



CLIENT ALERT

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CHANGES TO ONTARIO'S FRANCHISE LAWS: WHAT YOU NEED TO KNOW FOR 2021

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On July 16, 2020, the government of Ontario announced that amendments to the *Arthur Wishart Act (Franchise Disclosure), 2020* (the "Act") and to its General Regulation (the "Regulation") will be brought into force on September 1, 2020. The amendments were first introduced in 2017 as part of Ontario's push towards less burdensome disclosure requirements and greater clarity on the Act and Regulations.

CONFIDENTIALITY AGREEMENTS

Currently, a franchisor is required to provide a disclosure document to a prospective franchisee 14 days prior to the payment of any consideration or the signing of the franchise agreement or **any other agreement relating to the franchise**. This later requirement was considered broad enough to apply to confidentiality and non-disclosure agreements, thus denying franchisors the ability to protect sensitive information contained in their disclosure documents. As of September 1st, franchisors will be able to require a franchisee to enter into an agreement relating to the franchise, without providing a disclosure document, as long as the agreement contains only terms that:

- i. require any information or material that may be provided to a prospective franchisee to be kept confidential;
- ii. prohibit the use of any information or material that may be provided to a prospective franchisee; or
- iii. designates a location, site, or territory for a prospective franchisee.

DEPOSITS

Currently, a franchisor is prohibited from receiving payment of any consideration related to the franchise from a prospective franchisee prior to or during the 14-day disclosure period. The amendments will lift this absolute prohibition on payments and will permit franchisors to receive deposits as long as the deposit:

- i. does not exceed 20% of the initial franchise fee, up to maximum of \$100,000,
- ii. is refundable without any deductions, and
- iii. is given under an agreement that in no way binds the prospective franchisee to enter into a franchise agreement.

CHANGES TO FINANCIAL DISCLOSURE

Currently, franchisors are required to include in their disclosure documents financial statements prepared in accordance with generally accepted auditing standards or review engagement standards that are, at a minimum, equivalent to those set out in the *CPA Canada Handbook*. These requirements have been burdensome for foreign franchisors who are required to reconcile their financial statements with Canadian standards prior to including them in a disclosure document.

The amendments replace this requirement and will now permit financial statements to be "prepared in accordance with generally accepted auditing standards as set out:

- i. in the CPA Canada Handbook,
- ii. by the Auditing Standards Board of the American Institute of Certified Public Accountants or the Public Company Accounting Oversight Board of the United States, as applicable, or
- iii. by the International Auditing and Assurance Standards Board."

If financial statements are prepared on a review engagement basis, the amendments will permit them to be prepared in accordance with generally accepted accounting principles that meet the review and reporting standards applicable to review engagements as set out:

- i. in the CPA Canada Handbook,
- ii. by the Financial Accounting Standards Board of the United States, or
- iii. by the International Accounting Standards Board.

CHANGES TO DISCLOSURE EXEMPTIONS

A franchisor is exempt from providing disclosure documents to a prospective franchisee who has been an officer or director of the franchisor for at least six months. The amendments will leave this exemption in place but clarify that the exemption is applicable to both an individual who has been an officer or director of the franchisor corporation, and a corporation controlled by the individual that has been an officer or director provided that the individual:

- i. has been an officer or director for at least six months and is currently an officer or director; or
- ii. was an officer or director for at least six months and not more

than four months have passed since the individual ceased being an officer or director.

Currently, there is an exemption from the requirement to provide a disclosure document to a prospective franchisee who is required to make a “total annual investment” of \$5,000 or less to acquire and operate the franchise. The amendments will instead make the exemption available when a prospective franchisee’s “total initial investment” is \$15,000 or less. The total initial investment is determined by adding all of the franchisee’s costs associated with the establishment of the franchise inclusive of:

- i. the amount of any deposit or franchise fee;
- ii. an estimate of the costs of inventory, leasehold improvements, equipment, leases, rentals and all other tangible and intangible property necessary to establish the franchise; and
- iii. any other costs or estimate of costs associated with the establishment of the franchise not listed in (i) or (ii), including any payment to the franchisor, whether direct or indirect, required by the franchise agreement.

Lastly, the exemption from providing a disclosure document to a prospective franchisee whose required “total annual investment” is \$5,000,000 or more to acquire and operate the franchise will be replaced with a lower threshold of \$3,000,000 or more “total initial investment” as a result of the amendments.

STATEMENT OF MATERIAL CHANGE

Although generally common practice, it will now be a requirement that a certificate of disclosure, signed by the franchisor (or an officer or director of the franchisor if incorporated), be included with the Statement of Material Change certifying that it contains no untrue information, representations or statements, and includes every material change.

KEY TAKEAWAYS

The amendments were proposed in Ontario to address ambiguity in the Act and reduce the cost of compliance for franchisors. Practically speaking, changes to the investment dollar amounts for disclosure exemption eligibility will be instrumental to few and the inclusion of a certificate of disclosure with the Statement of Material Change is already common practice; the amendments in these regards are hardly momentous. However, the ability to use U.S. prepared financial statements, as is, in an Ontario franchise disclosure document is a huge step towards lessening the burden of American franchisors looking to expand into Ontario. With

this amendment, Ontario will be the only province in Canada permitting disclosure of financial statements that are not at least equivalent to Canadian standards. Therefore, franchisors who use a single disclosure document for its operations across Canada will not derive any benefit from this amendment until other provinces follow suit. All things considered, the amendments are long-awaited and welcomed revisions to the Act and its Regulations.

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