

Franchising - Canada

Franchisors as advisers? Proposed changes to franchise disclosure in Ontario

Contributed by [Lapointe Rosenstein Marchand Melançon LLP](#)

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As of October 12 2010, Bill 102, the Arthur Wishart Amendment Act (Franchise Disclosure) 2010, has passed the second of three readings before the Legislative Assembly of Ontario, Canada's largest province. This proposed amendment could change the existing franchise legislation by greatly increasing the quantity and scope of information that a franchisor would be required to communicate to prospective franchisees.

Content

Bill 102 adds a single section to the Arthur Wishart (Franchise Disclosure) Act 2000 (SO 2000, c 3). This new Section 5.1 would require a franchisor to provide a prospective franchisee with an "educational document" whose scope goes far beyond that of the disclosure document already required by law. The content of this educational document includes many elements which have traditionally been considered part of the potential franchisee's own due diligence. For example, the educational document is meant to include:

- self-evaluation criteria for franchisees to help them determine whether they have the capital, skills, education and experience to run the franchise successfully, whether the franchise being considered is the best suited for them and whether they in fact need a franchise to be successful in the line of business being considered;
- the franchisor's selectivity in choosing franchisees;
- information regarding the goods and services, such as their uniqueness, whether demand is reasonable, competitive pricing and supply guarantees;
- sales potential and future growth potential of the sales territory;
- an offer to provide a list of current franchisees in the area and a list of topics to be discussed with them;
- an explicit recommendation that the prospective franchisee have a lawyer and accountant review the franchise agreement; and
- discussion of various other issues, such as deferral of royalties, flexibility in franchisor systems, controls and policies, and compensation for goodwill built up by the franchise.

Issues

Some have argued that this amendment legally requires the franchisor to act as a consultant and adviser to the prospective franchisee, guiding the latter's business decision as much as ensuring that the franchisor's own interests are protected.

Beyond the overall weight of the proposed information regime, of particular note is the inclusion of many broad and undefined terms, such as 'new innovations', 'unique goods and services', 'reasonable demand', 'fair price', 'future growth potential' and 'hidden or unexpected costs'. These appear likely to give rise to differing interpretations and contentious relationships between the parties while the significance of the communicated information is worked out. It remains to be seen whether the educational document will remain purely informative and predictive, or whether it will be elevated to the level of a representation or warranty.

In addition, the amendment is silent as to the consequences for franchisors that provide an incomplete or inaccurate educational document, or none at all. Nor is it specified whether the right of rescission, available to franchisees if the disclosure

Authors

[David Kyffin](#)

[Bruno Floriani](#)



document does not fulfil the legal requirements, also applies to the educational document.

Legislative progress and reaction of franchisor community

Immediately following Bill 102's first reading on September 15 2010, the Canadian Franchise Association began communicating with Ontario legislators to put forth franchisors' points of view, specifically highlighting the issues outlined in this update and raising a broader practical argument: the risk of over-reliance by inexperienced entrepreneurs on the education document as their sole source of information, to the exclusion of adequate due diligence on their part. Partial duplication with the already demanding Arthur Wishart disclosure regime and compliance costs were also underlined as justifying a rethink of the proposed amendment.

Despite these efforts, Bill 102 passed second reading on September 23 2010 and now rests with the Standing Committee on Finance and Economic Affairs, where public consultations are expected to be held. As a private member's bill, the bill does not enjoy the explicit support of the government, which would normally make improbable its passing into law.

However, since this particular bill has sponsors from all three parties represented in the Legislative Assembly, it may not be too far-fetched to speculate that it might be headed for adoption into law before the end of the current legislative session.

For further information on this topic please contact [Bruno Floriani](#) at Lapointe Rosenstein Marchand Melançon LLP by telephone (+1 514 925 6300), fax (+1 514 925 9001) or email (bruno.floriani@lrm.com).

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