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The International Comparative Legal Guide to:

# Franchise 2017

**3rd Edition**

A practical cross-border insight into franchise law

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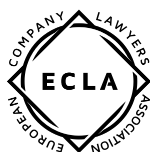


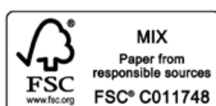


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# Canada

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## 1 Relevant Legislation and Rules Governing Franchise Transactions

### 1.1 What is the legal definition of a franchise?

There are six provinces in Canada which have enacted franchise-specific legislation. Franchise legislation in five of the provinces, namely the Arthur Wishart Act in the Province of Ontario (the Ontario Act), the Prince Edward Island Franchises Act (PEI Act), the New Brunswick Franchises Act (the NB Act), the Manitoba Franchises Act (the Manitoba Act) and the British Columbia Franchise Act (the BC Act, set to come into force on February 1, 2017), generally defines a 'franchise' as a right to engage in a business where the franchisee is required to make one or several payments to the franchisor in the course of operating the business or as a condition of acquiring the franchise or commencing operations, and in which the franchisee is granted either:

- the right to sell goods or services substantially associated with the franchisor's trademarks in circumstances where the franchisor or any of its associates has significant control over, or offers significant assistance in, the franchisee's method of operation; or
- representational or distribution rights to sell goods or services supplied by the franchisor or its designated supplier, and the franchisor (or any person it designates) provides location assistance to the franchisee.

In Alberta's Franchises Act (the Alberta Act), a 'franchise' is defined as a right to engage in a business:

- in which goods or services are sold, offered for sale or distributed under a marketing or business plan substantially prescribed by the franchisor or any of its associates and that is substantially associated with any of its trademarks, service marks, trade names, logotypes or advertising; and
- that involves a continuing financial obligation of the franchisee to the franchisor or any of its associates and significant continuing operational controls by the latter on the operation of the franchised business, or the payment of any franchise fee (the latter fee being defined as any direct or indirect payment to purchase or to operate a franchise), and includes a master franchise and sub-franchise.

Given the breadth of these definitions, Canadian franchise legislation may cover a number of business agreements and traditional distribution or licensing networks that would not typically qualify as franchise agreements, as the term 'franchise agreement' may be understood in other jurisdictions.

### 1.2 What laws regulate the offer and sale of franchises?

The offer and sale of franchises in Canada is regulated by the provinces rather than by the federal government. Currently adopted franchise legislation is limited to the Alberta Act, the Ontario Act, the PEI Act, the NB Act, the Manitoba Act and the BC Act, which is set to come into force on February 1, 2017 (collectively, the Canadian Franchise Acts). The Civil Code of Quebec also contains provisions applicable to all contracts governed by Quebec law, including franchise agreements. No other province or territory of Canada has regulated the offer and sale of franchises through franchise-specific legislation.

### 1.3 If a franchisor is proposing to appoint only one franchisee/licensee in your jurisdiction, will this person be treated as a "franchisee" for purposes of any franchise disclosure or registration laws?

Yes, even a grant to a single franchisee would fall under the definition of a 'franchise' in the Canadian Franchise Acts and would be subject to its application. However, the Acts, other than the Alberta Act, provide for a specific exemption which applies to arrangements whereby a licensor grants one single licensee a licence for a specific trademark, trade name, logo or advertising or other commercial symbol where such licence is the only one of its general nature and type to be granted in Canada.

### 1.4 Are there any registration requirements relating to the franchise system?

There are no registration requirements for establishing a franchise system in Canada. A franchisor is not required to register before offering franchises for sale, nor is there a requirement that disclosure documents or other materials be registered.

### 1.5 Are there mandatory pre-sale disclosure obligations?

A franchisor governed by any of the Canadian Franchise Acts must furnish a prospective franchisee with a disclosure document no fewer than 14 days before the earlier of the signing by the prospective franchisee of the franchise agreement or any other agreement relating to the franchise, or the payment of any consideration by or on behalf of the prospective franchisee to the franchisor or any of its associates relating thereto.



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All of the Canadian Franchise Acts, other than the Ontario Act, exclude confidentiality and site selection agreements from the definition of franchise agreements for the application of the disclosure requirements. In addition, the Alberta Act exempts agreements that only contain terms and conditions relating to a fully refundable deposit (that is, a deposit that does not exceed 20% of the initial franchise fee and is refundable without any deductions or any binding undertaking of the prospective franchisee to enter into any franchise agreement).

Under each of the Canadian Franchise Acts, a franchisor must also furnish a prospective franchisee with a description of any 'material change' that occurs after disclosure has been provided, as soon as practicable after the change has occurred and prior to the earlier of the signing of any agreement or the payment of any consideration by the prospective franchisee in relation to the franchise. A 'material change' is defined as a change (even if not yet implemented in certain cases) in the business, operations, capital or control of the franchisor or any of its associates, or in the franchise system, which change would reasonably be expected to have a significant adverse effect on the value or price of, or on the decision to acquire, the franchise.

In Quebec, the general duty of good faith in contracts is established by the Civil Code of Quebec and extends to pre-contractual negotiations. The obligation of pre-contractual good faith has been interpreted as imposing a positive obligation to inform a contracting party of any information which could affect its decision to enter into a contract, including in franchising. In particular, the courts have interpreted the civil law's general duty of good faith as imposing an obligation on franchisors to inform potential franchisees of any information in their possession that may have a decisive influence on the franchisee's will to contract, including internal documents, feasibility studies, aptitude tests and the like.

### 1.6 Do pre-sale disclosure obligations apply to sales to sub-franchisees? Who is required to make the necessary disclosures?

Each of the Canadian Franchise Acts imposes the obligation to disclose upon 'franchisors', the definition of which includes a sub-franchisor with regard to its relationship with a sub-franchisee. Accordingly, pre-sale disclosures must be made to a sub-franchisee by the sub-franchisor in accordance with the same procedural and substantive requirements that apply to franchisors with regard to their relationships with their franchisees. Any applicable exemptions would apply similarly. Moreover, information regarding a sub-franchisor's relationship with the franchisor must be disclosed to a prospective sub-franchisee, but only to the extent that such information constitutes a material fact or is necessary for the sub-franchisor to properly acquit itself of its duty to furnish the information expressly prescribed by the relevant statutory and regulatory provisions governing disclosure.

### 1.7 Is the format of disclosures prescribed by law or other regulation, and how often must disclosures be updated? Is there an obligation to make continuing disclosure to existing franchisees?

The regulations under each of the Canadian Franchise Acts require that general information concerning the franchisor be included in the relevant disclosure document. Such information includes the history of the franchisor, the business background of its directors, the general partners and the officers of the franchisor, and whether any of those persons has been subject to bankruptcy or insolvency proceedings or has been previously convicted of fraud or unfair or deceptive business practices. While substantively similar, the list of information that must be disclosed under each of the Canadian Franchise Acts is not identical.

Financial statements must be included in the disclosure document governed by the Canadian Franchise Acts, although the requirements set out in the regulations adopted under the Alberta Act (Alberta Regulations) differ substantially from those adopted under the other Canadian Franchise Acts. For instance, the latter regulations compel the inclusion in each disclosure document of statements regarding initial 'risk factors', whereas those are not required under the Alberta Regulations.

The disclosure document must also include all 'material facts'. This encompasses any information about the business, operations, capital or control of the franchisor, its associates or the franchise system that would reasonably be expected to have a significant effect on the decision to acquire, or the value of, the franchise.

None of the Canadian Franchise Acts requires continuing disclosure beyond the signing of the franchise agreement or the payment of any consideration by the prospective franchisee to the franchisor with respect to the franchise, whichever occurs first. Before this point, any material change, defined as any change or prescribed change that could reasonably be expected to have a significant adverse effect on the value or the price of the franchise to be granted or on the decision to acquire the franchise, must be brought to the prospective franchisee's attention as soon as practicable.

### 1.8 Are there any other requirements that must be met before a franchise may be offered or sold?

No. Unlike in other jurisdictions, there are no particular operational requirements in Canada, such as for a franchisor to be in business for a specific amount of time, operating a minimum number of corporate locations or conducting its business in Canada for any prescribed period.

### 1.9 Is membership of any national franchise association mandatory or commercially advisable?

Although there is no requirement to become a member of the Canadian Franchise Association (CFA), membership of the CFA typically lends credibility to a franchise, given that franchisors are required to meet the definition of a franchise in order to qualify as members, provide proper documentation in support of their membership application, and commit to abide by the CFA Code of Ethics.

### 1.10 Does membership of a national franchise association impose any additional obligations on franchisors?

Membership of the CFA requires that franchisors use the CFA disclosure document guide and commit to giving potential franchisees all the information they need to make a viable business decision. The CFA also requires its members to adhere to the CFA Code of Ethics (a copy of which can be found at the following website: http://www.cfa.ca/about-our-members/cfa-code-of-ethics/). By becoming a member, a franchisor agrees to comply with the spirit of the Code of Ethics in the context of its operations, including by:

- fully complying with federal and provincial laws, and with the policies of the Canadian Franchise Association;
- providing full and accurate written disclosure of all material facts and information in advance to prospective franchisees within a reasonable time prior to executing a binding agreement;
- selecting and accepting only those franchisees that possess the adequate basic skills, education, personal qualities and financial resources to perform under the requirements of the franchise;




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- providing reasonable guidance, training, support and supervision over the business activities of franchisees;
- making reasonable efforts to resolve grievances and disputes through fair/reasonable direct communication and through alternative dispute resolution;
- encouraging prospective franchisees to seek legal, financial and business advice prior to signing the franchise agreement;
- encouraging prospective franchisees to contact existing franchisees to gain a better understanding of the requirements and benefits of the franchise; and
- encouraging open dialogue with franchisees through franchise advisory councils and other communication mechanisms.

### 1.11 Is there a requirement for franchise documents or disclosure documents to be translated into the local language?

The language of business, contracts (including franchise agreements) and disclosure would generally be English throughout Canada. However, in Quebec, the Charter of the French Language compels businesses to prepare franchise agreements and other documents (including disclosure documents from other provinces) in French for use in the Province of Quebec unless the parties have expressly agreed that another language may be used, which is not uncommon in circumstances where both parties are comfortable in another language.

## 2 Business Organisations Through Which a Franchised Business can be Carried On

### 2.1 Are there any foreign investment laws that impose restrictions on non-nationals in respect of the ownership or control of a business in your jurisdiction?

Pursuant to the Investment Canada Act, foreign business entities seeking to acquire or establish a Canadian business are required to notify Industry Canada no later than 30 days following such acquisition or establishment. Although most franchised businesses will escape the application of these requirements based on the nature of the transactions at issue, an onerous and thorough review process applies to non-World Trade Organization investors where the asset value of the acquired Canadian business is at least C$5 million for direct acquisitions or C$50 million for indirect acquisitions. However, the C$5 million threshold will apply to indirect acquisitions where the asset value of the acquired Canadian business represents greater than 50% of the asset value of the global transaction. The review threshold for World Trade Organization investors was raised to an ‘enterprise value’ of C$600 million as of April 24, 2015. The review threshold will increase to C$800 million in enterprise value starting April 24, 2017 and will increase again to C$1 billion as of April 24, 2019.

Furthermore, it is important to note that certain corporate statutes, such as the Canadian Business Corporations Act and the Ontario Business Corporations Act, set out requirements as to the residency of directors pursuant to which at least one director (or 25% of the directors if there are more than four) must be a Canadian resident. The corporate statutes of other provinces, such as British Columbia and Quebec, do not impose similar residency requirements.

### 2.2 What forms of business entity are typically used by franchisors?

There are several different vehicles available to foreign franchisors who wish to carry on business in Canada, each with varying tax and corporate consequences.

The preferred choice of vehicle used for the expansion of a foreign franchise system into Canada is the incorporation of a Canadian subsidiary. By using a Canadian subsidiary, the franchisor has a local direct physical presence and indicates to the general public that it has made a commitment to Canada. Foreign franchisors may instead wish to enter the Canadian market by franchising directly from their country without the creation of a permanent establishment in Canada, thus avoiding being considered by the Canadian tax authorities as carrying on business in Canada.

### 2.3 Are there any registration requirements or other formalities applicable to a new business entity as a pre-condition to being able to trade in your jurisdiction?

Registration mechanisms for forming and maintaining business entities in Canada are generally straightforward, requiring little more than the payment of prescribed fees and the filing of specific corporate or business registry forms that describe, *inter alia*, the nature of the business, its structure, the scope of its undertakings and basic information regarding its shareholders and directors. Annual filings are also typically required in each of the provinces in which a business entity carries on business and, in the case of corporations incorporated under the CBCA, at the federal level.

## 3 Competition Law

### 3.1 Provide an overview of the competition laws that apply to the offer and sale of franchises.

The Competition Act sets forth penal and civil recourses with respect to various practices, including those identified as conspiracies and collusion, abuse of dominance, price maintenance, promotional allowances and price discrimination, misleading advertising, deceptive marketing and pyramid selling, refusal to deal, exclusive dealing, tied selling, as well as certain other vertical market restrictions.

While the penal provisions of the Competition Act impose a higher burden of proof, their violation grants injured parties the right to sue for damages caused by such practices; those damages are restricted to actual loss and costs. Fines are also applicable for certain types of offences. On the other hand, reviewable practices are civil in nature and are subject to the exclusive jurisdiction of the Competition Tribunal, upon the request of the commissioner of competition or at the request of a private party with leave from the Competition Tribunal to that effect. In the latter case, it should be noted that private litigants may only seek redress through orders, as monetary awards are not provided for. The Competition Tribunal may make orders for a reviewable trade practice to cease, or compel a business to accept a given customer or order on reasonable trade terms.

### 3.2 Is there a maximum permitted term for a franchise agreement?

There is no maximum term for a franchise agreement. Parties will be free to contract for the length of the term and the number of renewals they wish. In Canada, though uncommon, a franchise agreement can even be perpetual or perpetually renewable.

The typical term of franchise agreements in Canada is between five and 10 years. Particularly in the retail and restaurant industries, franchise agreements are usually coterminous with the lease of the franchisee’s premises.



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### 3.3 Is there a maximum permitted term for any related product supply agreement?

There is no maximum permitted term for a supply agreement.

### 3.4 Are there restrictions on the ability of the franchisor to impose minimum resale prices?

Restrictions on minimum resale prices may qualify as price maintenance and therefore be a reviewable trade practice under the Competition Act. The threshold for enforcement authorities to apply sanctions on the basis of price maintenance requires that the franchisor's conduct be likely to have an adverse effect on competition. Providing a minimum resale price or advertised price may be considered evidence of undue influence by the franchisor and invite review by the Competition Bureau.

However, franchisors may impose maximum prices as long as the latter are clearly referred to and defined in the franchise agreement and are not construed by courts as demonstrating intent to establish a minimum resale price. Accordingly, it is always prudent for franchisors to include disclaimers, whether in advertising or on packaging, to the effect that franchisees are at liberty to establish their own resale prices. Furthermore, it is preferable to provide contractually that prices are only suggested and that the failure of the franchisee to adhere to the suggested prices will not result in termination of the franchise agreement or detrimentally affect the relationship between the parties.

### 3.5 Encroachment – are there any minimum obligations that a franchisor must observe when offering franchises in adjoining territories?

While it might be a strategy to entice potential franchisees, granting exclusive territories to franchisees is not a legal requirement. If a franchisor does provide a franchisee with an exclusive territory, such a right may be contingent on the franchisee maintaining certain performance targets. However, it is important to prevent situations where the franchisor's exploitation of different distribution channels could unreasonably compete with its franchise network. Such a situation could potentially be interpreted as bad faith or a failure to have due regard for franchisees' success. It is therefore important to explicitly reserve rights in the franchise agreement and expressly allocate as many existing and potential distribution channels as possible between the franchisor and the franchisee, without ignoring the basic tenets of good faith which may preclude unreasonable forms of direct competition with franchisees.

### 3.6 Are in-term and post-term non-compete and non-solicitation of customers covenants enforceable?

Non-compete and non-solicitation covenants will be enforceable unless they are unreasonable. In order to comply with the reasonableness requirement, such clauses must protect a commercially legitimate interest of the franchisor and must not be broader – in geographical area, time period or scope – than what is necessary to protect the franchisor's interests. In addition, it is important to note that if a court determines that a non-competition clause is unreasonable, it will simply strike down the covenant in its entirety.

In-term non-compete covenants can have a far-reaching scope as compared to post-term non-competes, which are more strictly interpreted. In Quebec, the reasonable geographic limitation is imposed on both in-term and post-term non-competition provisions, although the latter can be broader.

On the other hand, non-solicitation clauses can be more broadly drafted than non-competition clauses, as they are considered less of a constraint on a person's ability to earn a living. Accordingly, the geographical restriction and duration of the covenant are not subject to the same strict scrutiny as non-competition covenants. There is, however, a requirement that the persons who are not to be solicited be clearly identifiable.

In the event of a violation of a non-compete or non-solicitation provision, Canadian courts will generally be willing to grant interlocutory injunctions if the following conditions are met: (i) there is a serious issue to be tried; (ii) the claimant will suffer irreparable harm if the injunction is not granted; and (iii) the balance of inconvenience lies in favour of granting the injunction.

## 4 Protecting the Brand and other Intellectual Property

### 4.1 How are trade marks protected?

The Trademarks Act (Canada) defines a trademark as a 'mark that is used by a person for the purpose of distinguishing or so as to distinguish wares or services manufactured, sold, leased, hired or performed by him from those manufactured, sold, leased, hired or performed by others, a certification mark, a distinguishing guise or a proposed trademark'. As such, distinctiveness is central to the definition and a trademark need not be registered to be valid, or even licensed, in Canada. Nonetheless, registration with the Canadian Office of Intellectual Property has the advantage of providing nationwide protection of the registered trademark. An application for registration may be filed on several bases, namely on previous use or making known in Canada, proposed use in Canada or foreign use and registration. However, it is important to note that Canada has adopted amendments to its trademark law (in order to enable accession to the Madrid Protocol), which are set to come into effect in 2018. One of the material amendments would be the removal of the requirement that a trademark be 'used' prior to registration, ultimately allowing applicants to register trademarks in Canada without having used the mark anywhere in the world. It would therefore be prudent for trademark owners to protect their priority and be the first to file their marks in Canada prior to the implementation of these amendments.

Remedies available following the breach of exclusive use clauses or the use of a confusing trademark range from injunctive remedies to passing-off actions that may be instituted before either the Federal Court of Canada or the provincial court having jurisdiction.

### 4.2 Are know-how, trade secrets and other business-critical confidential information (e.g. the Operations Manual) protected by local law?

There is no statutory protection of know-how in Canada. Parties must rely on common law tort and contractual undertakings to protect know-how from unauthorised disclosure or use. Accordingly, the nature of the confidential information that a franchisor wishes to protect, as well as the legal consequences arising as a result of its dissemination, should be clearly identified by the contracting parties in their franchise agreement.





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### 4.3 Is copyright (in the Operations Manual or in proprietary software developed by the franchisor and licensed to the franchisee under the franchise agreement) protected by local law?

In Canada, every original literary, dramatic, musical and artistic work is automatically granted copyright protection. While it is possible to register a copyright under the federal Copyright Act, it is usually not necessary, since copyright protection is granted automatically by law. However, registration will create a presumption that copyright exists and that the registrant is the owner of the copyright. Registering a copyright may therefore overcome a difficult evidentiary hurdle and spare significant expenses in the event that the copyright holder wishes to sue for copyright infringement and is required to prove ownership of the copyright.

In situations where work is being created by third parties, such as a software developer, it is essential to require the third party to enter into a written contract assigning ownership of the work developed for the franchisor. In addition to agreeing to assign ownership of the work, developers must assign ownership of the work to the franchisor after the work has been developed. This two-step process is essential to ensure that franchisors are the legal owners of the copyright in work created by independent third parties. Furthermore, authors of work should also be required to provide franchisors with written waivers of their moral rights in the work. Such moral rights are different from copyright and include the rights to have one's name associated with the work and to prevent the work from being modified or associated with a product or business.

## 5 Liability

### 5.1 What are the remedies that can be enforced against a franchisor for failure to comply with mandatory disclosure obligations? Is a franchisee entitled to rescind the franchise agreement and/or claim damages?

Disclosure requirements are typically enforced by the affected parties rather than by government agencies, as the interests are generally considered to be private rather than public. Under each of the Canadian Franchise Acts, an action for damages or rescission may be instituted by the franchisee for non-compliance with mandatory disclosure obligations. The NB Act provides that a party to a franchise agreement may, in the event of a dispute with another party to such agreement, trigger a mandatory alternative dispute resolution mechanism (mediation). The foregoing does not, however, preclude any party to such franchise agreement from availing itself of other recourses available under contract or at law.

**Rescission**

Pursuant to all Canadian Franchise Acts, other than the Alberta Act, a franchisee may rescind the franchise agreement without penalty or obligation: (a) 'for late disclosure', no later than 60 days after receiving the disclosure document if the franchisor failed to provide said document or a statement of material change within the prescribed time or if the contents of the disclosure document do not satisfy statutory requirements; or (b) 'for absence of disclosure', no later than two years after entering into the franchise agreement. In either case, within 60 days of the effective date of rescission the franchisor must:

- purchase from the franchisee any remaining inventory, supplies and equipment purchased pursuant to the franchise agreement, at a price equal to the purchase price paid by the franchisee, and refund any other money paid by the franchisee; and
- compensate the franchisee for the difference between any losses incurred in acquiring, setting up and operating the franchise, and any amounts paid or refunded pursuant to the preceding paragraph.

Should a franchisor fail to provide the disclosure document as required under the Alberta Act, the prospective franchisee is entitled to rescind the franchise agreement by giving a cancellation notice to the franchisor or its associate, as the case may be, no later than the earlier of 60 days after receiving the disclosure document or two years after the grant of the franchise.

The franchisor does not have an obligation to purchase any of the franchisee's assets under the Alberta Act but must instead, within 30 days after receiving a cancellation notice, compensate the franchisee for any net losses incurred by the latter in acquiring, setting up and operating the franchised business.

**Damages**

Pursuant to all Canadian Franchise Acts, other than the Alberta Act, if a franchisee suffers a loss because of a misrepresentation contained in the disclosure document or in a statement of a material change or as a result of the franchisor's failure to comply with any disclosure requirements, the franchisee has a right of action for damages against the franchisor, the franchisor's broker (if any), the franchisor's associates, every person who signed the disclosure document or statement of material change (and, under the Ontario Act, the franchisor's agent), all of whom are jointly and severally liable.

Under the Alberta Act, a franchisee who suffers a loss resulting from a misrepresentation contained in a disclosure document has a right of action for damages against the franchisor and every person who signed the disclosure document, on a joint and several basis.

### 5.2 In the case of sub-franchising, how is liability for disclosure non-compliance or for misrepresentation in terms of data disclosed being incomplete, inaccurate or misleading allocated between franchisor and master franchisee? If the franchisor takes an indemnity from the master franchisee in the Master Franchise Agreement, are there any limitations on such an indemnity being enforceable against the master franchisee?

Liability is imposed on franchisors and sub-franchisors for misrepresentations contained in a disclosure document, although the extent and scope of such liability is contingent upon the provisions and wording of the applicable franchise legislation. Where a franchisor and a sub-franchisor are found liable for misrepresentations contained in a disclosure document, their liability will be of a joint and several nature. An indemnity will be invalid to the extent that it provides for the release or waiving of obligations owed by the franchisor to its sub-franchisee under the Canadian Franchise Acts (see question 5.3).

### 5.3 Can a franchisor successfully avoid liability for pre-contractual misrepresentation by including disclaimer clauses in the franchise agreement?

Under Canadian franchise law, covenants which have the effect of waiving or releasing franchisors from its obligations to franchisees or sub-franchisees granted by the applicable law are void. Therefore, a franchisor cannot contract out of its duty of good faith and disclosure obligations. In Quebec, a contractual disclaimer will generally be enforceable except in cases of fraud or intentional or gross fault but, in the context of a franchise agreement that is characterised as an adhesion contract, it is possible that such clauses may be considered abusive and unenforceable in certain circumstances.





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**5.4 Does the law permit class actions to be brought by a number of allegedly aggrieved claimants and, if so, are class action waiver clauses enforceable?**

Canadian Franchise Acts specifically provide for franchisees' right to associate. However, such legislative provisions do not protect franchisees' right to class action proceedings, which may be waived validly by contract. Nonetheless, in the presence of a mandatory arbitration clause, class action waivers have been given effect by Canadian courts.

## 6 Governing Law

**6.1 Is there a requirement for franchise documents to be governed by local law? If not, is there any generally accepted norm relating to choice of governing law, if it is not local law?**

Under the Canadian Franchise Acts, a choice of law provision which attempts to contractually restrict the application of local laws will be void. Where the Canadian Franchise Acts do not apply, Canadian courts will generally recognise and uphold the parties' choice of foreign governing law, provided that there is a sufficient nexus to the parties' relationship. However, a choice of foreign governing law made with a view to avoiding the consequences of the applicable provincial laws of any Canadian jurisdiction will generally be considered invalid. Furthermore, where the applicable law is that of any province in Canada, the Vienna Convention on the International Sale of Goods will automatically apply in respect of sales of goods by foreign franchisors who are nationals of any other signatory nation, unless expressly set aside by the parties in the contract.

**6.2 Do the local courts provide a remedy, or will they enforce orders granted by other countries' courts, for interlocutory relief (injunction) against a rogue franchisee to prevent damage to the brand or misuse of business-critical confidential information?**

Foreign judgments rendered by the foreign court with proper jurisdiction and which provide for monetary awards are typically recognised and enforced in Canada. Conversely, if the decision is non-monetary, such as an injunction, it is unlikely that a Canadian court will recognise and enforce such judgment.

Canada is a signatory party of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards. As a result, there are fewer defences to enforcement of a foreign arbitral award than to that of a foreign judgment. Canada is also a signatory to the UNCITRAL Arbitration Rules and both the federal and provincial governments have adopted substantially similar legislation.

## 7 Real Estate

**7.1 Generally speaking, is there a typical length of term for a commercial property lease?**

There is no typical length of term for a commercial property lease, though terms of at least 10 years may often be observed for established brands. Renewal rights for additional periods of five to 10 years are not uncommon. Of course, factors such as the strength of the tenant's trademark, the location and the type of shopping centre influence lengths of terms. Barring exceptional circumstances, one would typically not encounter terms that are shorter than five years or longer than 15 years.

**7.2 Is the concept of an option/conditional lease assignment over the lease (under which a franchisor has the right to step into the franchisee/tenant's shoes under the lease, or direct that a third party (often a replacement franchisee) may do so upon the failure of the original tenant or the termination of the franchise agreement) understood and enforceable?**

Conceptually, yes, an option/conditional lease assignment over the lease is understood in Canadian law and enforceable in Canada. However, it is not unusual for the franchisor to be the tenant under a head lease and for it to have a broad right to sublet the premises to a franchisee.

**7.3 Are there any restrictions on non-national entities holding any interest in real estate, or being able to sub-lease property?**

In general, non-national entities are entitled to hold any interest in real estate and to lease and sub-lease property in Canada. Few restrictions apply and they are almost exclusively related to agricultural or cultural land.

**7.4 Give a general overview of the commercial real estate market. Specifically, can a tenant reasonably expect to secure an initial rent free period when entering into a new lease (and if so, for how long, generally), or are landlords demanding "key money" (a premium for a lease of a particular location)?**

As is the case with the Canadian economy in general, there is regional disparity in terms of the market for leased commercial retail space. That market is typically measured by discrete urban centres, given the concentration of the Canadian population in major cities, with lower vacancy rates in high-end shopping centres and other desirable locations. For prime locations, landlords may actively favour tenants with an international reputation or top-tier Canadian brands, together with staple tenants that are considered 'must haves' for any shopping centre for the sake of synergies and completeness of the tenant mix. Although always subject to the law of supply and demand, we have not observed tenants of such calibre being asked for key money or given initial rent-free periods covering actual retail operations, though rent-free fixture periods of between one and six months, advances by landlords for tenant improvements and, at times, additional scope for a landlord's work have been observed. One must assume, however, that each of the latter are factored into the rental rates being charged.

## 8 Online Trading

**8.1 If an online order for products or request for services is received from a potential customer located outside the franchisee's exclusive territory, can the franchise agreement impose a binding requirement for the request to be re-directed to the franchisee for the territory from which the sales request originated?**

Franchisors may grant exclusive territorial rights, including in respect of online channels, to franchisees. In such cases, for example, if a franchisee in Ontario were to receive an order from a




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customer in Quebec, the Ontario franchisee could be contractually required to redirect the order to the Quebec franchisee. Given the franchisor's central role in allocating territories, it could be required to intervene in the context of any enforcement of rights of this nature.

### 8.2 Are there any limitations on a franchisor being able to require a former franchisee to assign local domain names to the franchisor on the termination or expiry of the franchise agreement?

There are no limitations on franchisors requiring franchisees to assign local domain names upon termination or expiry of the franchise agreement. The obligation to assign (typically for a nominal consideration) should, however, be expressly stated in the franchise agreement. Best practice would include having a franchisee sign an assignment in advance, which takes effect upon termination or expiry.

## 9 Termination

### 9.1 Are there any mandatory local laws that might override the termination rights that one might typically expect to see in a franchise agreement?

There are no legal restrictions on the parties' rights to contractually provide for termination rights and the consequences arising upon termination. However, Canadian courts generally do not condone terminations for technical or immaterial breaches (except if the specific breach is an expressly stated ground entitling a party to terminate). In any event, courts may require that a material breach of the agreement be proven in order to permit its termination, and may intervene in cases where termination has been exercised in bad faith.

## 10 Joint Employer Risk and Vicarious Liability

### 10.1 Is there a risk that a franchisor may be regarded as a joint employer with the franchisee in respect of the franchisee's employees? If so, can anything be done to mitigate this risk?

Canada has recognised the 'common employer' principle, which considers whether two companies function 'as a single, integrated unit' in order to attribute liability. This principle is most often cited in wrongful dismissal cases by employees who allege being employed by a group of entities, thereby enticing courts to look beyond corporate structures in order to determine the 'legitimate entitlements' of wrongfully dismissed employees. The principle may also find application in connection with workplace health and safety and benefit programmes (including pension plans and collective insurance). The test for determining whether a common employment relationship exists in Canada ultimately relies on whether there is a sufficient degree of relationship between the different legal entities for the purpose of determining liability for obligations owed to employees. The common employer principle can be contrasted with the 'joint employer' concept recently recognised in the United States, which has a more far-reaching effect by attributing liability to franchisors who possess any control, even indirectly, over the franchise employees' working conditions, regardless of whether such control is actually exercised. In the event that the 'joint employer' concept would be imported into Canadian law, by way of legislative amendments or case law, most franchise relationships would likely fall under its application, as this broad notion of control – encompassing control over employment conditions and policies – is often present, as it serves the purpose of ensuring brand uniformity and consistency, which are fundamental principles of franchising.

The principles applicable to related and common employment in Canada may also result in an extension of franchisor liability in connection with human rights and discrimination issues. In this regard, a handful of rulings suggest that such an approach may be gaining traction. For example, preliminary objections raised by franchisors in respect of human rights violations affecting franchise network employees have been rejected on more than one occasion, based on findings that the franchisor's involvement in or control over the daily operations of a franchisee and its employment practices would need to be decided through an appreciation of the evidence brought forth at the hearing stage. However, these preliminary findings are not dispositive of the franchisors' actual liability and decisions on the merits have yet to be rendered.

In order to mitigate the risk of a franchisor being considered a common employer, each franchisee must operate as a truly independent and distinct entity from its franchisor. Additionally, even if the franchisee is separately incorporated and operates independently, it is imperative to ensure that there exists no common control or direction emanating from the franchisor greater than that which is necessary to maintain the integrity of the brand. To do otherwise would be to run the risk of being qualified as a common employer, depending upon the number and extent of instances likely to be viewed as an exercise of common control or direction.

Instead of exercising authority over the franchisee's employees, franchisors may seek to communicate to franchisees the ultimate objectives and goals to strive for in relation to labour and employment, while adopting an interested but non-interfering approach in connection with their franchisees' actual operations. One way of achieving this result may be for franchisors to influence franchisees' conduct by rewarding compliance with stated best practice in labour and employment that is not identified as compulsory in the context of the franchise relationship.

### 10.2 Is there a risk that a franchisor may be held to be vicariously liable for the acts or omissions of a franchisee's employees in the performance of the franchisee's franchised business? If so, can anything be done to mitigate this risk?

In addition to the issues discussed in question 10.1 above, a franchisor may be held vicariously liable for various claims and damages associated with the franchised business, including for personal injury, data security and privacy breaches, human rights violations and other matters arising as a result of the use of the franchisor's brand and marks in the operation of the franchised business in a manner likely to mislead third parties into believing that they are interacting with the actual franchisor. In order to mitigate the risks of being held liable vicariously, franchisors must ensure that they are not exercising direction or control over their franchisees on a day-to-day basis. Franchisors must also ensure that any third parties, including the franchisee's employees, suppliers and customers, are clearly advised that the franchisee is an independent entity from the franchisor.


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## 11 Currency Controls and Taxation

**11.1 Are there any restrictions (for example exchange control restrictions) on the payment of royalties to an overseas franchisor?**

No, there are no restrictions.

**11.2 Are there any mandatory withholding tax requirements applicable to the payment of royalties under a trade mark licence or in respect of the transfer of technology? Can any withholding tax be avoided by structuring payments due from the franchisee to the franchisor as a management services fee rather than a royalty for the use of a trade mark or technology?**

Fees and royalties paid to a franchisor that is not a resident of Canada are generally subject to a withholding tax of 25%; however, the rate is often reduced by up to 10% by tax treaties entered into between Canada and other jurisdictions. The characterisation of any given fee as a service fee would not necessarily be sufficient to escape the application of withholding requirements altogether, particularly if the fee is paid in consideration of the use of the trademark or technology and would otherwise be characterised as a royalty. While it is possible to avoid taxes by qualifying certain fees as a 'service fee', it is imperative that such a fee be related to a legitimate third-party service, for an 'arm's length' fee, which the franchisor provides to its franchisees, and not otherwise constitute a disguised royalty.

**11.3 Are there any requirements for financial transactions, including the payment of franchise fees or royalties, to be conducted in local currency?**

A franchisee may be required to make payments in a foreign franchisor's domestic currency. Nevertheless, the Currency Act (Canada) precludes a Canadian court from rendering a judgment in any currency other than Canadian currency.

## 12 Commercial Agency

**12.1 Is there a risk that a franchisee might be treated as the franchisor's commercial agent? If so, is there anything that can be done to help mitigate this risk?**

Canada does not have commercial agency laws as that term is understood elsewhere in the world. However, a franchisee may be treated as the franchisor's agent if a reasonable third party would view the franchisee as acting on behalf of the franchisor and the franchisor held out that the franchisee was authorised to do so. To mitigate this risk, the franchise agreement should expressly provide that the franchisee is not the agent of the franchisor. Furthermore, the franchisor should ensure that the franchisee advises and presents itself to the public as an independent entity from the franchisor.

## 13 Good Faith and Fair Dealings

**13.1 Is there any overriding requirement for a franchisor to deal with a franchisee in good faith and to act fairly in its dealings with franchisees according to some objective test of fairness and reasonableness?**

The Canadian Franchise Acts impose a general obligation of good faith and fair dealing upon the parties to a franchise relationship. It is established law in Canada that the relationship between a franchisor and a franchisee is generally not a fiduciary one.

Outside the foregoing legislative context, the Supreme Court of Canada has found that there is an inherent duty for parties to honestly perform their contractual obligations. Canadian courts (even in provinces without franchise legislation) have also generally begun to read into franchise agreements an implied duty of simple good faith (as opposed to 'utmost good faith'). A more fulsome good faith obligation exists under the Civil Code of Quebec, which imposes a legal requirement for all parties in matters governed by Quebec civil law to conduct themselves in good faith at the time their obligations arise and at the time these are performed and extinguished. Accordingly, the courts have stated that where the franchisor retains sole discretion to authorise, prevent or proceed with a particular course of action, the franchisor will have to exercise its discretion reasonably. In addition, the duty to act in good faith requires a prompt response to another party's request and the making of a decision within a reasonable period of time thereafter. Moreover, parties under a duty of good faith must also pay any amounts that are clearly owed to another party in a timely manner.

## 14 Ongoing Relationship Issues

**14.1 Are there any specific laws regulating the relationship between franchisor and franchisee once the franchise agreement has been entered into?**

The legal principles applicable to the execution of contractual obligations generally apply throughout the franchise relationship. In Quebec, franchise agreements are generally regarded as contracts of adhesion. The Civil Code of Quebec, in an effort to correct a presumed economic imbalance between the parties to an adhesion contract, provides more favourable interpretation principles and a significantly broader margin of redress for the adhering party than that which would be available with other contracts. For example, an abusive clause in a contract of adhesion will be considered null, or the obligation arising from it may be reduced by a court.

## 15 Franchise Renewal

**15.1 What disclosure obligations apply in relation to a renewal of an existing franchise at the end of the franchise agreement term?**

Pursuant to the Canadian Franchise Acts, in the context of a renewal of an existing franchise, the franchisor is, in principle, under no obligation to provide a revised disclosure document if such renewal comes into effect pursuant to the same terms as the initial agreement and no new material facts have arisen since the initial disclosure document was provided. However, if there has been a material change or if the franchisee is required to sign a new franchise agreement, new disclosure would be required.




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### 15.2 Is there any overriding right for a franchisee to be automatically entitled to a renewal or extension of the franchise agreement at the end of the initial term irrespective of the wishes of the franchisor not to renew or extend?

There is not generally any obligation for a franchisor to renew a franchise agreement unless the contractual conditions for renewal have been satisfied. However, the statutory and common law duty of good faith requires that, if the franchisee has been granted a right of renewal, a franchisor must have a just or reasonable cause not to renew the agreement in violation of the contractual undertaking.

### 15.3 Is a franchisee that is refused a renewal or extension of its franchise agreement entitled to any compensation or damages as a result of the non-renewal or refusal to extend?

If a renewal or extension is refused, a franchisee will only be entitled to compensation if the failure to renew or extend constituted a contractual breach. If the franchisee fulfils all of the conditions provided in the contract in order to be entitled to renewal and the franchisor refuses to grant such renewal, the franchisee may have a right to damages and/or an injunction to force the franchisor to comply with the contract's renewal terms.

## 16 Franchise Migration

### 16.1 Is a franchisor entitled to impose restrictions on a franchisee's freedom to sell, transfer, assign or otherwise dispose of the franchised business?

A franchisor may contractually restrict a franchisee's ability to transfer its rights and interests under the franchise agreement by subjecting such transfers to the prior consent of the franchisor. It is not uncommon for the franchisor's consent to be conditional on its satisfaction with the proposed transferee's aptitudes and creditworthiness, among other criteria.

### 16.2 If a franchisee is in breach and the franchise agreement is terminated by the franchisor, will a "step-in" right in the franchise agreement (whereby the franchisor may take over the ownership and management of the franchised business) be recognised by local law, and are there any registration requirements or other formalities that must be complied with to ensure that such a right will be enforceable?

No restrictions exist on the takeover of an existing franchisee's business, including its customer base and goodwill. However, in practice, it will be necessary to obtain a court order or judgment sanctioning the franchisor's contractual takeover right prior to physically taking possession in circumstances where the franchisee does not voluntarily vacate the franchised business or otherwise contests the termination.

### 16.3 If the franchise agreement contains a power of attorney in favour of the franchisor under which it may complete all necessary formalities required to complete a franchise migration under pre-emption or "step-in" rights, will such a power of attorney be recognised by the courts in the country and be treated as valid? Are there any registration or other formalities that must be complied with to ensure that such a power of attorney will be valid and effective?

A power of attorney which grants the franchisor the right to complete all necessary formalities to complete a franchise migration will be recognised in Canada. The formalities of a valid power of attorney will be regulated by each province, although most require it to be in writing. There is no requirement that a power of attorney must be registered.



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Marissa specialises in negotiating and drafting complex legal agreements relating to licensing, franchising and distribution agreements as well as technology-related agreements. Her skilled expertise allows her to regularly advise corporations of all sizes in matters such as franchising, licensing, e-commerce, intellectual property, privacy, social media, contests, product labelling, marketing and advertising, consumer protection, French language, export controls, and other regulatory areas in order to comply with Canadian legal requirements, including those specific to the province of Quebec. She also advises foreign companies with respect to their entry into the Canadian market and continued compliance with Canadian and Quebec law.

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Lapointe Rosenstein Marchand Melançon LLP is one of the largest independent law firms in Quebec, offering superior legal services in various fields of law including franchising and all related areas of practice, such as real estate, leasing, intellectual property and licensing. The firm also has strong commercial, litigation, tax, labour and insurance departments.

The attorneys who are part of the Franchising Sector Team are experts in Canadian and international franchising issues. They are also able to counsel clients regarding Quebec's French language laws and the province's uniqueness as a civil law jurisdiction – an invaluable perspective when evaluating the impact of Canada's unique laws on international clients. As a result, they are able to better serve their clients in the face of increasing globalisation and market expansion.

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