WORKING FOR THE BRAND: THE REGULATION OF EMPLOYMENT IN FRANCHISE SYSTEMS IN AUSTRALIA

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Abstract: In the past five years or so, there has been a never-ending stream of investigations and inquiries into so-called ‘wage theft’ in franchise systems in Australia. This article seeks to go beyond these public accounts by considering key legislative provisions and recent case law which directly relates to the quality of franchise work and the regulatory behaviour of both franchisees and franchisors. In particular, the article considers three critical issues in this context: 1) the legal classification of franchisees under the Fair Work Act 2009 (Cth) (‘FW Act’), including their possible employment status; 2) the application of collective bargaining arrangements to franchise networks; and 3) the ascription of liability for contravention of the civil remedy provisions of the FW Act, including 2017 reforms expressly directed at franchise relationships. This analysis reveals that while the regulation of work and employment in franchise networks has attracted much attention, it remains uncertain in many key respects and continues to be in a state of great flux.

I INTRODUCTION

Following the 2015 investigation into the serious and systemic underpayment of vulnerable workers across the 7-Eleven franchise network, the business format franchising model has garnered much attention from policy-makers, regulators and the public. While the 7-Eleven case may constitute the biggest instance of ‘wage theft’ in Australia’s history, it has been observed that ‘7-Eleven is unlikely to be alone in being associated with significant wage exploitation of its franchisee employers.’ Indeed, in the wake of the 7-Eleven investigation, a number of other well-known brands, such as Sunglass Hut and Subway, have been plagued by similar underpayment

† Senior Lecturer, Melbourne Law School, University of Melbourne. This research was supported by the Australian Government through the Australian Research Council's Discovery Early Career Award (DE180100279). The author is grateful to the helpful comments of the anonymous referee and the excellent research assistance of Louise de Plater. This article was largely written prior to the declaration of the COVID-19 pandemic. While COVID-19 has significant implications for the regulation of work in franchises, it is only briefly surveyed in this piece (but see T Hardy, ‘What Now for Wage Theft? Enforcement of Employment Rights and Entitlements in a Time of Crisis’, Labour Law Downunder, 22 April 2020 <https://labourlawdownunder.com.au/?p=829>).

1 In this instance, it was revealed that franchisee employers across the 7-Eleven network had sought to evade the law, reduce their labor costs, and increase their profits by falsifying employment records and underpaying and intimidating vulnerable employees, including international student workers. Workers were frequently paid for only half their hours worked or they were forced to repay a significant proportion of their wages back to their employers in cash. See Senate Education and Employment References Committee, A National Disgrace: The Exploitation of Temporary Work Visa Holders (2016).

2 Laurie Berg and Bassina Farbenblum, ‘Remedies for Migrant Worker Exploitation in Australia: Lessons from the 7-Eleven Wage Repayment Program’ (2018) 41(3) Melbourne University Law Review 1035. Latest reports suggest that over $160 million has been paid to current and former 7-Eleven employees in wages, superannuation and interest. See Allan Fels and David Cousins, Report of the Migrant Workers’ Taskforce, Australian Government (March 2019) 40 (‘Migrant Workers’ Taskforce Report’).

3 Migrant Workers’ Taskforce Report (n 2) 40.
scandals. A recent audit of emerging franchises by the Office of the Fair Work Ombudsman (‘FWO’) found that 78% of businesses were in breach of at least one workplace obligation.

Historically, most franchising experts and industrial relations scholars have believed that franchisees, in their capacity as the direct employer, would be held responsible for compliance with employment-related entitlements and obligations in Australia. However, in the wake of various inquiries and reforms over the past five years, it seems that franchisors can no longer assume that they may avoid accountability in this domain. The head of the FWO has previously noted that: ‘[a]ll franchise outlets are on notice that they must pay staff lawful minimum pay rates and franchisors should take responsibility for ensuring that their franchisees comply with the law.’ The recent Parliamentary Inquiry into the Franchising Code of Conduct (‘Franchising Code’) similarly stated that ‘the issue [of wage theft] is far more complex and partly inherent to the business models' structural breakdown of power and the imposition of cost controls.’ This brief description of the problem is supported by more detailed research undertaken elsewhere. For example, it has been pointed out that while franchisors’ claim they have no influence over the wages franchisees pay to workers, they effectively control wages ‘by controlling every other variable in the business except wages.’ Separately, Professor David Weil, a labour economist based in the United States, has argued that a failure to adequately address franchisor opportunism may have direct implications for franchise workers as it can ‘create incentives for franchisees to violate laws.’ More generally, Lorelle Frazer and Anthony Grace have observed that although ‘the franchisor and its franchisees share a common goal of profit maximization they operate as legally distinct businesses and will therefore have different priorities and viewpoints, sometimes diverging widely in their behaviours.’

It is clear from this short overview that the regulation of work and employment within franchise systems is gaining prominence as an important area for research and reflection. This article will consider a number of discrete issues that arise in the regulation of work and employment in franchise systems in Australia, with particular reference to the provisions of the Fair Work Act 2009 (Cth) (‘FW Act’): the statutory cornerstone of the federal workplace relations system. The article commences with a discussion of the extent to which franchisees may be characterised as employees at common law and access employment-related entitlements, benefits and protections

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7 Ashlea Kellner, David Peetz, Keith Townsend and Adrian Wilkinson, ‘“We are Very Focused on the Muffins”: Regulation of and Compliance with Industrial Relations in Franchises’ (2016) 58(1) Journal of Industrial Relations 25, 41.
8 Fair Work Ombudsman, ‘Former Chatime Franchisee Faces Court’ (Press Release, 4 April 2019).
9 Ibid.
under the FW Act and other related legislation. This is followed by an analysis of the enterprise bargaining system under the FW Act and its application to franchise systems. The final section undertakes an analysis of whether, and under what provisions, a franchisor may be held liable for underpayment contraventions committed by its franchisees.

II COVERAGE OF THE FW ACT AND MINIMUM EMPLOYMENT STANDARDS

Classifying a work contract as one of employment has significant regulatory consequences. For example, many of the key rights and protections prescribed by the FW Act – such as the National Employment Standards, modern awards, enterprise agreements and unfair dismissal provisions – only apply to employees and do not typically extend to independent contractors.

As the FW Act does not contain a statutory definition of employment, we must rely on common law tests to determine whether a particular individual is an employee or an independent contractor. The leading case on this issue – the High Court decision in Hollis v Vabu – requires the balancing of multiple indicia, taking into account the totality of the relationship. These indicia include, amongst other factors:

a) whether the principal/putative employer has the right to control the way work is performed;
b) whether the worker is integrated into the principal/putative employer’s business;
c) whether the worker is exposed to financial risk or potential profits from the running of a business; and
d) whether the worker has the power to delegate or subcontract the work to another.

While this broad list of indicia usefully captures a wide range of circumstances, the application of this general test is not necessarily settled. In particular, the proper weight to be placed on the terms of the written employment contract, the receipt of paid leave, the deduction of employment-related taxes and other entitlements, and the use of the corporate form, are all relatively contentious. Ultimately, however, it is the substance and not the form of the relationship which the court will consider. Labelling a business activity a franchise (or some other form of commercial relationship) will not be determinative.

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14 The distinction between employees and independent contractors is also relevant in relation to a range of other legislation regulating matters such as long service leave, workers’ compensation and superannuation/pension entitlements, amongst others. However, discussion of these other statutory regimes goes beyond the scope of this article and will not be discussed.

15 The National Employment Standards statutorily prescribes 10 minimum employment conditions, including working hours, various leave entitlements, notice of termination, redundancy pay and other matters. While all these standards apply to ongoing employees (including full-time and part-time employees), only a select number apply to casual employees.

16 Modern awards are instruments which operate with the force of legislation and are designed to supplement the National Employment Standards. Modern awards generally prescribe industry or occupational wage rates across different work classifications, loadings, penalty rates and allowances. Awards also generally regulate scheduling of working hours, consultation over change initiatives and dispute resolution procedures. The coverage of awards does not normally extend to managerial, supervisory or professional workers.

17 Outworkers in the textile, clothing and footwear industries are a notable exception.


In the context of franchising, the common law distinction drawn between independent contractors and employees is arguably most difficult to apply in relation to ‘small sole trader franchisees in unsophisticated franchising arrangements such as those, for example, involving domestic services.’ Some courts in the United States have previously found franchisees to be employees in certain, select instances. For example, in the case of *Auwah v Coverall North America Inc*, the court – at trial and on appeal – found that the franchisor, Coverall North America, Inc, had unlawfully misclassified a group of janitorial franchisees as independent contractors rather than employees. As a result, the janitors were able to successfully claim unpaid employment benefits. At this stage, there have not been any reported cases in Australia where franchisees have challenged their legal characterisation as an independent contractor.

The absence of case law in this area is somewhat surprising for two reasons. First, many have argued that franchisees exhibit features typical of ordinary employees. Some, such as Alan Felstead, have gone so far as to suggest that a franchising relationship is one of quasi-employment. In the Australian context, Joellen Riley has previously argued that if a franchisee (along with family members) is the only worker in the business, then it is very similar to a standard employment relationship (except that the franchisee is required to purchase their entitlement to work and accept the risks that come along with business operation and ownership). She further notes that while remuneration in a franchise is based on sharing business revenue, this ultimately makes the franchisee similar to an employee who is paid on commission.

Second, the risks of potentially misclassifying franchisees as independent contractors is heightened by the statutory prohibition relating to ‘sham contracting’. More specifically, under the FW Act, employers are prohibited from misrepresenting an actual or proposed employment relationship as an independent contracting arrangement. If the sham contracting provisions are enlivened, the ‘real’ or ‘actual’ employer may not only be liable for employment-related entitlements, but may

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21 Terry and Huan (n 6) 399.
23 For further discussion, see Emerson (n 6).
24 There has, however, been at least one successful claim brought against a former Coverall franchisor under the Franchising Code of Conduct and the *Competition and Consumer Act 2010* (Cth) for breach of the unconscionable conduct provisions, amongst other claims. It is quite possible that the franchisee cleaners in these proceedings may have had potential claims under the *Fair Work Act 2009* (Cth), but these do not appear to have been pursued. See *Australian Competition and Consumer Commission v South East Melbourne Cleaning Pty Ltd (in liq) (formerly known as Coverall Cleaning Concepts South East Melbourne Pty Ltd)* [2015] FCA 25 (29 January 2015). See also a series of cases involving another Coverall franchisor which was brought under state-based consumer protection legislation: *Coverall NSW Pty Ltd v Chow* [2013] NSWDC 59.
28 See FW Act, s 357, Sections 358 and 359 of the FW Act respectively prohibit a person: from dismissing or threatening to dismiss an employee in order to engage them to perform substantially the same work as an independent contractor; and from making what they know to be false statements to induce a current or former employee to agree to such an engagement. See generally FW Act, Pt 3-1, Div 6.
also be exposed to a range of civil remedies, including pecuniary penalties. However, for various reasons, the sham contracting provisions have been largely underutilised. An important conceptual limitation is that, unlike the accessorial liability provisions outlined below, the sham contracting provisions do not have the effect of extending liability to third parties that display only some (if any) employer characteristics, such as a franchisor. Rather, the sham contracting provisions reflect and uphold key concepts underpinning the binary employment relationship, albeit a greater emphasis is placed on the economic realities of the relevant arrangements, rather than technical corporate forms.

Notwithstanding the control and economic dependence inherent within most franchising relationships, historically it has been assumed that ‘the structure of these business networks precludes any finding of an employment relationship between the parties’. For a start, the franchisees are often incorporated, which makes it difficult, albeit not impossible, to argue that the contract is one of personal service. Further, franchisees generally enjoy a contractual, if not a practical, right to delegate non-managerial work to others. In these circumstances, and under current case law, it is somewhat unlikely that an independently owned and operated franchisee will be classified as an employee at common law.

Even if a franchisee is properly characterised at law as an independent contractor, it is important to note that the FW Act provides some level of protection for non-employees. In particular, employees and independent contractors may be able to make a claim under provisions dealing with workplace bullying, as well as an array of prohibitions – known as ‘general protections’ – which are broadly designed to protect workers from a range of wrongful treatment. There have been some isolated instances where employees within franchises, including company-owned franchise units, have successfully obtained compensation under the ‘adverse action’ provisions of the FW Act, which essentially prohibits a person taking ‘adverse action’ for a ‘prohibited reason’. It is important to point out that the broad scope of certain adverse action provisions (e.g.

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29 See, eg, Fair Work Ombudsman v Quest South Perth (2015) 256 CLR 137.
34 Fair Work Ombudsman v Ecosway Pty Ltd [2016] FCA 296.
35 FW Act, Pt 6-4B.
36 FW Act, Pt 3-1. In addition, independent contractors may avail themselves of protections under various anti-discrimination statutes that apply at both federal and state levels in Australia.
38 ‘Adverse action’ may include various forms of conduct engaged in by: 1) employers in relation to their employees; or 2) principal contractors in relation to independent contractors. Relevant forms of adverse action include: termination of the contract; injuring an employee in their employment or injuring an independent contractor in relation to the terms and conditions of their engagement; or altering an employee’s or independent contractor’s position to their prejudice.
39 There are three ‘prohibited reasons’ which are proscribed under the FW Act. First, s 340 prohibits adverse action against another person because of certain grounds relating to workplace rights. Second, s 346 prohibits adverse action against another person because of grounds generally relating to their industrial status or their engagement in industrial activities. Third, s 351 prohibits employers taking adverse action against an employee because the employee has a particular status (e.g. race, colour, sex, sexual preference, age, physical or mental disability, marital status, family or carer’s responsibilities, pregnancy, religion, political opinion, national extraction or social origin). For a detailed discussion of these provisions, see Beth Gaze, Anna Chapman and Adriana Orifici, ‘Evaluating the Adverse Action Provisions of the Fair Work Act: Equality Thwarted?’ in John
s 340 applies to all persons and is not confined to employees), combined with the express reference to forms of adverse action that a principal contractor may take against an independent contractor, means that it may be possible for an independent franchisee to seek relief if they have been subject to ‘adverse action’ taken by the franchisor as a result of exercising a ‘workplace right’.

As yet, however, there have been no cases brought by franchisee contractors on this basis.

### III COLLECTIVE BARGAINING, ENTERPRISE AGREEMENTS AND FRANCHISES

In addition to the minimum standards set out in the FW Act and modern awards, terms and conditions of employment may also be set via an ‘enterprise agreement’. Enterprise agreements are typically negotiated between employers and their employees (often, but not always, with the involvement of a union). While these agreements generally deal with wages and other employment conditions as they apply to a specific ‘enterprise’, it is important to note that ‘enterprise’ is defined broadly to mean any kind of business, activity, project or undertaking.

There are a number of ways in which enterprise agreements may apply to workers beyond the boundaries of a single firm or franchise unit. For example, a 2016 survey of the Australian franchising sector estimated that some 23 percent of franchisors had an enterprise agreement in place that governed wages and working conditions of employees across the franchise network.

More specifically, under the FW Act, there are a number of different types of agreements available, including single- and multi-enterprise agreements, which may be relevant in relation to franchises. While a single-enterprise agreement can be made by a single employer, it can also be made with two or more employers where they are related corporations, or conduct a joint venture or common enterprise. The concept of a common enterprise has been found to require some degree of ‘commonality of interest, or closeness of connection or sharing of operations.’

There have been various instances where a franchise has sought approval of a single-interest enterprise agreement under these provisions and on the basis that the various employers to be covered by the agreement are engaged in a ‘common enterprise’.

Alternatively, it is also possible to make a single enterprise agreement where the applicant has obtained a ‘single interest employer authorisation’ from the federal tribunal. This authorisation procedure was introduced under the FW Act to ‘clarify the uncertainty arising from inconsistent...

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40 FW Act, s 342. See also *Fair Work Ombudsman v First Group of Companies Pty Ltd & Ors* [2018] FCCA 1228, where Jones J reflects on application of Part 3-1 to supply chains: at [156].

41 FW Act, s 12.

42 The use of enterprise agreements was found to be slightly higher in retail franchises (25 percent) rather than non-retail franchise formats (21 percent). See Lorelle Frazer, Scott Weaven, Anthony Grace and Selva Selvanathan, *Franchising Australia 2016* (Griffith University, 2016) 28 (‘Franchising Australia Survey’).

43 See Appendix for extract of key provisions relating to enterprise agreements under the FW Act.

44 For example, a single unit-holder may make an enterprise agreement which covers only the employees employed directly by the franchisee (e.g. *Re Pennyco Pty Ltd (t/as Zarraffas West Ipswich)* [2016] FWCA 7494; *Gohomilli Pty Ltd (t/as Grill’d Darlinghurst re Grill’d Darlinghurst Enterprise Agreement 2010* [2010] FWAA 9222). There may also be more than one single-enterprise agreement within a single employer. This is particularly common where there are multiple unions representing workers within the employer’s business or where the employer has multiple sites at different locations.

45 *Qantas Airways Ltd v AMWU* (AIRC, S5768, 8 May 2000) at [32].

46 See, eg, *Yum! Restaurants Australia Pty Ltd v Pizza Hut* [2014] FWCA 6547.

47 FW Act, s 172(2), (5).
[tribunal] decisions on whether franchisees were engaged in a “common enterprise” within the meaning of the predecessor legislation.\textsuperscript{48} In the decade since these provisions were introduced, it has been relatively common for a franchisor,\textsuperscript{50} or a group of franchisees operating separate businesses under the same brand,\textsuperscript{51} to formally apply to the Fair Work Commission (‘FWC’) for a single interest employer authorisation. The FWC is required to grant the authorisation in relation to a proposed enterprise agreement, if the relevant statutory requirements are satisfied (e.g. the employers that will be covered by the agreement have agreed to bargain together, no person coerced, or threatened to coerce, any of the employers to agree to bargain together, and the employers carry on similar business activities under the same franchise).\textsuperscript{52} Once the single interest employer authorisation is granted, the franchisor, or group of franchisees, may subsequently make an enterprise agreement which applies to workers in certain franchise units, or throughout the franchise. Since the passage of the FW Act, there have been numerous applications brought by a range of emerging and established franchises seeking a ‘single interest employer authorisation.’ For example, applications have been made by, and granted to, a wide variety of applicants, including: McDonald’s (in relation to 315 franchisees);\textsuperscript{53} Oporto (in relation to the franchisor and 26 other employers);\textsuperscript{54} Jellis Craig (where the two franchisee employers sought a relevant authorisation to make an enterprise agreement to cover employees working in the areas of property management, property sales and administration);\textsuperscript{55} and Bendigo Bank franchisees (in relation to clerical employees working in two specified units).\textsuperscript{56}

In comparison, a multi-enterprise agreement is an agreement made by two or more employers that cannot meet the ‘single interest’ requirement noted above. There is no need to obtain prior authorisation before making a multi-enterprise agreement, no capacity for protected industrial action to be taken in support of such an agreement, and no enforceable obligation to bargain in good faith in relation to a multi-enterprise agreement. The major drawback of a multi-enterprise agreement (as compared to a single enterprise agreement) relates to the procedures for employee approval.\textsuperscript{57} Ultimately, under the FW Act, employers are generally free to elect whether to make a single-enterprise agreement or a multi-enterprise agreement.

\textsuperscript{48} Andrew Stewart et al, Creighton and Stewart’s Labour Law (Federation Press, 6th ed, 2016) 361.
\textsuperscript{49} Workplace Relations Act 1996 (Cth).
\textsuperscript{50} McDonald’s Australia Ltd [2018] FWC 5831.
\textsuperscript{51} For example, six Bakers Delight franchisees applied for a single interest employer authorisation in relation to themselves and other specified franchisees in various states around Australia. While this application was not made directly by the franchisor, it was supported by the HR Manager of the Bakers Delight franchisor (who was nominated as the relevant contact person in relation to the authorisation). See, eg, APP Badges Pty Ltd [2012] FWA 5131 (the single-interest employer authorisation was granted in relation to the proposed Bakers Delight (NSW) Enterprise Agreement 2012 (i.e. the authorisation was stated to apply to the applicant, APP Badges Pty Ltd, as well as 32 other Bakers Delight franchisees based in NSW and named in the application).
\textsuperscript{52} FW Act, s 249.
\textsuperscript{53} McDonald’s Australia Ltd [2018] FWC 5831.
\textsuperscript{54} Application by Oporto (Franchising) Pty Ltd [2016] FWC 2297.
\textsuperscript{55} Application by Jellis Craig North Side (Sales) Pty Ltd and Jellis Craig North Side (PM) Pty Ltd [2016] FWC 5809.
\textsuperscript{57} A multi-enterprise agreement will only be valid if there is majority approval in at least one enterprise. Where such approval is not given by employees at any given enterprise, that enterprise will not be bound by the multi-enterprise agreement. In comparison, a single-enterprise agreement must be approved by a majority of employees across the relevant enterprise casting a valid vote: FW Act, s 182. Another potential disadvantage of multi-enterprise agreements is that at any time an employer who is covered by such an agreement may choose to enter into a single-enterprise agreement of its own. If this occurs, the single-enterprise agreement effectively overrides the multi-enterprise agreement. FW Act, s 58(3).
In some respects, the potential flexibility and breadth of these enterprise agreements represent important developments in light of the fact that it has been ‘difficult if not impossible for employees in small franchise outlets to organise, and bargain effectively for wages and working conditions’. However, as Riley has observed, removing legal hurdles to bargaining across a franchise does not necessarily address the many practical obstacles facing workers and their unions in this sector. For example, in a 2018 interim decision relating to the Guzman Y Gomez franchise, Commissioner McKenna expressly raised concerns about the apparent absence of an employee bargaining representative and the lack of evidence to suggest that there was any bargaining which had taken place in relation to the proposed enterprise agreement. The Commissioner further noted that these issues were particularly significant in light of the fact that ‘[o]f the approximately 1,688 employees who would be covered by the Agreement, 1043 are from non-English speaking backgrounds; 716 are part-time employees; 829 are casual employees; and 538 are aged under 21 years (including school children, given the arrangements for their minimum shifts).’

In the past few years, there have been growing concerns about the standards being applied under enterprise agreements made under the FW Act, as well as so-called ‘zombie agreements’ which were made under the predecessor legislation, but continued to apply to employees beyond the nominal expiry date. Many of the employees covered by these agreements were receiving less than those covered by the applicable modern award. This has led to a slew of applications by employees, unions and other collective representatives, including applications to terminate expired agreements so that employees may benefit from the terms of the underlying award, as well as applications to extend the coverage of enterprise agreements to employees who may have been excluded for historical or technical reasons. By way of illustration, in 2017, the Retail and Fast Food Workers’ Union (‘RAFFWU’) applied to terminate Domino’s Pizza 2005 collective agreement, which largely applied to drivers working in the pizza franchise. In a separate and earlier

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59 Ibid.
60 Guzman Y Gomez Leasing Pty Ltd v Guzman Y Gomez [2018] FWC 6706.
63 The Retail and Fast Food Workers’ Union is not a registered organisation under the FW Act, but has nonetheless been active in various applications relating to existing and proposed enterprise agreements.
64 See, eg, Re Oliver May-Johnstone-Wyly [2018] FWCA 908. This application was made by an employee of a Yoghurt Shop franchise seeking termination of the ‘Yoghurt Shop Pty Ltd Collective Agreement Number One’, which was originally made in 2006 under the Work Choices legislation. Notwithstanding the fact that the agreement had passed its nominal expiry date in 2009, it continued to apply to employees working in one or more SA-based outlets of the Yoghurt Shop franchise up to its formal termination in 2018.
65 See, eg, Caden Group Pty Ltd v Shop, Distributive and Allied Employees Association & Ors [2017] FCCA 3055. In this case, a Bakers Delight multi-unit franchisee sought a declaration that its non-transferring employees (those employed by a store after it was taken over by the franchisee) were not covered by the General Retail Industry Award 2010 (but rather were covered by either the Bakers Delight Collective Agreement (Victoria) 2006 or the Bakers Delight (Victoria) Enterprise Agreement 2011). As at the time of the application, both agreements prescribed conditions that were less generous than the relevant Award. The Court ultimately rejected the application determining that the Award applied to all non-transferring employees of the franchisee. Cf Re Shop, Distributive and Allied Employees Association [2014] FWC 4394 and Shop, Distributive and Allied Employees Association [2013] FWC 3859. In both these cases, the SDA sought orders that two transferable instruments, the Red Rooster Agreement 2009 and the Chicken Treat Employees SDA Agreement 2009 which covered transferring employees would also cover non-transferring employees who performed transferring work for the new employer franchisees notwithstanding the fact that those agreements would not have passed the BOOT. The SDA entered into an MOU with Red Rooster and Chicken Treat specifying that a replacement enterprise agreement would be negotiated, and employees would receive pay increases in the meantime.
application, the Shop, Distributive and Allied Employees Association (‘SDA’) had applied to terminate 27 industrial instruments that applied to employees working under the Domino’s Pizza brand.66 Both applications were ultimately heard together with SDP Hamberger deciding to terminate all expired agreements, which meant that employees – whose conditions were previously set by these agreements – reverted to the underlying modern award.67 This has since led to a novel Federal Court class action brought on behalf of franchisees who allege that the franchisor engaged in misleading or deceptive conduct by instructing franchisees to pay workers in accordance with these outdated enterprise agreements.68 This case continues before the courts.

Broadly-speaking, in order for an enterprise agreement to come into effect under the FW Act, it must comply with certain statutory requirements,69 be voted on and approved by a majority of employees70 and must ultimately pass the ‘better off overall test’ or ‘BOOT’. This last requirement is arguably the most significant in that it requires the FWC to be satisfied, as at the test time, that an employee to be covered by the proposed enterprise agreement would be better off overall if the agreement applied to the employee than if the relevant modern award applied to the employee.71 This has proved to be a major stumbling block for some franchises that have sought to remove or reduce key conditions, such as weekend penalty rates, that would otherwise apply under the relevant award. For example, in 2018, Domino’s Pizza sought approval for a new enterprise agreement which was intended to cover all employees working across approximately 660 outlets throughout the network.72 While the proposed agreement was approved by the requisite number of employees,73 and the main union involved in the negotiation praised several key provisions,74 other employee representatives, such as the RAFFWU, believed it represented a ‘terrible deal’75 on the basis that it failed the BOOT. The Domino’s-SDA Enterprise Agreement was initially put before the FWC for approval, however, the agreement was the subject of formal challenge by RAFFWU. Then, in March 2018, the franchisor – Domino’s Pizza Enterprises Ltd – unexpectedly withdrew the application prior to any decision by the tribunal.76 It seems the franchisor had decided to apply the Fast Food Industry Award to employees throughout the franchise, rather than proceed with the enterprise agreement, ostensibly on the basis that it could achieve ‘better benefits and security for

67 Shop, Distributive and Allied Employees Association & Ors [2017] FWCA 5703.
69 For example, the content of the proposed enterprise agreement: must only deal with ‘permitted matters’; must include mandatory terms (e.g. a nominal expiry date, a dispute settlement clause); and must not include any unlawful terms (e.g. discriminatory terms or opt-out clauses). See Stewart et al (n 48) 365-382.
70 A single enterprise agreement is made when a majority of the employees who have been asked to approve the agreement, and who cast a valid vote, approve it (FW Act, s 182(1)). However, in relation to a single-enterprise agreement involving two or more single interest employers, the proposed agreement is approved by the majority of employees employed by all of the employers that will be covered by the agreement, even if a majority of employees within a single employer unit have not voted to approve the agreement. See Stewart et al (n 48) 386.
71 FW Act, s 193(1).
73 According to reports, 30 percent of a total of 20,000 employees voted on the deal, with 89 percent of those who voted in favour of the agreement, which was largely negotiated between Domino’s Pizza and the SDA. See ‘Domino’s Deal Backed; Prices and Pay Neck-and-Neck; and More’, Workplace Express, 31 January 2018.
74 For example, the SDA pointed to new agreement provisions which guaranteed 15 hours per week for part-time workers, allowed voluntary work on public holidays, improved the uniform provisions and provided enhanced leave benefits. See ‘Domino’s Deal Backed; Prices and Pay Neck-and-Neck; and More’, Workplace Express, 31 January 2018.
75 ‘Domino’s Deal Backed; Prices and Pay Neck-and-Neck; and More’ (n 74).
76 ‘Domino’s Abandons Bargaining, Plumps for Award’, Workplace Express, 26 March 2018
employees through the award, rather than through bargaining’.\(^{77}\) The Franchise Council of Australia recently submitted that

the enterprise bargaining system is failing employers and employees. With many large companies now opting to fall back on the award because of uncertainty about what would be an acceptable enterprise agreement, or pass the better off overall test (BOOT), it’s time for a rethink.\(^{78}\)

The setting of standards in franchise networks – whether via modern awards or enterprise agreements – has just become even more complex, and contested, as a result of COVID-19.\(^{79}\) This is deeply concerning from a regulatory perspective. Clarity around standard-setting is critical for compliance purposes, and yet it is an area where uncertainty abounds. As Deputy President Colman recently observed in a decision relating to termination of a McDonald’s enterprise agreement:

The stakes are high. It is of the utmost importance that, when the Award commences to apply to the workforce, McDonald’s and its franchisees comply fully with their obligation to pay all 109,000 of their workers properly. If they do not do so, they will face claims for underpayment and the imposition of penalties.\(^{80}\)

The potential liabilities of franchisor and franchisee is the issue to which this article now turns.

### IV FRANCHISOR AND FRANCHISEE LIABILITY FOR CONTRAVENTIONS OF THE FW ACT

As noted in the introduction to this article, the notorious case involving the 7-Eleven franchise, and the various scandals that followed, have revealed that franchisees across a range of brands have routinely committed ‘serious and systematic contraventions of the most basic of the employees’ workplace rights’.\(^{81}\) While there have been some notable exceptions,\(^{82}\) in virtually all the underpayment cases decided thus far, the relevant franchisor was either not named as a party to the civil remedy proceedings, or there has been an absence of evidence regarding the part played by the franchisor (if any).\(^{83}\) As a result, there has so far been limited judicial consideration of the role and responsibilities of the franchisor in the context of underpayment matters.\(^{84}\)

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\(^{77}\) ‘IR Compliance Eats into Domino’s Profits’, Workplace Express, 21 February 2019.

\(^{78}\) Franchise Council of Australia, Submission No 88 to Senate Standing Committee on Economics Inquiry into Unlawful Underpayment of Employees’ Remuneration (9 March 2020) 2.

\(^{79}\) For example, a recent application to vary the Fast Food Award 2010 to allow for ‘flexible part-time’ arrangements, amongst other changes, is currently being contested before the Fair Work Commission. David Marin-Guzman, ‘McDonald’s Rebuffed Over Fast Food Flexibility Deal’, Australian Financial Review, 6 May 2020.

\(^{80}\) Application by Xzavier Kelly, Shop, Distributive and Allied Employees Association re McDonald’s Australia Enterprise Agreement 2013 [2019] FWCA 8563 [72].


\(^{82}\) But see Fair Work Ombudsman v Yogurberry World Square [2016] FCA 1290 (2 November 2016) (‘Yogurberry’) discussed below. The FWO has recently initiated proceedings against the Chatime franchisor, but this appears to relate to contraventions that occurred in franchisor-owned units (rather than in workplaces owned and operated by separate franchisee employers). See Fair Work Ombudsman, ‘Chatime Franchisor Faces Court’, Media Release, 18 December 2019.

\(^{83}\) See, eg, Fair Work Ombudsman v Kingsford Carwash Pty Ltd (No 2) [2012] FMCA 1210 (18 December 2012); Fair Work Ombudsman v QHA Foods Pty Ltd & Ors [2019] FCA 3120 (1 November 2019).

\(^{84}\) While this situation has been expected to change with the passage of the extended liability provisions introduced under the Fair Work Amendment (Protecting Vulnerable Workers) Act 2017 (Cth), there is yet to be a finalised case against a franchisor for breaches committed by their franchisees (see section [9.2.3(b)] below).
The fact that the franchisor has not been formally named as a party has not prevented many of the franchisee employers seeking to justify or defend their wrongdoing by reference to the actions taken by head office. For example, in the 2018 decision of *Fair Work Ombudsman v Skyter Trade Pty Ltd*, a Pizza Hut franchisee (Skyter Trade Pty Ltd), and its sole director and shareholder (Dong Zhao), were found to have misclassified a delivery driver as an independent contractor, which amounted to a contravention of the sham contracting provisions of the FW Act. More specifically, Mr Zhao submitted that he had borrowed a significant amount to invest in the franchise in reliance on a Profit & Loss Projection prepared by the franchisor. The loan repayments proved to be a ‘major financial burden’, particularly when the profitability of the business plummeted as a result of a rival Domino’s Pizza outlet opening in the area and the franchisor’s decision to force all of its outlets to sell cheap pizzas below cost. In its submission, the FWO argued that sham contracting and other types of underpayment contraventions were relatively common in this particular franchise network, and the penalties should reflect the need for general deterrence in the ‘Pizza Hut franchise industry’. While Jarrett J did not make any direct ruling on these submissions, his Honour did note that the franchisor had provided the franchisee with training and information as part of the induction process, including explicit advice that franchisees should avoid engaging contractors. Given this, Jarrett J ultimately found that the franchisee’s conduct was ‘deliberate’.

A number of the same arguments were run in cases relating to the 7-Eleven network, which frequently involved not only significant underpayments, but serious and deliberate breaches of the relevant record-keeping obligations. More specifically, data entered by the franchisees onto the central payroll system administered by 7-Eleven Stores Pty Ltd (‘7-Eleven Stores’) was fabricated so as to conceal the underpayments from head office. These elaborate record-keeping systems also appeared to successfully hide the true extent of the wrongdoing from the FWO. Notwithstanding the gravity of these breaches, franchisees caught up in these cases sought to run the argument that it was the franchisor’s business model which had perpetuated the contraventions, at least in part.

85 [2018] FCCA 1483 (8 June 2018) (‘Skyter Trade’).
86 Ibid [63].
87 Ibid, at [64]. See also *Virk Pty Ltd (in liq) v YUM! Restaurants Australia Pty Ltd* [2017] FCAFC 190 (28 November 2017).
89 Skyter Trade [2018] FCCA 1483 at [54].
90 According to latest reports, since 2009, the FWO has commenced 11 civil remedy proceedings against 7-Eleven franchisees. In eight of these matters, total penalties have been in excess of $100,000. See Migrant Workers’ Taskforce Report (n ) 44.
91 See, eg, *JS Top* [2017] FCCA 1689 at [40]. See also *Fair Work Ombudsman v Amritsaria Four Pty Ltd* [2016] FCCA 968 (29 April 2016) (‘Amritsaria’); *Mai* [2016] FCCA 1481; *Fair Work Ombudsman v Hiyi Pty Ltd & Ors* [2016] FCCA 1634 (‘Hiyi’). But see *Fair Work Ombudsman v Viplus Pty Ltd* [2018] FCCA 741 (29 March 2018) (‘Viplus’), where it was found that ‘the respondents did not seek to cover up their underpayments and other non-compliance, nor did they falsify any records’: at [75].
93 See, eg, *Viplus* [2018] FCCA 741; *Mai* [2016] FCCA 1481. Cf *Fair Work Ombudsman v S & A Enterprises (Qld) Pty Ltd* [2017] FCCA 3332 (11 December 2017); *JS Top* [2017] FCCA 1689. In this latter case, there was no submission that the franchisee’s ‘failure to pay appropriate wages was driven by poor cash flow or an inability to meet the expenses of the business’: at [50].
For example, in *Fair Work Ombudsman v Hyi*, the franchisee, along with key directors, argued that the 7-Eleven franchising model which existed at the time of the contraventions (i.e. an obligation to pay 57 percent of gross profit to the franchisor) was ‘extremely detrimental to them’ and ‘made it very difficult … to pay [the] employees the appropriate minimum wage entitlements.’ While the Court was willing to accept that the original profit-sharing arrangements ‘placed significant restrictions on the capacity of the respondents to generate an income from the operation of the franchise’, the judge ultimately held that little weight would be attached to this factor. The judge went on to observe that the franchisees had voluntarily entered into the franchise agreement and they should have performed due diligence on the profitability (or otherwise) of the business before purchasing the franchise. Ultimately, Jones J was at pains to point out that the terms of the franchising agreement did not exempt the franchisees from their legal obligations as employers under the FW Act.

Overall, a survey of underpayment matters relating to franchise networks over the past decade or more has revealed a broad judicial consensus that the franchisor was not to blame for the contraventions committed by its franchisees. Rather, in many cases, the court appeared to be willing to accept that, by providing franchisees with initial and ongoing training regarding workplace relations obligations, the franchisor had fulfilled its ethical, if not legal, obligations. By way of illustration, in *Fair Work Ombudsman v Bosen Pty Ltd* – a separate case involving a 7-Eleven franchisee – the judge noted that:

This was a deliberate and calculated campaign to pay the Employees less than what they were legally entitled to and to obtain free labour and therefore a competitive advantage in the marketplace. They were not breaches brought about by naïve ignorance. The Defendants’ ignored training and regular updates and must have been wilfully blind to the well-known legal obligations of every small business operator.

The general pattern emerging from these cases is not especially surprising given that it is the direct employer (i.e. the franchisee) which is positioned as the primary wrongdoer for contraventions of civil remedy provisions of the FW Act. To a large extent, this statutory framework reflects traditional presumptions about employment arrangements – that is, primary responsibility and liability for contraventions of employment standards regulation is ordinarily ascribed to the relevant employer at common law.

However, an employer-orientated enforcement strategy has also proved problematic in the franchising context. The FWO’s inquiry into the 7-Eleven network illustrated many of these issues. For example, the regulator found that while 7-Eleven Stores ostensibly promoted franchisee

94 [2016] FCCA 1634. A somewhat similar argument was run in *Amritsaria* [2016] FCCA 968.
95 *Hyi* [2016] FCCA 1634 at [37].
96 Ibid, at [24].
97 Ibid, at [38].
98 Ibid.
99 Ibid, at [39].
100 JS Top [2017] FCCA 1689 at [42]; Viplus [2018] FCCA 741 at [53]; Mai [2016] FCCA 1481 at [105]–[106]. Cf *Fair Work Ombudsman v G & Z United Pty Ltd* [2019] FCCA 465. In this case, Baird J observed that there was a need not just for general deterrence in relation to employers that engage award-reliant workers, but a ‘message…should also bite on unsupportive franchisors, and their satellite organisations, and those entities that benefit from opportunistically terminating franchises’: at [112].
102 Ibid, at [39].
compliance with workplace standards, it ‘did not adequately detect or address deliberate non-compliance and as a consequence compounded it’. \(^{104}\) James, the former head of the FWO, further explained that:

Taking up complaints with individual outlets, often finding insufficient funds to pay the workers and sometimes, franchisees themselves under significant financial pressure was not addressing the root cause of the problem. The underlying problem invariably extended beyond individual outlets.\(^{105}\)

In light of these observations, and a growing consensus that franchisors had been let off too lightly, there has been an increasing focus on ways to extend liability beyond the franchisee employer.

**A Accessorial Liability under s 550 of the FW Act**

Historically, the principal mechanism by which the FWO, and others, have sought to pursue third party individuals or entities is via the ‘accessorial liability’ provisions of the FW Act. More specifically, under s 550, an accessory will be taken to be ‘involved in’ a contravention committed by another – and held liable under a civil remedy provision\(^{106}\) – if the person has:

a) aided, abetted, counselled or procured the contravention;

b) induced the contravention (whether by threats or promises or otherwise);

c) been in any way, by act or omission, ‘knowingly concerned’ in the contravention; or

d) conspired with others to effect the contravention.\(^{107}\)

These provisions have proven particularly valuable where the direct employer is insolvent or no longer in existence and the FWO has routinely used the accessorial liability provisions to bring enforcement proceedings against the individual directors of failed companies.\(^{108}\) On occasion, the FWO has also brought enforcement proceedings against advisors, such as HR managers or accountants, under the auspices of the accessorial liability provisions.\(^{109}\) However, it has historically been more difficult to ascribe liability to third party entities, such as host companies or principal contractors, because the courts have tended to apply a high bar when it comes to satisfying the ‘requisite knowledge’ requirement under s 550(2)(c) of the FW Act.\(^{110}\) In particular, the courts have emphasised that it is necessary to show that the accessory had ‘actual knowledge’ of the essential elements of the contravention.\(^{111}\) While this encompasses ‘wilful blindness,’ it does not include ‘recklessness or negligence.’\(^{112}\) Furthermore, constructive knowledge is not sufficient.\(^{113}\) The way that the requisite knowledge requirement has been interpreted and applied by the courts may make it difficult to pin liability on the alleged accessory, especially in franchise

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\(^{104}\) 7-Eleven Inquiry (n 84) 4.

\(^{105}\) Natalie James, ‘Reasonable Steps: The Regulator’s Perspective’, Address to the Franchise Management Forum hosted by the Franchise Advisory Centre, Brisbane, 13 June 2018, 1.

\(^{106}\) Under s 545 of the FW Act, the courts have a broad power to ‘make any order the court considers appropriate’ where it is satisfied that a person has contravened a civil remedy provision.

\(^{107}\) See Appendix for full extract of this provision.

\(^{108}\) This is essentially what occurred in the case *Fair Work Ombudsman v Haider Pty Ltd & Anor* [2015] FCCA 2113.


\(^{111}\) *Yorke v Lucas* (1985) 158 CLR 661.

\(^{112}\) *Fair Work Ombudsman v Hu (No 2)* [2018] FCA 1034.

\(^{113}\) *Giorgianni v The Queen* (1985) 156 CLR 473.
networks, where the franchisor frequently seeks to take a ‘hands off’ approach to employment-related matters (on the basis that these are the sole purview of the franchisee).114

In some rare instances, however, the accessorrial liability provisions have been successfully used to bring proceedings against the relevant franchisor (or the directors of the franchisor).115 The most well-known case in this regard is the 2016 Federal Court decision in *Fair Work Ombudsman v Yogurberry World Square*.116 In particular, the Franchise Council of Australia — which fiercely opposed introduction of the *Fair Work Amendment (Protecting Vulnerable Workers) Act 2017* (Cth) (‘PVW Act’) — sought to contend that the *Yogurberry* decision confirmed that s 550 was ‘adequate’117 in addressing underpayment issues in franchise networks and there was no need to extend franchisor liability under the proposed reforms. However, the circumstances of the *Yogurberry* case are somewhat exceptional. First, unlike most arms-length franchise relationships, the franchisee employer and the head franchisor were part of a complex group of companies controlled by various members of the same family.118 Second, the franchisor decided not to contest its liability under s 550 and therefore parties did not make submissions directed at this point. Combined, these features of the case mean the decision is of limited assistance in delineating the precise scope and application of s 550 in the context of franchise networks.119

**B Franchisor Liability under s 558B of the FW Act**

In any event, attribution of liability in franchise networks is now expressly addressed in the s 558B, which was introduced under the PVW Act. As the title of the legislation suggests, the PVW Act is consciously designed to curb ‘deliberate and systematic exploitation of workers’120 in Australia. Indeed, in addition to s 558B which is the focus of this section, the PVW Act also introduced higher maximum penalties for ‘serious contraventions’ of prescribed workplace laws and shifted the onus of proof to employers where there has been a failure to keep or maintain employment records or issue payslips. These reforms, amongst others, were variously aimed at strengthening the compliance and enforcement framework under the FW Act.121


115 In *United Voice v MDBR123 Pty Ltd* [2014] FCA 1344 and *United Voice v MDBR123 Pty Ltd (No 2)* [2015] FCA 76, the Federal Court found that a director of the head franchisor was liable under section 550 for contraventions of the adverse action provisions by one of its franchisees.


118 See also *Fair Work Ombudsman v Hasegawa & Ye International Pty Ltd & Anor* [2019] FCCA 142 and *Fair Work Ombudsman v Heiwa International Pty Ltd & Anor* [2019] FCCA 142.

119 For more detailed discussion of s 550, see Tess Hardy, ‘Big Brands, Big Responsibilities? An Examination of Franchisor Accountability for Employment Contraventions in the United States, Canada, and Australia’ (2019) 40 *Comparative Labor Law & Policy Journal* 285; Ranieri (n 114).

120 See generally Michael Rawling and Eugene Schofield-Georgeson, ‘Industrial Legislation in Australia in 2017’ (2018) 60(3) *Journal of Industrial Relations* 378. The FWO has recently initiated litigation against a former *Han’s Cafe* franchisee under the ‘serious contraventions’ provisions. The franchisee had previously been found by a court to have underpaid vulnerable workers. Notwithstanding this compliance history, the proceedings do not appear to name the franchisor as a respondent. Fair Work Ombudsman, ‘Perth Franchisee Faces Tenfold Increase in Max Penalties’, Media Release, 7 January 2020.
In the franchising context, the most significant change brought about by the PVW Act was the addition of an express provision which holds franchisors liable for the employment-related misdeeds of their franchisees. Broadly-speaking, s 558B makes a ‘responsible franchisor entity’ liable for prescribed contraventions122 committed by a ‘franchisee entity’ in circumstances where they either knew, or should reasonably have been aware of the contraventions, and could reasonably have taken action to prevent such contraventions from occurring.123

This section will now examine three essential questions raised by this provision:

a) Who falls within the definition of a ‘responsible franchisor entity’ and ‘franchisee entity’?
b) What level of knowledge is required to be proved on the part of the responsible franchisor entity?
c) When will the responsible franchisor entity be able to avoid liability by proving that it has taken ‘reasonable steps’ to prevent the relevant contravention?

Before discussing these questions in more detail, it is important to point out that these provisions are novel, and as at the time of writing, there has been no judicial consideration of their scope and application. While the FWO appears to have been actively considering these provisions with respect to certain franchise networks, such as United Petroleum124 and Subway125, it appears that the regulator had not yet gathered sufficient evidence or courage to commence proceedings under s 558B.

1 Who falls within the definition of a ‘responsible franchisor entity’ and ‘franchisee entity’?

As noted above, in order to trigger liability under these new provisions, it first needs to be shown that the civil remedy proceeding is being brought against a ‘responsible franchisor entity’ in relation to a contravention committed by a ‘franchisee entity’.126 Section 558A defines each of these concepts as follows:

(1) A person is a franchisee entity of a franchise if:
(a) the person is a franchisee (including a subfranchisee) in relation to the franchise; and
(b) the business conducted by the person under the franchise is substantially or materially associated with intellectual property relating to the franchise.

(2) A person is a responsible franchisor entity for a franchisee entity of a franchise if:
(a) the person is a franchisor (including a subfranchisor) in relation to the franchise; and

122 FW Act, s 558B(7).
123 Explanatory Memorandum (n 120) [54].
124 Instead, the FWO has initiated proceedings against United Petroleum Pty Ltd for failure to comply with a statutory Notice to Produce by providing the regulator with the requested records and documents. See Fair Work Ombudsman, ‘United Petroleum Faces Court’, Media Release, 27 September 2019.
126 However, under this Division, it is also clear that liability may be established against a franchisor under s 558B, even where the franchisee entity which is responsible for the contraventions has not been the subject of civil remedy proceedings or court orders: FW Act, s 558B(6).
(b) the person has a significant degree of influence or control over the franchisee entity’s affairs.

Somewhat confusingly, the Explanatory Memorandum to the PVW Bill suggests that the definition of ‘franchisee entity’ is generally consistent with the approach taken under the Franchising Code given that the term ‘only applies to franchisees whose business is substantially or materially associated with the “intellectual property relating to the franchise”’. The Explanatory Memorandum further notes that the definition of ‘franchisee entity’ adopted in the PVW Act ‘effectively limits the scope of the new provisions to franchisor/franchisee businesses which are appropriately associated by branding – and distinguishes it from other forms of arrangements – for example, distribution agreements or joint venture marketing.’

However, in light of the way in which key terms, such as ‘franchise agreement’, ‘franchisee’ and ‘franchisor’ are defined under the Franchising Code, it is arguable that the statutory definition of ‘franchisee entity’ departs from more well-established definitions of these key concepts. For example, the definition of ‘franchisee entity’ under s 558A does not require the franchisee to prove that they have paid an ongoing fee for operating the franchise (which may exclude commission agency arrangements). It also draws no distinction between ordinary business format franchises and fuel retail franchises (which is not the case in the competition and consumer sphere).

Another critical conceptual difference between the PVW Act and the Franchising Code is the way that ‘responsible franchisor entity’ has been defined. Under s 558A(2)(b), it must be proved that the putative franchisor ‘has a significant degree of influence or control over the franchisee entity’s affairs’. Notably, the term ‘affairs’ is not expressly defined in the statute. However, the Explanatory Memorandum states that the term is intended to be read broadly, and is not limited to particular aspects of a franchisee’s operations. Rather, it is intended to include involvement in the franchisee’s financial, operational and corporate affairs. Business groups lobbied hard to narrow this definition so that it only applied to franchisors that had control over ‘workplace relations matters’ relating to the franchisee. But ultimately the original, more expansive, definition endured. While the provisions explicitly capture ‘subfranchisors’ and ‘officers’ of the franchisor, either via the definition of ‘responsible franchisor entity’ or within s 558B itself, it is not clear how, and to what extent, the provisions may apply to a ‘master franchisor’ or an ‘associate’ of the franchisor.

2 What knowledge is required?

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127 The Explanatory Memorandum further states that this association ‘may be evidenced by use of trademarks, advertising or commercial symbols that are owned, used, licensed or specified by the franchisor or their associate.’ Explanatory Memorandum (n 120) [50].
128 Explanatory Memorandum (n 120) [50].
130 The Explanatory Memorandum notes that the definition of ‘responsible franchisor entity’ relies on the ‘ordinary meaning of the term “franchisor”, but clarifies that the term includes a subfranchisor (however described.)’ Explanatory Memorandum (n 120) [51].
131 FW Act, s 558A(2)(b).
132 Explanatory Memorandum (n 120) at [53].
133 Franchise Council of Australia, Supplementary Submission in Relation to the Proposed Wording of the Amendments to the Fair Work Act to Extend Liability to Franchisors and Parent Companies in Certain Situations, 2017.
Section 558B(1) of the FW Act is as follows:

A person contravenes this subsection if:

(a) an employer who is a franchisee entity of a franchise contravenes a civil remedy provision referred to in subsection (7);\(^{134}\) and

(b) the person is a responsible franchisor entity for the franchisee entity; and

(c) the contravention by the franchisee entity occurs in the franchisee entity’s capacity as a franchisee entity;\(^{135}\) and

(d) either:

(i) the responsible franchisor entity or an officer (within the meaning of the Corporations Act 2001) of the responsible franchisor entity knew or could reasonably be expected to have known that the contravention by the franchisee entity would occur; or

(ii) at the time of the contravention by the franchisee entity, the responsible franchisor entity or an officer (within the meaning of the Corporations Act 2001) of the responsible franchisor entity knew or could reasonably be expected to have known that a contravention by the franchisee entity of the same or a similar character was likely to occur.

Note: This subsection is a civil remedy provision (see this Part).

In relation to the knowledge requirement imposed under s 558B, it is clear from subsection (d), that the court may take into account not only what the responsible franchisor entity (or one of its officers) ‘knew’ about the contravention of the franchisee entity, but what it (or the officer) ‘could reasonably be expected to have known’. In short, the provisions capture not just actual knowledge (which is the relevant touchstone under s 550), but constructive knowledge (which presents a clear extension of the existing provisions). In addition, s 558B(1)(d) expands the knowledge requirement in a second important way – that is, by encompassing not just knowledge of the precise contraventions which have been committed by the franchisee entity, but by including knowledge of contraventions of a ‘same or similar character’.\(^{136}\)

The Explanatory Memorandum notes that ‘mere suspicion’ of contraventions will not be enough to satisfy s 558B(1)(d). Rather, ‘there must objectively be reasonable grounds to hold the belief’,\(^{137}\) taking into account the responsible franchisor entity’s knowledge, experience and acumen.\(^{138}\)

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\(^{134}\) Liability under s 558B(1) is only triggered in relation to certain, prescribed contraventions of the FW Act (and does not apply to all civil remedy provisions available under the Act). The Appendix sets out s 558B(7) in full – but generally-speaking, the prescribed contraventions are those that frequently arise in underpayment matters (e.g. breach of a term of a modern award, failure to comply with employer obligations in relation to employee records, etc).

\(^{135}\) This subsection is intended to clarify that contraventions of the FW Act by a franchisee entity occurring as part of the conduct of another external business will not be caught by s 558B. Explanatory Memorandum (n 120) [56].

\(^{136}\) The Explanatory Memorandum notes that the phrase ‘contraventions of a same or similar character’ is not defined and so has its ordinary meaning. However, it further explains that a contravention will be ‘of the same or a similar character’ if the contravention is legally the same or similar in character (e.g. breaches of the terms of an award or enterprise agreement) and there is some factual or temporal nexus or connection between the various contraventions in order to establish a series. Explanatory Memorandum (n 120) [62].

\(^{137}\) Explanatory Memorandum (n 120) [58].

\(^{138}\) Ibid, [60].
By prescribing the knowledge requirement in this way, s 558B(1)(d) makes it far easier to satisfy the evidentiary hurdle than is presently the case under s 550. In particular, there remains a level of debate about what must be proved to show that the accessory was ‘knowingly concerned’ in a contravention for the purposes of s 550. The knowledge threshold under s 550 can be especially difficult to satisfy where knowledge of essential elements of the contravention is dispersed between a number of different individuals within a third party entity. However, the Explanatory Memorandum makes clear that the test under s 558B(d):

looks to what the responsible franchisor entity knew, or could reasonably be expected to have known, about the general likelihood of contraventions affecting employee entitlements within its franchise network at the time the actual contravention occurred. There is no need to prove that the head office of a potentially large franchise network knew the exact details of contraventions being committed by their franchisees. It requires a general assessment of what was known, or could reasonably be expected to have been known, about levels of compliance with the relevant requirements within the franchise network.140

3 What constitutes reasonable steps?

Sections 558B(3)-(5) of the FW Act essentially set out a statutory defence, which would allow a ‘responsible franchisor entity’ (and ‘holding companies’)141 to avoid liability that would otherwise be imposed under the substantive liability provisions. More specifically, these sections (as they apply to franchises) are as follows

(3) A person does not contravene subsection (1)…if, as at the time of the contravention referred to in paragraph (1)(a)…, the person had taken reasonable steps to prevent a contravention by the franchisee entity or subsidiary of the same or a similar character.

(4) For the purposes of subsection (3), in determining whether a person took reasonable steps to prevent a contravention by a franchisee entity…(the contravening employer) of the same or a similar character, a court may have regard to all relevant matters, including the following:

(a) the size and resources of the franchise…;
(b) the extent to which the person had the ability to influence or control the contravening employer’s conduct in relation to the contravention referred to in paragraph (1)(a)… or a contravention of the same or a similar character;
(c) any action the person took directed towards ensuring that the contravening employer had a reasonable knowledge and understanding of the requirements under the applicable provisions referred to in subsection (7);
(d) the person’s arrangements (if any) for assessing the contravening employer’s compliance with the applicable provisions referred to in subsection (7);
(e) the person’s arrangements (if any) for receiving and addressing possible complaints about alleged underpayments or other alleged contraventions of this Act within [the franchise];

139 One of the most contentious issues in the context of underpayment matters is whether an accessory needs to know about the existence of the award and its terms: Potter v Fair Work Ombudsman [0214] FCA 187; cf Fair Work Ombudsman v Hu (No 2) [2018] FCA 1034.
140 Explanatory Memorandum (n 120) at [61].
141 While the focus of this discussion is on the application of these statutory provisions to franchise networks, it is important to note that a mirror set of provisions also apply in relation to holding companies and their subsidiaries. See FW Act, s 558B(2).
(f) the extent to which the person’s arrangements (whether legal or otherwise) with the contravening employer encourage or require the contravening employer to comply with this Act or any other workplace law.

(5) Subsection (4) does not limit subsection (3).

The non-exhaustive list of ‘reasonable steps’ set out in s 558(B)(4) is framed in such a way so as to avoid a ‘one size fits all’ approach – that is, to make it clear that franchisors are not required or expected to take ‘unreasonable or impractical’ measures. Rather, this provision is designed to allow franchisors ‘flexibility in deciding which steps to take to support compliance within their business networks.’ More specifically, the Explanatory Memorandum notes that ‘what constitutes “reasonable steps” for a multi-national business will be different for a small franchisor with only several franchisees.’

The Explanatory Memorandum further observes that the FWO website has ideas and resources about what steps a franchisor might consider taking, in addition to any existing arrangements, to help franchisees meet their legal obligations in this space. Suggestions include:

a) ensuring that the franchise agreement require franchisees to comply with workplace laws;

b) providing franchisees with a copy of the FWO’s free Fair Work Handbook;

c) encouraging franchisees to cooperate with any audits by the FWO;

d) establishing a contact or phone number for employees to report any potential underpayment to the business;

e) auditing of franchisees in the network.

A franchisor who seeks to rely on the statutory defence set out in s 558B(3) bears the evidentiary onus in proving that they have taken such steps as ought reasonably be expected or warranted in the circumstances. This underlines another point of divergence between s 550 and s 558B in that the former invites the court to focus on the active involvement of the franchisor, whereas the latter provision directs the court’s attention towards omissions or a failure to act.

Before engaging in discussion of other relevant matters relating to the operation of s 558B, it is important to note, in passing, that the statutory defence is only available where the franchisor has taken ‘reasonable steps’ to prevent a contravention by the franchisee entity. This means that a franchisor who may have taken steps to quickly remedy or rectify a contravention after it is brought to light cannot necessarily rely on this provision to avoid liability. In practical terms, however, this is unlikely to be the source of significant concern or contest for two reasons. First, if the contravention has only just come to the attention of the franchisor, then it will be more difficult to meet the knowledge test under s 558B(1)(d) (even when knowledge is assessed on the basis of

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142 Explanatory Memorandum (n 120) [65].
143 Ibid, [68].
144 Ibid, [65].
145 Ibid.
146 Ibid, [66].
147 Ibid, [67].
148 If a franchisor has rectified an underpayment that has arisen as a result of the franchisee’s contravention, the franchisor has a right to recover the amount from the franchisee entity responsible for the underpayment: FW Act, s 558C. However, there is no statutory provision which allows the franchisor to recover pecuniary penalties from the franchisee (albeit the franchisor may effectively seek to do so under an indemnity with the franchisee).
what the franchisor should reasonably be expected to have known). Second, in assessing whether the franchisor has taken ‘reasonable steps’, the court is expressly directed to consider any arrangements the person has for addressing possible complaints about alleged underpayments (or other contraventions).

It is clear that Parliament intended for s 558B to supplement, rather than substitute, the existing accessorial liability provisions. However, the complex interaction between these two liability provisions presents some dilemmas for franchisors seeking to manage or mitigate risks arising under the FW Act. On the one hand, a franchisor may be reluctant to become too engaged in setting or supervising employment-related matters for fear that doing so will mean that it will be easier to prove that the franchisor had actual knowledge of any contraventions that ensue (and will be held liable under s 550 as a consequence). On the other hand, adopting a proactive approach towards these same matters may allow the franchisor to invoke the statutory defence and save them from liability under s 558B. At this early stage, it is not yet apparent how the FWO, and the courts for that matter, will resolve the potential conflict between these provisions.

Publicly, the FWO has stated that it hopes the new laws ‘will help to change the attitude of some head franchisors about the investment required’ to ensure compliance. In contrast, the Franchise Council of Australia has previously argued that holding franchisors accountable for workplace contraventions committed by franchisees represents ‘regulatory over-reach’, which is both unnecessary and unhelpful. Others have similarly asserted that a more appropriate or effective response to systemic worker exploitation within franchises would be to leverage the ethical, moral or reputational concerns of franchisors. Indeed, over the past decade, the FWO has sought to do just that – by undertaking a range of activities in the franchising space, including voluntary programs, compliance audits, in-depth inquiries, and compliance partnerships. While these various initiatives have allowed the FWO to save resources and shift some of the enforcement burden to franchisors, it raises a host of other problems, not least of which is a perceived or actual lack of transparency and accountability. Moreover, there is evidence to suggest that franchisors can be reluctant to adopt voluntary compliance mechanisms, particularly where consumer

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149 Natalie James, ‘Fair Work Ombudsman Address to the Franchise Council of Australia NSW Luncheon’, speech delivered at the Franchise Council Australia NSW Luncheon, Sydney, 1 September 2016, at 10.


151 Frazer and Roussety (n 117).


153 The National Franchise Program – which commenced in 2012 as a pilot and concluded in 2014 – involved the FWO working closely with franchisors to identify and rectify issues of employer noncompliance throughout their respective franchise networks. For further discussion of this program, see Tess Hardy, ‘Brandishing the Brand—Enhancing Employer Compliance through the Regulatory Enrolment of Franchisors’ (Paper presented at the Labour Law Research Network Conference, Amsterdam, 25-27 June 2015).


155 ‘7-Eleven Inquiry’ (n 92). See also Hardy (n 92).

156 See, eg, Proactive Compliance Deed between the Commonwealth of Australia (as represented by the Office of the Fair Work Ombudsman) and 7-Eleven Stores Pty Ltd (6 December 2016). For further discussion of proactive compliance deeds, see Tess Hardy and John Howe, ‘Chain Reaction: A Strategic Approach to Addressing Employment Noncompliance in Complex Supply Chains’ (2015) 57(4) Journal of Industrial Relations 563.

pressure, regulatory scrutiny, and/or the credible threat of liability is absent. The outgoing head of the FWO pointedly observed that franchisors can be reluctant to proactively engage with the FWO before issues are uncovered, either by the FWO or through the media. Reputational leverage works as a “push” factor for franchisors to act, but has had limited effect as a general deterrence measure to encourage other franchisors to take reasonable steps to detect non-compliance and support franchisees to be compliant.

This tends to underline the importance of having sanctions available in order to coerce or compel franchisors to take an active interest, and enhanced role, in ensuring that franchisees throughout their network are complying with workplace laws.

V CONCLUSION

This article has surveyed some of the most pressing and contentious issues which apply to franchise networks in the context of the FW Act, including: the possible employment status of franchisees; the particular (and somewhat peculiar) ways in which collective bargaining operates in relation to franchise systems; and the various statutory mechanisms for attributing liability to the franchisor. While there has been significant regulatory reform in this area, the full effects of these changes on the compliance behaviour of franchisees, franchisors and other key stakeholders are yet to be fully considered or explored. Most notably, we are still waiting for a test case on the extended liability provisions introduced into the FW Act in 2017. However, the FWO has expressly identified that franchisors are a ‘strategic priority’ for 2019-20. The regulator also has a number of active inquiries into certain franchise systems, such as Subway. Combined, this is likely to mean that we may not be waiting much longer for judicial consideration of these novel provisions.

In the meantime, further change for the franchising sector is on the horizon. The interagency Franchising Taskforce – which was established in the wake of the Parliamentary Inquiry into the Franchising Code – is nearing completion. The Attorney-General’s Department is part way through an extensive consultation on the compliance and enforcement framework, albeit this consultation has been ‘paused’ due to the disruption caused by COVID-19. At the state level, the Andrews Labor Government has recently introduced a Wage Theft Bill 2020 into the Victorian Parliament, which makes the ‘dishonest’ withholding of wages a criminal offence. Most notably, the Bill provides that a prosecution can be brought against third parties, such as head franchisors,

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158 Similar in many ways to the resistance displayed by 7-Eleven Stores, following an inquiry into underpayment allegations in the United Petroleum network of franchises and commission agents, the FWO approached the head office of United Petroleum on at least two occasions to enter into a formal compliance partnership. At this stage, no such partnership has eventuated. See Fair Work Ombudsman, United Petroleum Retail Fuel Outlets: Summary of Compliance Activity Outcomes (Final Report, 2017). The FWO has since commenced proceedings against United Petroleum (see (n 124)).


on the basis that they were ‘complicit’ in the offending.\textsuperscript{163} While this article has documented some of the sweeping reforms, and critical decisions, in this area of law in the past five years, it is clear that the regulation of work in franchises is likely to remain in a state of flux for some time to come.

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Author/s:
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Title:
Working for the Brand: The Regulation of Employment in Franchise Systems in Australia

Date:
2020

Citation:

Persistent Link:
http://hdl.handle.net/11343/241887

File Description:
Accepted version