litigation environment and were originally described as forms of 'alternative' dispute resolution. Therefore, mediation does not need collaborative, cooperating parties to be successful. A skilful and experienced mediator does make a difference in achieving an agreed outcome.
>
> However, a necessary condition is that the parties be willing to negotiate in good faith and try to achieve an outcome. Where this condition is missing

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30 Mr Derek Minus, Franchising Code Mediation Adviser, Office of the Franchising Code Mediation Adviser; Oilcode Dispute Resolution Adviser, Office of the Oilcode Dispute Resolution Adviser, *Committee Hansard*, 8 June 2018, pp. 3–4; see also Dr Tess Hardy, Private capacity, *Committee Hansard*, 22 June 2018, p. 4.

31 Dr Tess Hardy, Private capacity, *Committee Hansard*, 22 June 2018, p. 4; Australian Small Business and Family Enterprise Ombudsman, *Submission 130*, p. 2.

32 Franchise Council of Australia, *Supplementary Submission 29.1*, Part B: Issue 10—Dispute Resolution Mechanisms, p. 11.

> the mediation process will fail by design. A determinative procedure is then required.[33]

15.36 Second, the FCA argued that mediation is well suited to franchising, where both parties are typically small businesses and their assets are essentially intangible. The FCA suggested that neither party can typically afford for a dispute to continue. The FCA argued that as a consequence both parties have a genuine vested interest in achieving a negotiated outcome, as they know an early compromise solution will usually yield the best net outcome.[34]

15.37 Similarly, the National Retail Association (NRA) was not in favour of adding arbitration as a dispute resolution option, informing the committee that, in its view, the current focus on mediation is more conducive to building and restoring effective working relationships between franchisees and franchisors.[35]

15.38 OFMA noted that the above proposition has significant limitations, arguing that:

> Mediation is well suited to the resolution of franchising disputes if the parties are acting in good faith to resolve the conflict. But where a party is using the process to avoid an outcome (e.g. repayment of the franchise fee as they have failed to complete the agreement) then there is no impetus to resolution. In fact the party with the superior economic power can just refuse to agree, safe in the knowledge that the franchisee is unable to afford to take the matter to litigation.[36]

15.39 Third, with respect to the FCA's claim that 'arbitration would almost certainly lead to higher costs of dispute resolution and delayed resolution of disputes',[37] OFMA pointed out that in the majority of cases, mediation is the cheapest and most effective option and will therefore remain the resolution process of choice on most occasions. Accordingly, it is incorrect to compare the costs of mediation with those of arbitration. Rather, for the minority of disputes that do not achieve a satisfactory resolution at mediation, the correct comparison is the price of 'justice' through the courts versus a fixed price arbitration process.[38]

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33 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 20.

34 Franchise Council of Australia, *Supplementary Submission 29.1*, Part B: Issue 10—Dispute Resolution Mechanisms.

35 National Retail Association, answers to questions on notice, 16 October 2018 (received 31 October 2018).

36 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 20.

37 Franchise Council of Australia, *Supplementary Submission 29.1*, Part B: Issue 10—Dispute Resolution Mechanisms, p. 12.

38 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 20.

15.40 Fourth, OFMA and the ACCC[39] rebutted the FCA's claim that 'there are few if any arbitrators in Australia who would have the requisite experience to act in a franchise arbitration'.[40] OFMA observed that:

> There are hundreds of trained and experienced private arbitrators (most of them with legal qualifications as it is the state law societies and bar associations that have kept the process alive) in Australia and professional associations that train and maintain their standards.
>
> Arbitrators are empowered under many legislative schemes to act as experts and conduct the resolution of the dispute first by attempting conciliation and then if that fails, determining the matter as an 'expert'. That is, the arbitrator is empowered to conduct an 'inquisitorial process' to use their business and technical expertise and call for evidence in order to determine a matter.[41]
>
> Of the 100 mediators appointed to the Franchising Mediator List there are already 12 people who are qualified, experienced and available as arbitrators.[42]

15.41 Fifth, the FCA argued that 'the courts have been effective in enforcing franchisee rights, with most franchising cases yielding favourable results to franchisees'.[43]

15.42 However, the committee received evidence that contradicted the proposition that franchisees are generally successful in court. OFMA noted that matters that go to trial usually result in a loss for the franchisees (see chapter 7 for evidence the committee received regarding the Pizza Hut cases: *Virk Pty Ltd (In Liquidation) v. Yum! Restaurants Australia Pty Ltd* and related cases).[44]

15.43 Further, OFMA submitted that even though beneficial legislation does exist to assist franchisees, most cannot avail themselves of it because of the crippling cost of the litigation system and the economic imbalance between the parties, particularly in respect to their ability to absorb the costs of, and delays in, litigation.[45]

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39 Dr Craig Latham, Deputy Ombudsman, Australian Small Business and Family Enterprise Ombudsman, *Committee Hansard*, 21 September 2018, p. 41.

40 Franchise Council of Australia, *Supplementary Submission 29.1*, Part B: Issue 10—Dispute Resolution Mechanisms, p. 12.

41 Office of the Franchising Mediator, *Submission 37*, p. 18.

42 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 21.

43 Franchise Council of Australia, *Supplementary Submission 29.1*, Part B: Issue 10—Dispute Resolution Mechanisms, p. 12.

44 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 21.

45 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 21.

15.44 Sixth, the FCA submitted that 'there is no need for arbitration in place of litigation'.[46] OFMA pointed out that arbitration 'is not a one-size fits all scheme but can be tailored to the particular nature and type of disputes'.[47] OFMA argued that it should be possible to design a process for the resolution of non-complex matters that parties want to refer to arbitration:

> Such a system would provide access to justice for small business franchise owners and franchisees, which have failed to reach agreement at a mediation.
>
> In this way, a quick decision by an experienced industry 'expert', using a flexible determination process, can deliver a binding decision at much less cost than attempting to conduct litigation in a Federal Court.[48]

Comparison of dispute resolution systems

15.45 This section compares dispute resolution arrangements for a range of sectors:

- franchising under the Franchising Code;
- small business and family enterprises under ASBFEO;
- the grocery supply chain under the Food and Grocery Code of Conduct; and
- financial services under the newly established Australian Financial Complaints Authority (AFCA).

15.46 The dispute resolution schemes under AFCA and the Food and Grocery Code of Conduct are both newer and more comprehensive than the franchising and ASBFEO dispute resolution schemes.

15.47 Appendix 4 compares the dispute resolution schemes under the Franchising Code, ASBFEO, the Food and Grocery Code of Conduct, and AFCA.

15.48 Although not included in Appendix 4, the committee notes the Oil Code of Conduct has a determinative process and allows the Oil Code Dispute Resolution Adviser to act as an expert in making a non-binding determination. Similarly, under the Horticultural Code of Conduct, a horticultural assessor is able to make an assessment.[49]

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46 Franchise Council of Australia, *Supplementary Submission 29.1*, Part B: Issue 10—Dispute Resolution Mechanisms, p. 12; see also Mr Derek Sutherland, Private capacity, *Committee Hansard*, 8 June 2018, pp. 11–12.

47 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 21.

48 Office of the Franchising Mediation Adviser, *Supplementary Submission 37.1*, p. 21.

49 Mr Derek Minus, Franchising Code Mediation Adviser, Office of the Franchising Code Mediation Adviser; Oilcode Dispute Resolution Adviser, Office of the Oilcode Dispute Resolution Adviser, *Committee Hansard*, 8 June 2018, p. 5.

15.49 A key difference between the dispute resolution schemes compared in Appendix 4 is that, unlike the Franchising Code, the AFCA and the Food and Grocery Code of Conduct schemes include binding arbitration and the capacity to award remedies, compensation, interest and costs.

15.50 The Food and Grocery Code of Conduct also has time limits for starting investigations, resolving complaints and for appointing a mediator. The ACCC recommended that the Franchising Code and Oil Code be amended to require that mediation commence within a specific period once a mediator has been appointed. The ACCC argued for the change because in its view:

> Currently, parties can conceivably delay mediation by consistently claiming they are unavailable to attend on certain dates. While the obligation to mediate in good faith is relevant in the event a party vexatiously seeks to delay mediation, this provides no recourse at the time for the affected party who is seeking to address the cause of their initial dispute.[50]

15.51 The FCA submitted that it did not object to the ACCC's proposed amendment, but indicated that, in the FCA's view, the lack of a time limit was not a problem.[51]

15.52 The AFCA model has further additional features including:

- restrictions on either party taking legal action until alternative dispute resolution is complete; and
- the capacity to refer systemic or serious matters to regulators.

Structure of the mediation and ombudsman roles in the franchising sector

15.53 One of the issues that arose in consideration of dispute resolution in franchising was the respective roles and functions of OFMA and ASBFEO.

15.54 The ACCC submitted that duplication exists in the current mediation arrangements for franchising, and consideration should be given to consolidating the mediation advisory services within ASBFEO.[52] The ACCC explained that, in their view, the consolidation of services within a single entity would simplify the system and help increase franchisee awareness of mediation services.[53]

15.55 The ACCC acknowledged that when it considered a dispute could be resolved by mediation, it referred parties to not just OFMA, but also ASBFEO and the various small business commissioners because they all offer similar services.[54]

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50 Australian Competition and Consumer Commission. *Submission 45*, p. 15.

51 Franchise Council of Australia, *Supplementary submission 29.1*, p. 22.

52 Australian Competition and Consumer Commission, *Submission 45*, p. 13.

53 Ms Kristie Piniuta, Director, Small Business and Industry Codes, Australian Competition and Consumer Commission, *Committee Hansard*, 21 September 2018, p. 56.

54 Ms Kristie Piniuta, Director, Small Business and Industry Codes, Australian Competition and Consumer Commission, *Committee Hansard*, 21 September 2018, p. 56.

15.56 Noting that ASBFEO also provides case management and referral to specialist mediators, the Small Business Development Corporation (SBDC) suggested merging OFMA into ASBFEO. The SBDC noted that this approach would avoid the duplication of services, reduce the length of time to resolve disputes, and increase the Ombudsman's ability to detect trends.[55]

15.57 ASBFEO advised that such an arbitration scheme would provide a referral or direction service to arbitration in the same way that it currently does for mediation or conciliation.[56]

Committee view

15.58 Negotiation between franchisors and franchisees is the cheapest and most flexible process for resolving disputes and different perspectives within a franchise relationship. Disputes can range from the relatively minor through to substantial changes in the way that the franchise operates. Indeed, the committee received evidence from a major franchisor that they have robust negotiations with their franchisees and franchisee association where differing perspectives and disagreements are put on the table and worked through. To a great extent, this approach presupposes a willingness on behalf of both parties to engage in good faith about the future of the business relationship between them, as well as recognition by both parties that the continued existence of a mutually beneficial and profitable relationship underpins the negotiations. Negotiation between the parties is the first step in any healthy business relationship and, given good intentions on all sides, it has the potential to resolve many disputes. Unfortunately, the committee received evidence that a mutually agreed understanding arising from constructive approaches to negotiation is absent in particular franchise operations. Additionally, the committee was made aware of negotiations that were tokenistic in manner, such that the franchisees' concerns or views were rarely attended to.

15.59 It is also apparent that not all disputes can be resolved without outside intervention. Mediation should be the next step in the process because it allows the parties to engage in negotiation with a trained and experienced facilitator. It appears from the evidence provided to the committee that mediation is well-suited to franchising and may achieve a satisfactory resolution in up to two thirds of cases.

15.60 Nevertheless, the committee affirms the recommendation put forward by the ACCC that the Franchising Code be amended to expressly allow a mediator to undertake multi-franchisee mediations when disputes with similar issues arise. Such an amendment would improve efficiency as well as ameliorating the power imbalance that exists between franchisor and franchisee in dispute resolution.

15.61 The ACCC did not provide further information on what may constitute a 'similar issue' in its submission. The committee considers that the notion of a similar issue needs to be sufficiently broad to allow franchisees to bargain collectively on a

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55 Small Business Development Corporation, *Submission 76*, pp. 4–5.

56 Dr Craig Latham, Deputy Ombudsman, Australian Small Business and Family Enterprise Ombudsman, *Committee Hansard*, 21 September 2018, pp. 40–41.

dispute even though the disputed issue may have had a varying impact on franchisees (that is, some may have been severely impacted and others less so; or the impact may not affect all franchisees simultaneously). The committee also considers that a mediator or arbitrator should be able to make decisions for each individual franchisee's circumstances, or a decision that applies to all franchisees involved in the dispute.

15.62 However, the committee agrees with the view put forward by OFMA, namely that a necessary condition of mediation is that the parties be willing to negotiate in good faith and try to achieve an outcome. Where this condition is missing, the mediation process will fail by design. Indeed, the evidence to this inquiry included a litany of instances where one party alleged the other party failed to engage in good faith in the mediation process, knowing that the only alternative was court action which was prohibitively expensive for one of the parties. In effect, the party in the stronger position had no incentive to reach a negotiated settlement and could effectively say to the weaker party, 'take it or leave it', or 'take it to court'. To be clear, most of the allegations put to the committee alleged that the franchisor refused to negotiate in good faith with the franchisee. In other words, the franchisor had a vested interest in impeding mediation because they knew the franchisee could not afford to take them to court.

15.63 It is in these circumstances, where all the issues are unable to be resolved satisfactorily through mediation, that a determinative procedure such as arbitration is required. Arbitration works in those situations where a party wants an investigation of the facts and a determination on the evidence.

15.64 The committee accepts that arbitration is more expensive than mediation because of the time and expertise required. But, it can deliver finality to parties who want to resolve a matter and move on. And arbitration is far cheaper and more flexible than pursuing court action, and this is the critical cost comparison in any attempt to deliver justice in a timely fashion at a reasonable price. Indeed, many of the concerns raised in the committee's 2008 report have now been addressed by a number of developments in arbitration during the ensuing decade.

15.65 Furthermore, the addition of arbitration within the overall dispute resolution framework for franchising would, in all likelihood, increase the number of satisfactory outcomes achieved through mediation. In addition, referral to arbitration would help level the current uneven playing field where many franchisees cannot afford to take franchisors to court, or defend themselves, when franchisors take them court. To prevent this scenario, the committee considers that the Franchising Code should include a requirement that franchisors should have to demonstrate to the court's satisfaction that the matter could not be resolved through mediation or arbitration. If the franchisor is not able to do that, the court should direct the parties to mediation or arbitration. In this regard, the committee suggests that similar to mediation, arbitration must be conducted in Australia[57] and should only be conducted in the state or territory

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57 Competition and Consumer (Industry Codes— Franchising) Regulation 2014, sub cl. 41(2).

in which the franchisee's business is based to be consistent with existing Franchising Code provisions on the jurisdiction for settling disputes.[58]

15.66 The committee also acknowledges that there may be certain types of dispute that can only, or should only, be determined or enforced through the courts. However, acknowledging this proposition does not detract from the overall argument that the inclusion of binding arbitration would be a valuable addition to the current dispute resolution system for franchising.

15.67 In terms of how the dispute resolution scheme for franchising could be enhanced, the overwhelming bulk of the evidence from a range of stakeholders strongly argued the Franchising Code be amended to include provision for binding arbitration. In this regard, the committee notes that more modern dispute resolution schemes under the Food and Grocery Code of Conduct and the AFCA both provide for binding arbitration.

15.68 The committee notes the ACCC recommendation to amend the Franchising Code and Oil Code to require that mediation commence within a specified time period once a mediator has been appointed. The committee notes that the FCA has indicated that it does not object to the proposed amendment. The committee is satisfied by the ACCC's argument that the absence of a time limit in the past has allowed parties to frustrate dispute resolution processes. The committee therefore recommends that the ACCC recommendation be implemented for both mediation and arbitration.

15.69 Further, the committee considers that certain features of the AFCA scheme referred to earlier would be valuable additions to the dispute resolution scheme under the Franchising Code. These features are:

- the capacity to refer systemic or serious matters to regulators; and
- the restrictions on taking legal action until the dispute resolution process is complete.

15.70 While membership of the food and grocery disputes resolution process is voluntary, the committee is firmly of the view that the mandatory nature of the franchising scheme should be maintained.

15.71 Finally, the committee notes that there is the potential for the duplication of services offered by ASBFEO and OFMA. The committee recommends that the Franchising Taskforce consider the appropriateness of merging the two bodies to improve efficiency and reduce complexity for franchisees seeking to use dispute resolution. While the committee notes the evidence it received that proposed OFMA be merged into ASBFEO, the committee does not have a firm view on what the best outcome would be.

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58 Competition and Consumer (Industry Codes— Franchising) Regulation 2014, cl. 21.

Recommendation 15.1

15.72 The committee recommends that the Franchising Taskforce consider the appropriateness of:

- **merging the Office of the Franchising Mediation Adviser with the Australian Small Business and Family Enterprise Ombudsman, and that franchising be included in the name of any combined body;**
- **funding any combined small business and franchising ombudsman through an industry levy based on numbers of complaints;**
- **all franchisees under the Franchising Code of Conduct falling within the jurisdiction of the combined body if established;**
- **enhancing the powers of any combined body so that it may refer and direct parties to binding arbitration under the Franchising Code of Conduct; and;**
- **the appointment of a combined small business and franchising ombudsman as an independent assessor with the ability to review handling of disputes and the capacity to refer systemic or serious matters to regulators.**

Recommendation 15.2

15.73 The committee recommends that the dispute resolution scheme under the Franchising Code of Conduct remain mandatory and be enhanced to include:

- **the option of binding arbitration with the capacity to award remedies, compensation, interest and costs, if mediation is unsuccessful (does not exclude court action);**
- **require that mediation and then arbitration commence within a specified time period once a mediator or arbitrator has been appointed;**
- **restrictions on taking legal action until alternative dispute resolution is complete (along similar lines to those used by the Australian Financial Complaints Authority);**
- **immunity from liability for the dispute resolution body;**
- **to include a requirement that if a franchisor takes a matter straight to court, the franchisor must demonstrate to the court's satisfaction that the matter cannot be resolved through mediation, and if not the court should order the parties to mediation;**
- **the capacity for a mediator or arbitrator to undertake multi-franchisee resolutions when disputes relating to similar issues arise (as determined by the mediator or arbitrator).**