Fundamentals of Franchising - Canada
Coming to Canada!

• Situation #1: Planning for Successful Expansion
  • A fairly typical client meeting about a U.S. franchisor’s planned expansion to Canada

• Situations #2 to 6: What went wrong, eh?
  • A few example client meetings about a U.S. franchisor’s expansion to Canada gone wrong
Planning for Success in Canada

• Situation #1:
  • U.S. franchisor expanding to Canada using direct franchising model
  • Andraya and Larry – partners in Toronto law firm
  • Judy – US client visiting from afar
So you want to expand to Canada?

• Franchise Model
• Corporate Structure and Tax Planning
• Trademark Clearance and Protection
• “Canadianization” of Franchise Agreement and Ancillary Agreements
• Compliance with Canadian franchise disclosure laws
• Other Legal and Business Issues that may arise
What is the Deal?

• Single unit direct franchising?
• Master Franchising?
• Development Agreement?
• Area Representative Agreement?
• Joint Venture?
What do we need to know about Canada?

- What **should** you know about Canada?
- Canada should not be treated as the 51\textsuperscript{st} State
- Understand local competition and opportunities
- The subtle but important everyday differences between the US and Canadian markets
- Create a Canadian Identity
- French language issues
What else should we know about Canada?

• Leasing Practices in Canada are different than in the US
• “Turn key” approach to unit development
• You cannot assume you can import all goods and services from the US, but you can assume things cost more
Do we need “Boots on the Ground”?

- Need a Canadian head office or Canadian based management?
- Franchisee selection
- Site selection
- Training
- Supervising/enforcing system standards
- Local advertising
Who should be the Franchisor?

• Simple question, but answer more complicated
• Primarily driven by US tax considerations
• Careful Corporate and Tax Planning
  • Common Structure:
    • Existing or new US corporation as franchisor?
    • What type of US entity?
    • Withholding Tax issues
    • No Permanent Establishment! – Is the fear of one holding you back from Success in Canada?
Who should be the Franchisor?

• If Canadian corporation, what kind?
  • Regular Business corporation or Unlimited Liability Company?
  • In which jurisdiction?
  • Canadian and US tax issues
  • Intercompany IP and System License may be required
• Franchisor’s Financial Statements
  • Will need to be disclosed unless exemption available
  • Must be prepared on audited or review engagement basis
Trademark Clearance & Protection

- Trademarks and other IP
- Do I need to register in Canada?
- Trademark searches done?
  - Can important IP be protected?
- Trademark applications filed and registrations obtained?
- Local Branding Helps
  - “Canadianize” your important marks and logos?
  - French language equivalents needed?
Situation #1 – Sample of ‘Canadianized’ Logos

McDonald’s

Great Clips
IT’S GONNA BE GREAT

Wendy’s
How do we Canadianize our Agreements?

• Non-competition covenants
• Monetary and Currency Issues
• Withholding taxes
• Advertising Fund
How do we Canadianize our Agreements?

• Governing Law and Venue
• Mediation, Arbitration and Litigation
• Releases
• Security Agreements
• Quebec civil law
• French language issues
Can we just tweak our US FDD?

• Our first deal is in Ontario - Can we just do a “wrap” to our US FDD?
• Do we really need a National Canadian FDD?
  • Do we need to disclose in the unregulated provinces?
  • What about Quebec? Do I need an FDD in Quebec? Does it need to be in French?
• Can we use our parent’s Financial Statements?
Is it true we need a Customized FDD for each candidate?

• “All material facts” => The days of generic disclosure are gone
• Need to customize FDD for each candidate
  • Location, Territory
  • Unique build-out costs
  • Renovation Costs
  • Head lease
  • Rent security deposits
  • Additional information for resales/renewals
• Statement of Material Change used for site specific info
Does FDD need to be up-to-date for each disclosure?

• Most information in the disclosure document must be current each time it is delivered
  • limited information tied to fiscal year end
  • Everything else tied to date of disclosure

• SMC used to provide any updates/changes (e.g., new officers or directors, litigation, trade-marks, existing franchisees)
Situations #2 to # 6

- Situations #2 to 6:
  - A few example client meetings about a U.S. franchisor’s planned expansion to Canada gone wrong
- Judy and Larry – partners in Toronto law firm
- Andraya – US client visiting from afar
Situation #2 – Disclosure Issues

Are we offside? ...

- LOI Signed
- Deposit Obtained
- Confidentiality Agreement Signed
- We gave out our US FDD for informational purposes only
Situation #3 – Rescission / Disclosure Issues

Do we have a disclosure problem?

• Location unknown
• Certificate not signed
Rescission

We failed to disclose – What’s the worst that can happen?

• 60 days to rescind following receipt; or
• Within 2 years if no FDD provided

• **But Judicial Trend:** If “material deficiencies” in FDD, courts say “akin to no disclosure” and will apply full 2 years rescission
• Refund fees and reimburse direct or indirect losses
Situation #4 – System Changes/Bad Faith

We’ve added a new product line!

• Requires new equipment
• Expensive but worth it
• Didn’t consult with our franchisees
Duty of Good Faith and Fair Dealing

- Cannot undermine or defeat contract objectives
- Permits self-interested acts with regard to interests of others
Situation #5 – Right to Associate

• A few vocal franchisees don’t like the new product
• They are trying to form a group and refuse to sell it!

How do we prevent this?
Situation #6 – Injunctive Relief

• We’ve terminated a Franchisee who refused to sell the new product
• They have taken down some of their signs but continue to operate

1. Can we make them take our signs down?

2. Can we stop them from operating?
Injunctive Relief

Test in Canada:

1. Serious Questions to be Tried
2. Irreparable Harm
3. Balance of Convenience
Non-Competition Clause

Considerations:

1. Reasonableness
   a) Duration
   b) Area
   c) Scope
2. Must protect legitimate interests
3. Unambiguous
Alternative Dispute Resolution

• Can we get an injunction when there is an arbitration clause?

• Do we have to arbitrate, if there is an arbitration clause?
Jurisdiction

• The governing law is Ontario. The franchisee is in British Columbia

• Where do we sue?
Andraya Frith
Osler Hoskin & Harcourt LLP
Toronto, ON, Canada

Judy Rost
Alexander Holburn Beaudin + Lang LLP
Vancouver, BC, Canada

Larry Weinberg
Cassels Brock & Blackwell LLP
Toronto, ON, Canada