

Franchising - Canada

Material Deficiencies in Disclosure Documentation Amount to Non-disclosure

March 17 2009

[Cases](#)
[Comment](#)

Two recent Ontario Superior Court of Justice decisions have held that material deficiencies contained in disclosure documents that must be provided to prospective franchisees pursuant to the Arthur Wishart Act (Franchise Disclosure) 2000 (Ontario) amount to non-disclosure within the meaning of the act, giving rise to a franchisee's right to rescind the franchise agreement without penalty or obligation, within two years of its execution.

Cases

Sovereignty Investment Holdings Inc v 9127-6907 Quebec Inc

In *Sovereignty Investment Holdings Inc v 9127-6907 Quebec Inc* the franchisee made an application for rescission of the franchise agreement that it had entered into with the franchisor for the operation of a restaurant. In its application the franchisee alleged that the documentation provided to it by the franchisor did not comply with various material disclosure requirements under both the Ontario act and the regulations adopted pursuant to the same. The franchisee essentially identified and alleged 19 deficiencies in the documents provided by the franchisor.

The Ontario Superior Court of Justice examined each of the alleged deficiencies and ultimately concluded that four of them were sufficiently material to amount to non-disclosure under the Ontario act. In particular, the franchisor's failure to provide its financial statements and its statement setting out the basis and assumptions for earnings projections was fatal. Furthermore, the fact that the documentation was provided to the franchisee in various packages rather than in a single document also constituted a material deficiency. Finally, the documentation provided did not include a signed and dated certificate of the franchisor, certifying that the disclosure documents contained no untrue information, representations or statements and included every material fact, financial statement, statement and other information required under both the Ontario act and the related regulations. Based on these deficiencies, the court granted the franchisee's application to rescind the franchise agreement on the basis of the franchisor's failure to comply with the substantive disclosure requirements under the Ontario act.

6862829 Canada Ltd v Dollar It Ltd

In *6862829 Canada Ltd v Dollar It Ltd* the Ontario Superior Court of Justice took a similar stance and held that the material deficiencies contained in the documentation provided by a franchisor to a prospective franchisee did not satisfy the essential disclosure requirements under the Ontario act, therefore also giving rise to the franchisee's right to rescind the franchise agreement.

In this second decision the material deficiencies identified included the absence of:

- financial statements and a balance sheet;
- the signed and dated certificate of the franchisor;
- disclosure of a pending lawsuit against the franchisor; and
- a copy of an existing offer to lease.

The court concluded that the missing information and documentation was material enough to amount to non-disclosure.

In each of the foregoing decisions the respondent franchisors argued that even if the

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disclosure documents were not entirely in compliance with the Ontario act, the deficiencies did not amount to non-disclosure, thereby allowing the franchisee to rely upon the two-year limitation period under the Ontario act. However, in both cases the franchisors' arguments were rejected and, after reiterating the objective of the Ontario act (ie, to ensure full and complete disclosure), the court held that the alleged deficiencies were in fact material enough to amount to non-disclosure.

Comment

In both *Sovereignty Investment Holdings* and *6862829 Canada Ltd* the Ontario Superior Court of Justice appeared to reiterate its position in previously rendered decisions, in which it also held that failure to include material elements of disclosure amounted to non-disclosure within the meaning of the Ontario act. The Ontario Superior Court of Justice appears to have taken a similar position to the Alberta Court of Appeal, which also recently held in *Hi Hotel Limited Partnership v Holiday Hospitality Franchising Inc* that the absence of a signed and dated certificate of the franchisor was fatal to the validity of the franchise agreement (for further details please see "[Failure to Comply with Disclosure Requirements Leads to Rescission](#)"). However, the Ontario Superior Court of Justice did nuance its position by stating clearly that a number of minor deficiencies cannot, even on a cumulative basis, amount to non-disclosure.

In view of the foregoing and in order to minimize the risks of rescission, it is imperative for franchisors to ensure that disclosure documentation to be provided to prospective franchisees is submitted in a single document, meets all requirements under franchise legislation and is supported by a signed and dated certificate of the franchisor, certifying the accuracy and completeness of the information provided.

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