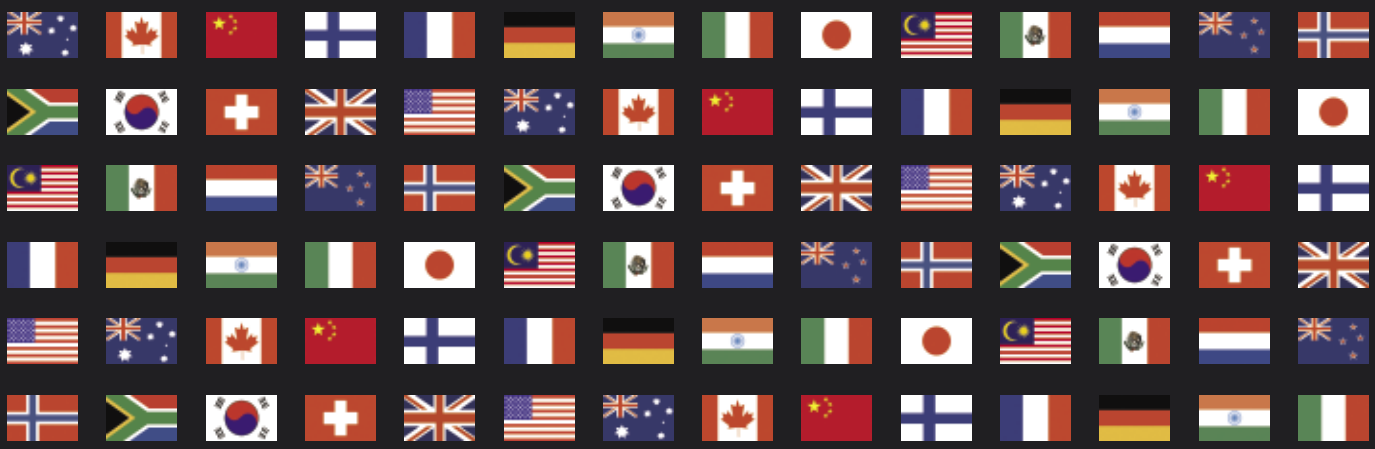
Franchise
2022

Contributing editor
Mark Kirsch



LEXOLOGY
Getting The Deal Through

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Published by
Law Business Research Ltd
Meridian House, 34-35 Farringdon Street
London, EC4A 4HL, UK

First published 2007
Sixteenth edition
ISBN 978-1-83862-663-1

Printed and distributed by
Encompass Print Solutions
Tel: 0844 2480 112

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Lexology Getting The Deal Through is delighted to publish the sixteenth edition of *Franchise*, which is available in print and online at www.lexology.com/gtdt.

Lexology Getting The Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique Lexology Getting The Deal Through format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on Australia, India and United States.

Lexology Getting The Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.lexology.com/gtdt.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Lexology Getting The Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editor, Mark Kirsch of Lathrop GPM, for his assistance with this volume.

LEXOLOGY
Getting The Deal Through

London
July 2021

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Canada

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MARKET OVERVIEW

Franchising in the market

1 How widespread is franchising in your jurisdiction? In which sectors is franchising common? Are there any economic or regulatory issues in the market that are more or less hospitable to franchising or make it economically viable in your jurisdiction?

Franchising is widespread across Canada in over 50 industries including automotive, travel, senior care, education, and health and fitness, with the retail and restaurant sectors being the most popular. In fact, Canada has the second-largest franchise industry in the world following the United States and franchising is often used by US companies to enter the Canadian market.

As opposed to other jurisdictions, there is no registration required to establish a franchise system in Canada or to obtain a license to enter into contracts and grant franchise rights. There is also no requirement that disclosure documents or other materials be registered, thereby facilitating entry into franchising. Moreover, the Canadian provinces that have adopted franchise disclosure laws have rules in place governing pre-contractual disclosure only. The pre-contractual disclosure process itself is self-governed; franchisors are solely responsible for the contents of the disclosure materials and their compliance, and there is no advance submission of the disclosure items to any regulatory authorities for verification or approval.

Associations

2 Are there any national or local franchise associations? What is their role in franchising, including any impact on laws or regulations? Are there any rules of conduct or membership requirements?

Canadian franchisors and franchisees have created the robust and effective Canadian Franchise Association (CFA) to build and support the franchise industry in Canada. The CFA currently has thousands of members nationwide. Although there is no requirement to become a member of the CFA, membership typically lends credibility to a franchise, given that franchisors are required to meet its definition of a franchise to qualify as members. Prospective members must also provide proper documentation in support of their membership application and commit to abide by the CFA Code of Ethics. Membership of the CFA also 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, including:

- information about the franchisor's business and franchise experience;
- the details of existing franchisees;
- the investment required by the franchisee (broken down into various categories);
- any rebates or other benefits received by the franchisor; and
- a summary of the salient provisions of the franchise agreement.

BUSINESS OVERVIEW

Types of vehicle

3 What forms of business entities are relevant to the typical franchisor?

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 and 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 creating a permanent establishment in Canada, thus avoiding being considered by Canadian tax authorities as carrying on business in Canada.

Regulation of business formation

4 What laws and agencies govern the formation of business entities?

The federal legislation under which a corporation may be incorporated is the Canada Business Corporations Act (CBCA). Provinces have also enacted similar statutes regulating the formation of corporate entities. The formation of partnerships and other non-corporate entities is governed solely by legislation that is specific to each province. Business entities must usually register with the relevant corporate or business registry of each province in which they wish to conduct business.

Requirements for forming a business

5 Provide an overview of the requirements for forming and maintaining a business entity.

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.

Restrictions on foreign investors

6 What restrictions apply to foreign business entities and foreign investment?

Pursuant to the Investment Canada Act, foreign business entities seeking to acquire or establish a Canadian business are required to notify Innovation, Science and Economic Development Canada no later than 30 days following such acquisition or establishment. 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 applies to indirect acquisitions where the asset value of the acquired Canadian business represents greater than 50 per cent of the asset value of the global transaction. The review threshold for World Trade Organization investors was decreased to an 'enterprise value' of C$1.043 billion as of 13 February 2021. This amount is indexed annually. Most franchisors do not meet this threshold.

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

Taxation

7 What aspects of the tax system are relevant to franchisors? How are foreign businesses and individuals taxed?

Generally, three business structures are available to a franchisor wishing to export its franchise system into Canada:

- A foreign franchisor may choose to contract directly with its Canadian franchisees without carrying on business in Canada directly or through a permanent establishment in Canada. In such an event, income earned in Canada by the franchisor through royalty payments and rent would be characterised as passive income and subject in Canada to a withholding tax only. The standard withholding tax rate of 25 per cent under Canadian income tax legislation is often reduced to 10 per cent by tax treaties entered into between Canada and other jurisdictions – these should be carefully reviewed and considered at the structural stage of planning any entry into the Canadian market.
- A franchisor may opt to carry on business in Canada using a Canadian branch or division. If the franchisor carries on business in Canada through a fixed place of business or permanent establishment, any income derived in respect thereof will generally qualify as 'business income' that is taxable in Canada on a net income basis. Furthermore, the income of a non-resident franchisor carrying on business through a Canadian branch will typically be subject to a 'branch tax' that is payable at the time the earnings of the subsidiary are accrued (and not at the time the income is paid to the foreign franchisor). In light of the foregoing, few franchisors choose to establish a branch office or division for the purpose of expanding into the Canadian market.
- A franchisor may choose to carry on business in Canada through a federally or provincially incorporated subsidiary. This is the most frequently used vehicle by non-resident franchisors wishing to export a franchise system into Canada. The incorporation of a subsidiary presents certain advantages, including the avoidance of Canadian withholding tax on passive income. Nonetheless, the subsidiary's income would be taxable in Canada on a net income basis and dividends paid to its parent would be subject to a withholding tax of 25 per cent. This rate is often reduced to between 5 and 15 per cent by tax treaties entered into between Canada and other jurisdictions. The franchisor may also charge a reasonable fee for providing assistance to its Canadian subsidiary in the operation of its business activities with the expectation that a reasonable portion of such fee may then be deducted from the subsidiary's income for tax purposes. Normally, a fee negotiated between arm's-length parties would meet the reasonability test.

In conclusion, significant business and tax consequences arise from each of the above-mentioned structures – a thorough review of all relevant Canadian legislation pertaining to each structure and a careful evaluation of the effect of tax treaties ratified by Canada is strongly advised.

Labour and employment

8 Are there any relevant labour and employment considerations for typical franchisors?

Each Canadian province has enacted its own health and safety, employment standards, and labour relations legislation. Accordingly, provincial laws and regulations govern most matters relating to labour law (for example, minimum wages, hours of work, overtime, leave, termination of employment, union certification and collective bargaining rights).

Each franchisee must operate as a truly independent and distinct entity from its franchisor so as to be considered a separate employer for labour union certification and collective bargaining purposes. 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 that is greater than that which typically characterises the franchisor – franchisee relationship. To do otherwise would run the risk of having a union certification or collective agreement with respect to one franchisee being extended to other franchised or corporate outlets. Furthermore, most provincial jurisdictions recognise successor liability following a transfer or sale of a business, such that the new employer is bound by the union certification and, in certain circumstances, by the collective bargaining agreement concluded with the union representing the employees of the sold business.

While no provinces have enacted legislation recognising a joint employer status for franchisors per se, it is important to note that the Ontario Fair Workplaces, Better Jobs Act, 2017 does not require that businesses carrying on associated or related activities have the intent or effect of defeating employment standards legislation in order to be treated as one employer and held jointly and severally liable, thus creating a wider scope of application and increasing the possibility of associated businesses being deemed joint employers. The act also allowed newly certified bargaining units to consolidate with other existing bargaining units of the same employer, thereby permitting an existing collective agreement to apply to employees of more than one franchise belonging to the same franchisee. This amendment was however repealed by the Making Ontario Open for Business Act, 2018, which came into force on 1 January 2019.

Intellectual property

9 How are trademarks and other intellectual property and know-how protected?

The Trademarks Act (Canada) defines a trademark as a 'sign or combination of signs that is used or proposed to be used by a person for the purpose of distinguishing or so as to distinguish their goods or services from those of others or a certification mark'. 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 Intellectual Property Office has the advantage of providing

nationwide protection of the registered trademark and, in the province of Quebec, enables the use of any English-only terminology that is a registered trademark on catalogues, brochures, public signs and certain other commercial advertising (provided that no French version of the trademark has been registered and, in the case of public signage, that a generic description of the goods and services is included in French) in circumstances where the same would, as a practical matter, be prohibited absent registration. An application for registration may be filed without having to specify a basis for filing or including a declaration as to the use of the concerned trademark. Recent amendments to the Trademarks Act (Canada) have also allowed for the filing of certain non-traditional types of trademarks (such as sound, scent or taste).

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 superior court with territorial jurisdiction.

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.

Canada has recently become a member country of the Madrid Protocol and therefore foreign franchisors seeking Canadian trademark registrations may apply for them by way of the Madrid International Trademark System.

Real estate

10 | What are the relevant aspects of the real estate market and real estate law? What is the practice of real estate ownership versus leasing?

With the exception of the province of Quebec, all provincial property laws are based on the English common law system, pursuant to which real estate can either be held in fee simple or by way of a leasehold interest. Such interest is registered with the public land registry. Quebec's property laws are based on the French civil law system. They require the registration of ownership rights and permit the registration of lease rights in the public land registry.

No particular restrictions exist as to the nature of the arrangement to be concluded between the franchisor and the franchisee with regard to real (or, in civil law, immovable) property. For instance, a franchisor may wish to enter into a head lease and sublease the premises to a franchisee. In such circumstances, cross-default provisions between the sublease and the franchise agreement are advisable so that a right to terminate for breach of one gives rise to a right to terminate the other. In the absence of such provisions, the franchise agreement and the sublease will be construed as two independent contracts and breach of one may not have any bearing on the other. Moreover, it is advisable to include automatic termination provisions in a sublease and a franchisor's right to terminate in a franchise agreement in circumstances where the head lease is terminated.

In Canada, it is more common for franchisors to lease (or require that their franchisees lease) than purchase real estate for franchise locations, given the significant capital investment that is required and that property located in prime locations is often not available for purchase.

Generally, foreign ownership of, or the transfer to non-residents of, real estate situated in Canada is not restricted, save for those instances where such real estate benefits from statutory protection given its cultural or historical significance.

Competition law

11 | What aspects of competition law are relevant to the typical franchisor in your jurisdiction? How is competition law enforced in the franchising sector?

The Competition Act sets forth penal and civil recourse with respect to various practices, including those identified as conspiracies and collusion, abuse of dominance, price maintenance, promotional allowances and price discrimination, false or misleading advertising, deceptive marketing and pyramid selling, refusal to deal, exclusive dealing, and 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 offence. 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, private litigants may only seek redress of conduct that constitutes a breach of an order under the Competition Act, as monetary awards are not provided for. The Competition Tribunal may order a reviewable trade practice to cease, or compel a business to accept a given customer or order on reasonable trade terms.

The Commissioner of Competition heads the Competition Bureau and has broad powers of investigation and inquiry, such as search and seizure and examinations under oath. The Competition Bureau also has the power to order the production of physical evidence or records and wiretapping (in certain circumstances). Its enquiries are conducted under strict rules of confidentiality and its powers remain subject to the supervision of the courts. On an international level, the Competition Bureau has concluded numerous agreements of notification and mutual assistance with its international counterparts, and is an active member of the International Competition Network.

OFFER AND SALE OF FRANCHISES

Legal definition

12 | What is the legal definition of a franchise?

The offer and sale of franchises in Canada is regulated by the provinces rather than by the federal government. Definitive franchise legislation is currently in force in six Canadian provinces: Alberta, Ontario, New Brunswick (NB), Prince Edward Island (PEI), Manitoba and British Columbia (BC). The Civil Code of Quebec also contains provisions applicable to all contracts governed by Quebec law, including franchise agreements.

The Arthur Wishart Act (Franchise Disclosure) 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) each generally define 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.

Under the Ontario Act, the definition of 'franchise' provides that the right to exercise control over the franchisee's method of operation, as opposed to the actual exercise of that control, may be sufficient for the purposes of characterising a business as a franchise, which by definition potentially increases the number of business relationships that may fall under the Ontario Act's application.

The Ontario Act, the PEI Act, the NB Act and the BC Act apply to franchise agreements entered into on or after 1 July 2000, 1 July 2006, 1 February 2011 and 1 February 2017 respectively, and to renewals or extensions of franchise agreements regardless of whether such franchise agreements were entered into before or after such date, provided that the business operated pursuant to such franchise agreements is to be operated partly or entirely in Ontario, PEI, NB or BC respectively. The Manitoba Act is conceptually similar and applies to franchise agreements entered into, renewed or extended on or after 1 October 2012. Furthermore, there is no residency requirement in respect of the franchisee with respect to whom the Ontario Act, the PEI Act, the NB Act, the Manitoba Act or the BC Act applies.

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.

The Alberta Act applies to the sale of a franchise made on or after 1 November 1995 if the franchised business is to be operated partly or entirely in Alberta and if the purchaser of the franchise is an Alberta resident or has a permanent establishment in Alberta for the purposes of the Alberta Corporate Tax Act.

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 differently in other jurisdictions.

Laws and agencies

13 What laws and government agencies regulate the offer and sale of franchises?

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 (collectively, the Canadian Franchise Acts). No other province or territory of Canada has regulated the offer and sale of franchises through franchise-specific legislation.

Exemptions exist in each of the Canadian Franchise Acts, other than the Alberta Act, as follows.

Full exemptions

The Canadian Franchise Acts, with the exception of the Alberta Act, do not apply to the following commercial relationships:

- employer – employee relationships;
- partnerships;
- memberships in a cooperative association, as prescribed in the NB Act, the PEI Act, the BC Act or the regulations of the Ontario Act, as the case may be;
- arrangements for the use of a trademark, trade name or advertising to distinguish a paid-for evaluation, testing, or certification service for goods, commodities or services;
- arrangements with a single licensee in respect of a specific trademark, trade name or advertising if it is the only one of its general nature and type to be granted in Canada;
- any lease, licence or similar agreement for space in the premises of another retailer where the lessee is not required or advised to buy the goods or services it sells from the retailer or any of its affiliates (Ontario Act only);
- oral relationships or arrangements without any writing evidencing any material term or aspect of the relationship or arrangement;
- a service contract or franchise-like arrangement with the Crown or an agent of the Crown (except the Manitoba Act or the BC Act); and
- an arrangement arising from an agreement for the purchase and sale of a reasonable amount of goods at a reasonable wholesale price or for the purchase of a reasonable amount of services at a reasonable price (except the Ontario Act).

Partial exemptions – the obligation to disclose

All of the Canadian Franchise Acts, other than the Alberta Act, contain exemptions from disclosure requirements that include, for example, the sale of a franchise to a person to sell goods or services within a business in which that person has an interest, provided that the sales arising from those goods or services do not exceed 20 per cent of the total sales of the business during the first year of operation of the franchise.

Exemptions are also set out in the Canadian Franchise Acts, other than the Ontario Act and the BC Act, in connection with a franchise being granted if the prospective franchisee is required to make a total annual investment to acquire and operate the franchise in an amount that does not exceed the amount prescribed under each of the Canadian Franchise Acts, currently C$5,000. Under the Ontario Act, a similar exemption exists in connection with a franchise being granted if the prospective franchisee is required to make a total initial investment (not a total annual investment), determined in the prescribed manner, of an amount that does not exceed a prescribed amount, currently C$15,000.

Exemptions exist in the Ontario Act, the Alberta Act and the BC Act regarding the obligation to provide a disclosure document as follows. Exemptions apply in the case of:

- the sale of a franchise by a franchisee provided that:
- the franchisee is not the franchisor or an associate, director, officer or employee of the franchisor;
- the sale is for the franchisee's own account;
- the sale is not effected by or through the franchisor; and
- in the case of a master franchise, the entire franchise is sold;
- the sale of a franchise to a person who has been an officer or director of the franchisor or the franchisor's associate for at least six months for that person's own account (Alberta Act and BC Act only).
- the sale of a franchise to a person for the person's own account or to a corporation that the person controls if the person:
- has been an officer or director of the franchisor or of the franchisor's associate for at least six months and is currently such an officer or director; or
- was an officer or director of the franchisor or of the franchisor's associate for at least six months and no more than four months have passed since the person was such an officer or director (Ontario Act only);
- the sale of an additional franchise to an existing franchisee if the additional franchise is substantially similar to the franchise that the franchisee is operating;
- a renewal or extension of an existing franchise agreement;

- the grant of a franchise for one year or less that does not involve payment of a non-refundable franchise fee (Ontario Act and BC Act only);
- the sale of a franchise by an executor, administrator, sheriff, receiver, trustee, trustee in bankruptcy or guardian on behalf of a person other than the franchisor or the estate of the franchisor;
- the grant of a franchise if the franchisor is considered to be operating or participating in a multilevel marketing plan as defined by the Competition Act (Ontario Act and BC Act only);
- the sale of a right to a person to sell goods or services within or adjacent to a retail establishment as a department or division of the establishment, if the person is not required to purchase goods or services from the operator or the retail establishment (Alberta Act only); and
- the sale of a fractional franchise (Alberta Act only).

The exemptions set out in each of the Canadian Franchise Acts, while substantively similar, are not identical. Under the BC Act, the sale of a franchise to a franchisee who invests more than a prescribed amount (currently C$5 million) into the acquisition and operation of the franchise is exempted from the application of the disclosure requirements. Under the Ontario Act, the sale of a franchise if the prospective franchisee is required to make a total initial investment, determined in the prescribed manner, of an amount that is greater than a prescribed amount (currently C$3 million) is exempted from the application of the disclosure requirements.

One does not have to comply with the disclosure requirements under the Alberta Act when granting a licence to a person to sell goods or services within or adjacent to a retail establishment as a department or division of said establishment without requiring that the person purchase goods or services from the operator of the retail establishment.

Under the Manitoba Act and the BC Act, a franchisor is not required to provide financial statements to a franchisee if the franchisor meets certain criteria, including:

- a net worth of at least C$5 million or, alternatively, having a net worth of at least C$1 million if the franchisor is controlled by a corporation that has a net worth of at least C$5 million; and
- the existence of at least 25 of its franchisees engaged in business in Canada at all times during the five-year period preceding the date of the disclosure document.

In addition, each of the Canadian Franchise Acts other than the Alberta Act and the BC Act affirms that a franchisor may apply for a ministerial exemption allowing it to exclude its financial statements from a disclosure document.

Principal requirements

14 What are the principal requirements governing the offer and sale of franchises under the relevant laws?

There are no specific requirements governing the offer and sale of franchises under the Canadian Franchise Acts, other than the requirements of pre-contractual disclosure. Article 1375 of the Civil Code of Quebec establishes a duty of the parties to conduct themselves in good faith that extends to pre-contractual negotiations. This obligation has generally been interpreted to require that franchisors inform franchisees during the offer and sale stage of franchises of any information that could affect their decision to enter into the franchise agreement and, correspondingly, that franchisees conduct reasonable due diligence and investigation prior to entering into the franchise agreement.

Franchisor eligibility

15 Must franchisors satisfy any eligibility requirements in order to offer franchises? Are there any related practical issues or guidelines that franchisors should consider before offering franchises?

Except for compliance with applicable Canadian Franchise Acts and other legislation, there is no requirement – for example, that a franchisor be in business for a minimum period, that a franchisor has operated a minimum number of franchisor-owned operations, or that a franchisor has operated in Canada with franchisor-owned operations for a minimum period – that must be met before a franchisor may offer franchises.

Franchisee and supplier selection

16 Are there any legal restrictions or requirements relating to the manner in which a franchisor recruits franchisees or selects its or its franchisees' suppliers? What practical considerations are relevant when selecting franchisees and suppliers?

There are no generally applicable restrictions governing the recruitment and selection of franchisees or franchisee's suppliers, the locations of franchised outlets or the distance between outlets. However, it is important to note that such restrictions do exist in certain industries whose products or services are specifically regulated, such as the tobacco industry, the alcohol industry and the cannabis industry. For practical purposes, it is generally advised to consider a prospective franchisee's aptitudes, character traits, financial wherewithal and experience as an independent business person when evaluating whether to enter into a long-term business relationship. Similarly, it is advisable to consider a prospective supplier's experience in the relevant industry, and its knowledge of the market and the territory before entering into a business relationship with that supplier.

Pre-contractual disclosure – procedures and formalities

17 What procedures and formalities for pre-contractual disclosure are required or advised in your jurisdiction? How often must the disclosures be updated?

A franchisor governed by any of the Canadian Franchise Acts must furnish a prospective franchisee with a disclosure document not less 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.

All of the Canadian Franchise Acts exclude confidentiality and site selection agreements from the definition of franchise agreements for the application of the disclosure requirements. In addition, the Alberta Act, the Ontario Act and the BC Act also exempt agreements that only contain terms and conditions relating to a fully refundable deposit (that is, a deposit that does not exceed 20 per cent 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).

A franchisor must also furnish a prospective franchisee under each of the Canadian Franchise Acts with a description of any 'material change' 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.

Pre-sale disclosure to sub-franchisees

18 In the case of a sub-franchising structure, who must make pre-sale disclosures to sub-franchisees? If the sub-franchisor must provide disclosure, what must be disclosed concerning the franchisor and the contractual or other relationship between the franchisor and the sub-franchisor?

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, and exemptions pertaining thereto, that apply to franchisors with regard to their relationships with their franchisees. 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.

Due diligence

19 What due diligence should both the franchisor and the franchisee undertake before entering a franchise relationship?

While the scope of proper due diligence efforts is too broad to be addressed in a short response, we would include at the core of such efforts:

- from a franchisee's perspective, conducting proper due diligence on the business opportunity being offered including evaluating its financial return, meeting with already established franchisees in the franchise system and building a business plan; and
- from a franchisor's perspective, it will be important to evaluate the financial wherewithal of the prospective franchisee, and whether its representatives have sufficient experience in the industry to successfully operate a franchise location and a fulsome grasp of the vision and philosophy of the franchised concept so as to be an effective operator and representative of the brand.

In addition, with respect to franchisees establishing the first Canadian franchise location of an existing foreign franchise system in Canada, it will be important for franchisees to evaluate whether the franchisor has adapted its franchise system to the Canadian market to comply with certain local requirements, for example, whether the franchisor has translated its materials and website to French for franchisees located in the province of Quebec.

Pre-contractual disclosure – content

20 What information is the disclosure document required or advised to contain?

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 have 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, which are not required under the Alberta Regulations. The regulations adopted under the BC Act also differ from those adopted under the other Canadian Franchise Acts as they require franchisors that have been operating for less than one fiscal year to disclose an opening balance sheet, prepared in the same manner as financial statements.

The disclosure document must also include all material facts, the definition of which 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 to the value of the franchise. Unlike all of the other Canadian Franchise Acts, the BC Act does not require franchisors to disclose how they select franchise locations unless this information is considered a material fact that would otherwise be subject to disclosure. The BC Act also provides that franchisors must provide potential franchisees with a list of all current franchises in Canada and not only those located in British Columbia.

Failure to disclose – enforcement and remedies

21 What actions may franchisees or any relevant government agencies take in response to a franchisor's failure to make required disclosures? What legal remedies are available? What penalties may apply?

The Canadian Franchise Acts do not generally provide for specific enforcement action by regulatory authorities or any administrative penalties where disclosure requirements are not respected. Rather, they allow franchisees to seek compensatory damages and other specific remedies in circumstances where disclosure rules have not been respected by a franchisor.

Under each of the Canadian Franchise Acts, an action for damages or rescission may be instituted by the franchisee for non-compliance. The NB Act provides that a party to a franchise agreement may, in the event of a dispute with another party to the agreement, trigger a mandatory alternative dispute resolution mechanism (eg, mediation). This does not, however, preclude any party to such franchise agreement from availing itself of other forms of recourse 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:

- '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
- '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 applicable) 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 of receiving a cancellation notice, compensate the franchisee for any net losses incurred by the franchisee 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 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 the above 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.

Failure to disclose – apportionment of liability

22 In the case of sub-franchising, how is liability for disclosure violations shared between franchisor and sub-franchisor? Are individual officers, directors and employees of the franchisor or the sub-franchisor exposed to liability? If so, what liability?

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 applicable franchise legislation. Where a franchisor and a sub-franchisor are found liable for misrepresentations contained in a disclosure document, their liability is of a joint and several nature.

Generally, the officers, directors and employees of a company cannot be sued in their personal capacity for the debts and obligations of the company. Accordingly, a key advantage presented by the subsidiary structure is the creation of a generally effective shield for the foreign franchisor seeking to avoid exposure to liabilities arising in Canada. Nevertheless, liability is not entirely absorbed by the corporate subsidiary in cases where a separate entity furnished a guarantee under the franchise agreement, or breached its legal or statutory obligations in regards to the franchise agreement.

The Canadian Franchise Acts extend liability for misrepresentations contained in a disclosure document to a much broader class of persons than those who would otherwise be liable under Canadian common law. Under the Alberta Act, a franchisee has a right of action not only against the franchisor, but also against every person who signed the misrepresentative disclosure document. Similarly, each of the other Canadian Franchise Acts provide that a franchisee may not only claim damages for misrepresentation from the franchisor, but also from the broker and associate of the franchisor as well as every person who signed the relevant disclosure document or statement of material change. In light of the very broad statutory construction given to the term 'franchisor's associate', the principal owner or controlling shareholders of a franchisor who are personally involved in the granting or marketing of the franchise may qualify as franchisor's associates. Similarly, parent companies of Canadian subsidiaries incorporated to conduct franchise operations in Canada may also qualify as franchisor's associates when such parent companies participate in the review or approval of the granting of a franchise.

General legal principles and codes of conduct

23 In addition to any laws or government agencies that specifically regulate offering and selling franchises, what general principles of law affect the offer and sale of franchises? What industry codes of conduct may affect the offer and sale of franchises?

General principles of law that may affect the offer and sale of franchises vary depending on the province in which a franchisor wishes to grant franchises.

In all provinces of Canada other than Quebec, general common law principles regarding contract formation govern the offer and sale of franchises. In Quebec, franchise agreements are governed by the general principles of contract formation found in the Civil Code of Quebec and are generally regarded as contracts of adhesion. The Civil Code of Quebec, in an effort to correct a presumed economic imbalance between the parties, provides more favourable interpretation principles and a significantly broader margin of redress for the adhering party to a contract of adhesion than that which would be available absent a contract of adhesion. Furthermore, an abusive clause in a contract of adhesion will be considered null, or the obligation arising from it may be reduced by a court.

In addition, courts in Quebec have established that franchisors have an obligation to inform potential franchisees of any information in their possession that may have a decisive influence on the franchisee's will to contract. While franchising practitioners in Quebec have generally viewed this disclosure obligation as essentially similar to the obligation of franchisors under the Canadian Franchise Acts to disclose all material facts to the franchisee, Quebec courts may give it a broader interpretation – courts have found a franchisor liable for failing to disclose to the potential franchisee internal reports and documents commissioned and produced upon the franchisor's request and at its expense, such as feasibility studies in respect of potential locations and aptitude tests with respect to the potential franchisee.

Fraudulent sale

24 What actions may franchisees take if a franchisor engages in fraudulent or deceptive practices in connection with the offer and sale of franchises?

The rights conferred by each of the Canadian Franchise Acts are in addition to, and do not derogate from, any other right, remedy or recourse that a franchisee may have in law.

Judicial decisions emanating from the common law provinces reflect a general and growing affirmation of the common law duty of good faith in franchising, the substantive requirements of which will be conditioned by the specific set of circumstances surrounding the formation of the franchise agreement and the conduct of both parties. Where the courts find that there has been a breach of such duty of good faith, the franchisor may be found liable to the franchisee for its damages. Not every breach of such duty constitutes a fundamental breach of the franchise agreement, which would excuse the franchisee from future performance under the agreement.

In addition, pursuant to article 1401 of the Civil Code of Quebec, an error by a party induced by a fraud committed by the other party, or with its knowledge, nullifies consent whenever, but for the error, the misled

party would not have contracted or would have contracted on different terms. It is important to note that in Quebec silence may amount to a misrepresentation. Such a fraud could be sanctioned with damages and annulment of the contract or, should the franchisee prefer to maintain the contract, a reduction of its obligations set out in the franchise agreement equivalent to the damages to which it would otherwise be entitled.

FRANCHISE CONTRACTS AND THE FRANCHISOR/ FRANCHISEE RELATIONSHIP

Franchise relationship laws

25 What laws regulate the ongoing relationship between franchisor and franchisee after the franchise contract comes into effect?

Other than the Canadian Franchise Acts (namely, the Arthur Wishart Act (Franchise Disclosure) in the province of Ontario, the Prince Edward Island Franchises Act, the New Brunswick Franchises Act, the Manitoba Franchises Act, the British Columbia Franchise Act and Alberta's Franchises Act), there are no specific statutes directly affecting the franchise relationship. Regarding matters not governed by the Canadian Franchise Acts, the ongoing franchise relationship is subject to generally applicable federal and provincial statutes and to the principles of contract law that emanate from the civil law in Quebec or from common law everywhere else in Canada.

Canadian courts have been pragmatic in their approach to ongoing relational matters as they relate to franchising. The clear and express terms of a franchise agreement are determinative of the issues arising in connection with the franchise agreement. If such agreements are ambiguous on a given point, courts will generally construct the litigious terms in a manner that provides for a sensible commercial result. This has not, however, prevented courts from rendering judgments against franchisors that excessively and unlawfully interfere with the economic interests of their franchisees.

Operational compliance

26 What mechanisms are commonly incorporated in agreements to ensure operational consistency and adherence to brand standards?

Franchise agreements often contain several controls and oversight mechanisms in favour of the franchisor in order to verify the accuracy of royalty payments made, supervise the use of its marks and ensure overall compliance of the franchised operations with the franchised concept and the brand. These may include an obligation for the franchisee to submit weekly, monthly or annual reports of its sales, or all three, in addition to point of sale, inventory control and other software that report in real time. The franchisor may also have a right to inspect and audit franchisee's records in the event that a franchisee fails to submit such reports or such reports are suspected or determined to be inaccurate. Other controls include requiring that franchisees submit all proposed store locations, store designers and contractors, product suppliers, and marketing materials to the franchisor for prior approval, as well as a right to inspect the franchise location during operating hours to ensure that the franchisee is properly implementing the franchise system, including rights to assume management of the franchised location in extreme cases.

Amendment of operational terms

27 May the franchisor unilaterally change operational terms and standards during the franchise relationship?

In order to maintain competitiveness in the market, franchisors must continuously change and evolve their franchise systems to adapt to market realities. While franchisors may reserve the right to modify the franchise system throughout the term of the franchise agreement, the implementation of substantial operational standards may be difficult if not all franchisees are in agreement with the change or such change imposes a significant financial burden on franchisees. On the other hand, in the province of Quebec a franchisor may be liable if it fails to implement necessary changes in order to maintain the competitiveness and relevance of the franchise system, resulting in a significant erosion of the franchise network's market share. Franchisors should, therefore, be mindful of its franchisee's interests when implementing any operational changes to avoid potential objections, whether business or legal, from a large group of franchisees in the network.

Policy affecting franchise relations

28 Do other government or trade association policies affect the franchise relationship?

No other government policies or requirements directly affect the franchise relationship.

Termination by franchisor

29 In what circumstances may a franchisor terminate a franchise relationship? What are the specific legal restrictions on a franchisor's ability to terminate a franchise relationship?

There are no restrictions at law on the parties' rights to contractually establish termination rights and consequences arising upon termination. Nevertheless, courts may require that a material breach of the agreement be proven in order to permit its termination and will, from time to time, intervene to redress cases of abuse.

Termination by franchisee

30 In what circumstances may a franchisee terminate a franchise relationship?

There are no rights at law that would specifically allow a franchisee to terminate the franchise relationship other than those applicable to all contracts under general principles of law and those expressly granted by the Canadian Franchise Acts. Similarly, there is no restriction precluding the parties from granting specific termination rights to a franchisee, although this is not often seen in typical franchise agreements used in Canada.

Renewal

31 How are renewals of franchise agreements usually effected? Do formal or substantive requirements apply?

The requirements to renew a franchise agreement are not prescribed by law. As such, the franchisor and franchisee are free to determine the conditions incumbent upon the franchisee's exercise of a right to renew the franchise agreement. These conditions generally include requirements to provide written notice of the franchisee's intention to exercise the renewal right within a specific period of time, to make certain capital expenditures to modernise its franchise location to reflect the then-current image of the brand, to be in compliance with the terms of the franchise agreement and to pay a franchise renewal fee. The right to renew may also be conditioned upon the execution of an updated

version of the franchise agreement. While a franchise agreement may provide for automatic renewal, it is more common for renewal to be subject to substantive requirements.

Refusal to renew

32 | May a franchisor refuse to renew the franchise agreement with a franchisee? If yes, in what circumstances may a franchisor refuse to renew?

In Canada, a franchisor may refuse to renew a franchise agreement with its franchisee unless such renewal is contractually required. The franchisor may contractually subject such renewal to the signature by the franchisee of a new franchise agreement and other conditions, including performance goals that the franchisee is required to achieve.

Transfer restrictions

33 | May a franchisor restrict a franchisee's ability to transfer its franchise or restrict transfers of ownership interests in a franchisee entity?

A franchisor may contractually restrict a franchisee's ability to transfer its rights and interests under the franchise agreement, most notably by subjecting such transfer to the prior consent of the franchisor.

Fees

34 | Are there laws or regulations affecting the nature, amount or payment of fees?

No general restrictions apply to payment of initial fees. Where franchises are involved in the sale of specifically regulated products or services, including liquor, medical or pharmaceutical products and services, however, a franchisor's ability to collect royalties on such sales may be restricted.

Usury

35 | Are there restrictions on the amount of interest that can be charged on overdue payments?

Franchise agreements frequently set out the rates of interest charged on overdue fees and royalty payments. Section 347 of the Criminal Code (Canada) provides that anyone who enters into an agreement to receive interest, or who receives a payment or partial payment of interest, at an effective annual rate of interest (broadly defined) in excess of 60 per cent on the credit advanced, commits an offence thereunder.

In addition, section 4 of the Interest Act (Canada) specifies that unless the contract expresses the applicable rate of interest on an annualised basis, interest will only be recoverable at a rate of 5 per cent per annum despite the terms of the contract.

Foreign exchange controls

36 | Are there laws or regulations restricting a franchisee's ability to make payments to a foreign franchisor in the franchisor's domestic 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.

Confidentiality covenant enforceability

37 | Are confidentiality covenants in franchise agreements enforceable?

Confidentiality covenants in franchise agreements are not only enforceable but highly advisable in light of the fact that recourse is only otherwise available under common law tort, as opposed to under any specific Canadian statute governing trade secrets or other confidential information. Confidentiality clauses can be for a longer duration than non-compete clauses.

Good-faith obligation

38 | Is there a general legal obligation on parties to deal with each other in good faith during the term of the franchise agreement? If so, how does it affect franchise relationships?

The Canadian Franchise Acts impose a general obligation of 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.

The Supreme Court of Canada has found that there is an inherent duty for parties to honestly perform their contractual obligations, which precludes a contracting party from actively deceiving or knowingly misleading its contractual counterparty, including by way of lies, half-truths, omissions and even silence, depending on the circumstances.

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 perhaps more fulsome 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 during contractual and pre-contractual dealings. 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 must exercise its discretion reasonably. In addition, the duty to act in good faith requires a prompt response to another party's request and a decision to be made 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.

The duty to act in good faith does not necessarily preclude a franchisor from competing with its franchisee (assuming, of course, the absence of contractual exclusivity in favour of the franchisee). A franchisor that opts to compete with its franchisee must ensure that it continues to perform its legal obligations towards the latter and that it acts in such a way that the franchisee may continue to enjoy the benefits of its franchise. The common law principle of non-interference with the freedom of the parties to contract often limits judicial interference in franchise agreements when the terms of which are found to accurately reflect the intent of the parties and are not patently inequitable. A determination as to whether a duty of good faith has been breached is contingent upon all of the surrounding circumstances.

Franchisees as consumers

39 | Does any law treat franchisees as consumers for the purposes of consumer protection or other legislation?

Consumer protection legislation in Canada has been enacted at the provincial level. The applicability of such legislation is generally restricted to transactions entered into for personal, family or household purposes and the legislation generally excludes from its ambit transactions entered into for business purposes. In a 2004 case before the Superior Court of Quebec, a franchisee sought to avail itself of protection under the Consumer Protection Act (Quebec) but was unsuccessful,

the Court concluding that the tenor of the correspondence between the franchisee and the franchisor, as well as the nature of the franchise agreement, both clearly implied a commercial relationship falling outside of the scope of the legislation.

Language of the agreement

40 | Must disclosure documents and franchise agreements be in the language of your country?

The Charter of the French Language (Quebec) compels businesses to prepare franchise agreements and disclosure documents 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 such other language.

Restrictions on franchisees

41 | What types of restrictions are commonly placed on the franchisees in franchise contracts?

Franchise agreements often provide for exclusive territories and exclusive dealings with designated suppliers. These are not illegal per se but are subject to competition law concerns relating to the substantial lessening of competition and market barriers, including the exclusive dealings and abuse of dominance provisions of the Competition Act. Restrictions on the customers that the franchisee is entitled to serve may not be acceptable as they may be viewed as violating the market division prohibitions of the Competition Act or providing strong evidence of collusion pursuant to it. These business practices are only subject to review if they have a negative impact on competition in the concerned market, which would typically only arise if a franchisor or its network has a considerable market share.

Price maintenance is 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 they are clearly referred to and defined in the franchise agreement, and are not construed by courts as demonstrating an 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 contractually provide 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 relations between the parties.

Franchisors who are deemed to control a market are also subject to review by the Competition Bureau under the abuse of dominance provisions in the Competition Act. As of 2009, the criminal pricing provisions addressing price discrimination, predatory pricing, geographical price discrimination and promotional allowances have been repealed with a view to promoting innovative pricing programmes and increasing certainty for Canadian businesses. Nonetheless, such pricing policies may be reviewed under civil provisions of the Competition Act where there is evidence of a likely substantial anticompetitive effect.

Non-competition and non-solicitation covenants are closely monitored by the courts. All restrictive covenants raise restraint of trade concerns and, accordingly, only reasonable restrictions as to the scope of action (described with sufficient particulars), duration and geographical reach will be upheld by the courts. Canadian courts generally do not write down or reduce restrictive covenants determined to be unreasonable, but uphold or strike down the covenant in its entirety.

Last, all Canadian provinces permit the selection of a foreign governing law provided that doing so is not considered to be in fraud of the domestic law. That said, Canada is party to numerous international treaties such as the Vienna Convention on the International Sale of Goods – where the selected or applicable law is that of Canada, the Vienna Convention finds automatic application unless expressly set aside by the parties in their contract.

Courts and dispute resolution

42 | Describe the court system. What types of dispute resolution procedures are available relevant to franchising?

The Constitution Act 1867 sets out the areas of law with respect to which the federal government has the power to legislate (for example, intellectual property, bankruptcy, trade and commerce) and the areas of law with respect to which each provincial government has the power to legislate within provincial borders (eg, property and civil rights). Canada also has a dual court system. The Federal Court of Canada has jurisdiction over matters in respect of which jurisdiction as to subject matter is specifically conferred to it by statute, whereas the provincial courts have residual jurisdiction over remaining matters.

Choice of forum clauses are generally enforced by the Canadian courts, thus making it possible for the parties to choose that a non-Canadian court resolve any dispute or claim arising from any agreement. In addition, mediation and arbitration are viable and recognised mechanisms of dispute resolution across Canada. Furthermore, Canada is a signatory party to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Both the federal and the provincial governments have also adopted substantially similar legislation to the UNCITRAL Arbitration Model Law. As at June 2021, four provinces (Ontario, British Columbia, Alberta and Saskatchewan) have incorporated mandatory alternative dispute resolution processes into their respective procedural statutes, and most provinces have enacted arbitration legislation. In addition, the revised Quebec Code of Civil Procedure, which came into force on 1 January 2016, requires parties to consider private dispute prevention and resolution methods before referring their dispute to the courts.

Governing law

43 | Are there any restrictions on designating a foreign governing law in franchise contracts in your jurisdiction? How does the governing law affect the contract's enforceability?

Under the Canadian Franchise Acts, a choice of law provision that attempts to contractually restrict the application of local franchise laws is void. Where the Canadian Franchise Acts do not apply, Canadian courts generally recognise and uphold a 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 of avoiding the consequences of the applicable provincial laws of any Canadian jurisdiction would 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 automatically applies to sales of goods by foreign franchisors who are nationals of any other signatory nation, unless expressly set aside by the parties in the contract. Enforcement of a contract in any Canadian province governed by the law of another Canadian province (or another country) may also prove to be cumbersome from a practical perspective as experts of the governing law in question must be retained in order to provide evidence of the relevant provisions of the relevant foreign law in court.

Arbitration – advantages for franchisors

44 What are the principal advantages and disadvantages of arbitration for foreign franchisors considering doing business in your jurisdiction? Are any other alternative dispute resolution (ADR) procedures particularly favoured or disfavoured in your jurisdiction?

The principal advantages and disadvantages of arbitration for foreign franchisors in Canada are essentially the same as for local franchisors.

Arbitration has the main advantage of being confidential. Disputes between franchisors and franchisees do not become a matter of public record as would be the case with litigation in the judicial system. In addition, arbitration gives the parties a level of control that they may not otherwise have over some aspects of the dispute, such as choice of venue and forum, or the selection of an arbitrator with expertise in franchise issues or the relevant technical or specialised fields. Arbitration agreements are final, reliable and not open to appeal; Canadian courts have generally refrained from intervening in such decisions. Finally, arbitration tends to be faster and cheaper than litigation, at least in theory.

As for its disadvantages, arbitration, like litigation, can become bogged down procedurally, diminishing the cost and time savings that often motivate its use. The lack of ability to appeal heightens risk for the parties that have no recourse against a bad decision. Some also argue that arbitration clauses that preclude access to the judicial system will prevent the use of proceedings such as injunctive or other equitable relief that can be obtained quickly to effectively end a breach of contract.

Another form of alternative dispute resolution favoured in Canada is mediation, which allows the parties to discuss between themselves – usually with the aid of an impartial and respected mediator – in order to resolve the dispute on mutually acceptable terms. Mediation is often provided in agreements as a dispute resolution procedure through which parties must first attempt to resolve their dispute. Failing that, they can resort to arbitration.

National treatment

45 In what respects, if at all, are foreign franchisors treated differently (legally, or as a practical matter) from domestic franchisors?

There is no legal discrimination or heightened level of legal requirements for foreign franchisors. Nevertheless, depending on the vehicle they choose through which to export their franchises to Canada, foreign franchisors may find themselves subject to a different taxation regime from domestic franchisors, and subject to certain notice requirements under the Investment Canada Act. As a practical matter, franchisees may be more hesitant to enter into a franchise agreement, particularly one where the obligations of the franchisor (for example, training or advertising) are numerous, in circumstances where the franchisor has no domestic presence of note.

UPDATE AND TRENDS

Legal and other current developments

46 Are there any proposals for new legislation or regulation, or to revise existing legislation and regulation? Are there other current developments or trends to note?

The province of Ontario recently enacted legislation providing for a series of amendments to the Arthur Wishart Act (Franchise Disclosure) (the Ontario Act) and its general regulation. The amendments include measures to clarify the province's franchise laws and temper or delay franchisors' disclosure obligations towards prospective franchisees in certain circumstances. Key changes to the act and its general regulation are as follows.

- Confidentiality agreements: a franchisor may require a prospective franchisee to enter into a confidentiality agreement without providing a disclosure document in advance, provided that the agreement in question contains only terms that require any information or material that may be provided to a prospective franchisee:
- to be kept confidential;
- to to be prohibited from use by the prospective franchisee; or
- to designate a location, site or territory for a prospective franchisee.
- Deposits: a franchisor is may receive a deposit by, or on behalf of, a prospective franchisee prior to or within the prescribed 14-day disclosure period if certain conditions are met.
- Statements of material change: statements of material change must include a certificate, signed by the same signatories as that of the certificate included in the disclosure document, certifying that it:
- contains no untrue information, representations or statements, whether of a material change or otherwise; and
- includes every material change.
- Financial statements: greater flexibility is extended to franchisors by allowing for the preparation of financial statements in accordance with generally accepted auditing, reporting and review standards as prescribed in the Chartered Professional Accountants Canada Handbook, or by US or international standards boards.

Generally, the amendments to the Ontario Act and its general regulation provide much-needed clarity and create more attractive business conditions for franchisors in Ontario. With these recent amendments, the Ontario legislature has arguably managed to strike a fair balance between reducing franchisors' regulatory burdens without adversely affecting the rights of franchisees to obtain access to the information reasonably required to make an informed business decision.

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ISBN 978-1-83862-663-1