

Updates to Ontario's Franchise Regulations

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In Ontario, franchise disclosure is governed by the *Arthur Wishart Act (Franchise Disclosure), 2000* (the “*Wishart Act*”) and its associated regulations. On September 1, 2020, several amendments (the “Amendments”) to the *Wishart Act* and its corresponding General Regulation, O. Reg 581/00, (the “General Regulation”) came into effect. The Amendments, which have been detailed below, have been adopted from recommendations made by Ontario's Business Law Modernization and Burden Reduction Council.

Confidentiality and Location Agreements

Under the previous s. 5 of the *Wishart Act*, franchisors were required to provide potential franchisees with a disclosure document at least 14 days before asking the franchisee to pay, or sign any agreement relating to the franchise, including confidentiality and non-disclosure agreements.

The amended s. 5(1.1) of the *Wishart Act* has carved out exceptions to the disclosure requirement. Pursuant to the Amendments, franchisors and potential franchisees can enter into legally-binding preliminary agreements relating to the franchise before providing a disclosure document, as long as the preliminary agreement only contains terms that:

- i. Requires the potential franchisee to maintain confidentiality regarding the information provided to them by the franchisor;
- ii. Restricts the potential franchisee from using any information that was provided to it by the franchisor; or
- iii. Reserves a location, site or territory for the potential franchisee.

It is noteworthy that the above exception will not apply if the franchisor:

- i. Seeks to protect confidentiality of information that was publically-available, disclosed without any contravention of the preliminary agreement, or disclosed with the franchisor's consent; or
- ii. Restricts disclosure of information to an organization of franchisees, other franchisees in the same franchise system, or their professional advisors.

Deposits

The previous s. 5(1)(b) of the *Wishart Act* prohibited the franchisor from receiving any consideration from the potential franchisee related to the franchise in the 14-day period immediately following the delivery of a disclosure document.

The amended s.5(1)(b) of the *Wishart Act* now permits franchisors to accept a deposit, as long as:

- i. The deposit does not exceed the prescribed amount, which is stated to be the lower of 20% of the franchise fee or \$100,000 (s. 7.1(1) of the General Regulation);
- ii. The deposit is fully refundable; and
- iii. The deposit does not oblige the potential franchisee to enter into a franchise agreement.

Statements of Material Change

The previous *Wishart Act* did not prescribe any requirements for the contents of a Statement of Material Change.

Section 5(5.1) of the amended *Wishart Act* states that a Statement of Material Change must contain certain prescribed information. The Amended ss. 7.1(2) and (3) of the General Regulation clarify that Statements of Material Change must include a certificate of disclosure, signed by the franchisor or its director or officer, certifying that the statement of Material Change does not contain any untrue information, representation or statement, and includes every material change.

Disclosure Exemption - Directors and Officers

The previous s. 5(7)(b) of the *Wishart Act* exempted a franchisor from the obligation to provide a disclosure document to a potential franchisee, if the potential franchisee was a director or officer of the franchisor or a franchisor's associate.

The amended s. 5(7)(b) of the *Wishart Act* exempts a franchisor from providing a disclosure document to a potential franchisee, if the potential franchisee is an individual or a corporation controlled by an individual who:

- i. Is currently a director or officer of the franchisor or a franchisor's associate and has been in the role for at least six months; or
- ii. Was a director or officer of the franchisor or a franchisor's associate for at least six months until no longer than four months ago.

Disclosure Exemption - Fractional Franchisee

The previous s. 5(7)(e) of the *Wishart Act* exempted a franchisor from the obligation to provide a disclosure document to a potential franchisee, if it involved the grant of a franchise to a person with an interest in a pre-existing business, where the anticipated sales from the franchise would constitute less than 20% of the pre-existing business' revenues.

The amended s. 5(7)(e) of the *Wishart Act* clarifies that the disclosure exemption applies when the anticipated sales from the franchise would constitute less than 20% of the pre-existing business' revenues during the first year of the franchise's operation.

Disclosure Exemption - Investment size

The previous s. 5(7)(g)(i) of the *Wishart Act*, in conjunction with the previous s. 9 of the General Regulation, exempted a franchisor from the obligation to provide a disclosure document to a potential franchisee if the franchisee invested less than \$5,000 for the acquisition and operation of the franchise. Additionally, the previous s. 5(7)(h) of the *Wishart Act*, in conjunction with the previous s. 10 of the General Regulation, exempted a franchisor from the obligation to provide a disclosure document to a potential franchisee if the franchisee invested greater than \$5,000,000 in one year for the acquisition and operation of the franchise.

The amended s. 5(7)(g)(i) of the *Wishart Act*, in conjunction with the amended s. 9(2) of the General Regulation, exempts the franchisor from the obligation to provide a disclosure document to a potential franchisee if the total initial investment is less than \$15,000. Additionally, the amended s. 5(7)(h) of the *Wishart Act*, in conjunction with the amended s. 9(3) of the General Regulation, exempts the franchisor from the obligation to provide a disclosure document to a potential franchisee if the total initial investment is greater than \$3,000,000.

Furthermore, the amended s. 9(1) of the General Regulation clarifies that the amounts to be included in calculating the total initial investment for the purposes of the above exemptions are:

- i. Deposits and franchise fees;
- ii. Estimated cost of inventory, leasehold improvements, equipment, leases, rentals, and other property costs; and
- iii. Any other costs associated with the establishment of the franchise.

Financial Statements

The previous ss. 3(1)(a), (b) and ss. 11(2)(a), (b) of the General Regulation required franchisors to include the franchisor's financial statements prepared on an audit or review engagement according to Canadian standards in their disclosure documents.

The amended ss. 3(1)(a), (b) and ss. 11(2)(a), (b) of the General Regulation permit the franchisor's financial statements to be prepared in a manner consistent with:

- i. The CPA Canada handbook;
- ii. The Financial Accounting Standards Board of the United States; or
- iii. The International Accountant Standards Board.

Conclusion

The Amendments were implemented with the objectives of reducing the cost of compliance with franchise disclosure requirements and providing clarity to certain sections of the *Wishart Act* and the General Regulation.

While the Amendments do provide clarity and resolve certain ambiguities, the regulatory burden of complying with the requirements might not change drastically for franchisors,

depending on the franchisor's aims. If an international franchisor wishes to grant franchises across Canada, the franchisor will be required to comply with franchise disclosure obligations across all regulated provinces, and may still be required to generate new financial statements. Moreover, the updated disclosure exemption based on investment size will likely not apply to most franchise systems. However, the new ability for franchisors to collect deposits and enter into non-disclosure agreements will provide franchisors with greater flexibility when engaging in negotiations with potential franchisees.