

ADMINISTRATIVE LAW PARALLELS WITH PRIVATE LAW CONCEPTS: UNCONSCIONABLE CONDUCT, GOOD FAITH AND FAIRNESS IN FRANCHISE RELATIONSHIPS

ABSTRACT

In 21st century business format franchising, the search for solutions has taken the legislature and the courts into the areas of unconscionable conduct and good faith. To date these concepts have lacked the ability to curtail franchisor opportunism in exercising contract-granted discretions. Similar difficulties afflict administrative law approaches to good faith, lawfulness and rationality, errors of law and fact finding, and fairness — criteria against which contract-based discretions have been appropriately exercised by franchisors. We examine franchising cases against the administrative law approaches, acknowledging doctrinal differences (as well as similarities) and conclude that a common body of principle underlies both areas. This allows a fresh approach to interpreting the exercise of franchisor's discretions.

I INTRODUCTION

Franchising is a significant aspect of Australian commercial life.¹ Opportunities are marketed to franchisees as if they were consumer products, but are unaccompanied by statutory warranties. Once a franchise agreement is signed and the seven-day statutory cooling off period has elapsed, the arrangement is treated as a commercial one.

In Australia, the misleading and deceptive conduct legislation provides some protection for franchisees *ex ante* from exploitative conduct by franchisors. However, the reality of relationships between franchisors and their franchisees, manifested by the sometimes strong disconnect between what was sold in an environment akin

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¹ See Michael T Shaper and Jenny Buchan, 'Franchising in Australia: A History' (2014) 12(4) *International Journal of Franchising Law* 3.

to that of a consumer sale (and the actual relationship) has led to calls for better protection for franchisees and their businesses *ex post*. The 1998 expansion of the unconscionable conduct provisions of the then *Trade Practices Act 1974* (Cth) (*'TPA'*), by the addition of s 51AC, may have been able to rebalance the relationship. But, as we will see, it has not been done. The search for tools to fundamentally rebalance the power dynamic between a franchisor and its franchisees continues.

Power imbalance has long been the Achilles heel of the franchise model. As a structural weakness it has the ability to make the model less attractive to franchisee investors. It remains problematic for the following reasons. The ability to draft the standard form contract enables franchisors to cast their obligations in discretionary terms, and the franchisees' role in terms of predominantly non-negotiated, iron-clad obligations. Franchisees accept that the blatantly 'unfair' aspects of their franchise agreements are necessary to enable the franchisor to bring rogue franchisees into line and thus to protect the brand, but arguably they are more often used to force franchisees to 'behave'. Richard Hooley writes of controlling contractual discretions.² He acknowledges that contracts may be incomplete and that 'an unfettered contractual discretion may not properly reflect the intention of the parties at the time of contracting'.³ He also, pertinently, accepts that 'in a long-term contract that depends on co-operation between the parties, an unfettered discretion afforded to one party may undermine the economic potential of the contract'.⁴ Intractable problems that can undermine the economic potential of the contract for the franchisee arise out of the contract-entrenched power imbalance between a franchisor and a franchisee.

There are difficulties for the law in attempting to balance the franchisor-franchisee relationship in order to mitigate the effects of asymmetries.⁵ These are partly a consequence of seeking to impose a traditional commercial contract paradigm, based on negotiation followed by mutual consent, on a 'necessarily and intentionally incomplete'⁶ agreement. However, regulators in many jurisdictions have nonetheless attempted to impose balance on the relationship.⁷ This article examines two responses. They are unconscionable conduct under the *Competition and Consumer Act 2010* (Cth) (*'CCA'*), and the much mooted good faith concept.

² Richard Hooley, 'Controlling Contractual Discretion' (2013) 72 *Cambridge Law Journal* 65.

³ *Ibid* 67.

⁴ *Ibid* 68. See also H Collins, 'Discretionary Powers in Contracts' in David Campbell, Hugh Collins and John Wightman (eds) *Implicit Dimensions of Contracts, Discrete, Relational and Network Contracts* (Oxford, 2003) 231.

⁵ Jenny Buchan, 'Ex Ante Information and Ex Post Reality for Franchisees: the Case of Franchisor Failure' (2008) 36 *Australian Business Law Review* 407.

⁶ Gillian K Hadfield, 'Problematic Relations: Franchising and the Law of Incomplete Contracts' (1990) 42 *Stanford Law Review* 927.

⁷ See Elizabeth Crawford Spencer, *The Regulation of Franchising in the New Global Economy* (Edward Elgar 2011) 118–19. Table 4.1 identifies examples of legislation designed to variously 'guarantee non-discriminatory treatment for all franchisees of the same franchisor' (Mexico), remedying information disparity and power imbalance (USA).

Australia's Commonwealth consumer protection legislation was amended in 1998 in statutory recognition that small businesses could be treated unconscionably within the context of a commercial relationship.⁸ Eighteen years of the possibility of a statutory unconscionable conduct action have, however, failed to reduce franchisor over-reaching. Concerns continue to be raised in relation to the asymmetrical elements of franchising,⁹ and are also evidenced by the conduct of several governmental and parliamentary inquiries at both federal and state level.¹⁰

The adoption of standard form contracts by franchisors is unavoidable. In Australia, the average ratio of franchisors to franchisees is 1:60. It is unrealistic to expect a franchisor to negotiate a bespoke contract with each franchisee. Doing so would result in inefficiency. A further difficulty in franchising is that both contracting parties (franchisor and franchisee) have multiple legal relationships. These additional contractual and statutory relationships potentially place any of the parties in a situation of conflict vis-a-vis their obligations under the franchise contract. It may not, for example, be possible to respect the contract-based expectation of one's counterparty to a franchise agreement whilst also adhering to statutory duties to one's shareholders. It is timely to consider whether a different approach to measuring fairness in franchise relationships is required.

Despite the dissenting judgment of Kirby J in *NEAT Domestic Trading Pty Ltd v AWB Ltd*,¹¹ the majority of the Australian High Court left open the question of whether administrative law remedies were available against a private entity. Both

⁸ CCA sch 3 s 22 (formerly TPA s 51AC).

⁹ See, eg, Albert H Choi and George G Triantis, 'The Effect of Bargaining Power on Contract Design' 98(8) (2012) *Virginia Law Review* 1665. See also Jenny Buchan, *Franchisees as Consumers: Benchmarks, Perspectives and Consequences* (Springer, 2013) 84-95.

¹⁰ Franchising Code Review Committee, *Review of the Disclosure Provisions of the Franchising Code of Conduct: Report to Hon Fran Bailey MP: Minister for Small Business and Tourism* (2006) ('*Matthews Report*'); Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Inquiry Into the Franchising Code of Conduct* (2008) ('*Cth Inquiry*') resulting in Parliamentary Joint Committee on Corporations and Financial Services, Parliament of Australia, *Opportunity Not Opportunism: Improving Conduct in Australian Franchising* (2008) ('*Opportunity not Opportunism Report*'); Small Business Development Corporation, Parliament of Western Australia, *Inquiry into the Operation of Franchise Businesses in Western Australia: Report to the Western Australian Minister for Small Business* (2008) ('*WA Inquiry*'); Economic and Finance Committee, Parliament of South Australia, *Franchises* (2008) ('*SA Inquiry*') and Alan Wein, Submission to Minister for Small Business and Parliamentary Secretary for Small Business, *Review of the Franchising Code of Conduct*, 30 April 2013 ('*Wein Review*').

¹¹ 216 CLR 277, 300 [67] (Kirby J) questioning 'whether, in the performance of a function provided to it by federal legislation, a private corporation is accountable according to the norms and values of public law or is cut adrift from such mechanisms of accountability and is answerable only to its shareholders and to the requirements of corporations law or like rules'.

laws against unconscionable conduct and the developing doctrine of good faith have struggled when faced with the exercise of franchisor discretion; they are applied purely by reference to private law principles. Our thesis is that, by adapting the principles underlying administrative law to the consideration of whether a franchisor has exercised a contractual discretion appropriately, greater clarity can be brought to the assessment of whether a contract-granted discretion has been exercised in ‘good faith’ and fairly.

Many of the dilemmas faced in administrative law are also found within the ambit of private law. Unit franchise agreements, being standard form, executory, relational contracts that confer broad discretionary powers and few explicit obligations on franchisors, are one example. Administrative law has long possessed tools empowering the review of discretionary decision-making by public authorities. Reference to these approaches could guide franchisors, and enable judges and regulators alike, to formulate appropriate responses to problems arising out of franchise relationships.

This article is in seven parts, the first being this introduction. In the next we consider 21st century franchising, franchise agreements and the triggers for disputes that are resolved in court. We also identify the similarities that exist between the exercise of the franchisor’s power and the officials exercising discretion. Part III addresses the current solution of statutory unconscionable conduct and common law good faith, and the new statutory duty of good faith. Part IV examines the administrative law jurisprudence surrounding good faith, lawfulness and rationality, errors of law and fact finding, and fairness. This is done against the possibility that the approach might be used to refine the private law concept of good faith in franchising. In Part V we observe that the solutions reached by judges applying a mix of statutory and common law rules to restrain the abuse of contractual discretions by franchisors, already draw on the framework of administrative law jurisprudence in ascertaining the presence of good faith. Doctrinal issues must be addressed and we do so in Part VI. Part VII is the conclusion.

II 21ST CENTURY FRANCHISING

The economic reasons for the success of business format franchising are well understood.¹² The franchisee’s capital and local knowledge is combined with the franchisor’s know-how and brand reputation. The economies of collective purchasing power are harnessed. As a result, the franchisee should ‘hit the ground running’ rather than risking the pitfalls a nascent stand-alone business may experience.

The success of franchising has largely been founded on its flexibility and ability to deal with fast-changing market conditions. The franchisor necessarily retains the freedom to make changes to the system to enable it to respond to market conditions

¹² Economists are, however, yet to include the cost of franchisor insolvency in the model. It remains an externality whose inclusion could challenge the rarely questioned popular notion of the success of the franchise model.

and remain competitive. To term franchise contracts ‘agreements’ is almost a misnomer. They are incomplete, drafted to protect the franchisor’s interests as well as to embed a power and risk imbalance that favours the franchisor.¹³ The long duration of franchise agreements,¹⁴ and the franchisees’ often large sunk investments, mean franchisees are vulnerable to opportunistic behaviour by franchisors. The nature of the grant enjoyed by the franchisee towards the end of its term consequently may bear little resemblance to that at the outset.

Disputes between franchisors and franchisees are of two main types. Firstly, there is a tendency by franchisors to oversell the franchise, the franchisor’s experience, ability to support its franchisees or its solvency, thus potentially misrepresenting the true nature of what the franchisee is purchasing.¹⁵ This may lead to an action under s 18(1) of the *CCA*.¹⁶ Secondly, and more relevant to the present discussion, are disputes based on performance of the franchise agreement. It is difficult for franchisees to successfully argue that their franchisor has breached a contract that imposes discretionary obligations that are few and vague. For example Hadfield notes that

the franchisee paid fees for a service that the service-provider retained full discretion to define in content and duration. ... the contract frames franchisor obligations in terms such as ‘reasonable’, ‘periodic’, and ‘from time to time’. The franchisor had no contractual duty to employ prudence or consideration in the making of decisions that directly affect the profitability of the franchisee.¹⁷

Indeed, Elizabeth Spencer states that ‘[c]lauses drafted to ensure discretion to a franchisor, leaving franchisees in a position of uncertainty and increased risk, are ubiquitous in franchising contracts.’¹⁸ As a consequence, they create ‘little in the

¹³ Buchan, above n 5. See also Elizabeth C Spencer, ‘Consequences of the Interaction of Standard Form and Relational Contracting in Franchising’ (2009) 29 *Franchise Law Journal* 31.

¹⁴ The average length of a franchise agreement in Australia is five years but some franchisors grant licences and master licences for 25 years and some for an indefinite period. For details, see Lorelle Frazer, Scott Weaven and Kelli Bodey, *Franchising Australia 2012* (Griffith University, 2012) 35.

¹⁵ See, eg, *Carlton v Pix Print Pty Ltd* [2000] FCA 337 (22 March 2000) where the franchisor misrepresented to the applicant master franchisee that the Pix Print business was successful and expanding in breach of s 52 of the *TPA*. See also *Billy Baxters (Franchising) Pty Ltd v Trans-It Freighters Pty Ltd* [2009] VSC 207 where the franchisee unsuccessfully claimed franchisor (Billy Baxter’s) had misled it about possible turnover. On appeal the Victorian Supreme Court in *Trans-It Freighters Pty Ltd v Billy Baxters (Franchising) Pty Ltd* [2012] VSCA 71 (20 April 2012) (Bongiorno and Hansen JJA and Kyrou AJA) unanimously reversed the decision.

¹⁶ Formerly s 52 *TPA*.

¹⁷ Hadfield, above n 6, 945-946.

¹⁸ Elizabeth Spencer, ‘Consequences of the Interaction of Standard Form and Relational Contracting in Franchising’ in Elizabeth C Spencer (ed), *Relational Rights and Responsibilities: Perspectives on Contractual Arrangements in Franchising* (Bond University Press, 2011) 47, 57.

way of real obligation on the part of a franchisor and no contractual right in a franchisee.’¹⁹ A further corollary is that although ‘[r]elational contracts accommodate uncertainty by leaving terms unspecified and providing high levels of discretion, ... [they] often fail to provide clear and specific answers in case of dispute’.²⁰ The courts, through recourse to doctrines such as good faith, and the legislature, through statutory remedies such as unconscionability, have applied solutions to accommodate such uncertainties that in many respects resemble the criteria for reviewing administrative action. We suggest the next step for regulators and courts is to look actively at how administrative law addresses disputes that originate from the exercise of discretion.

A Parallels between Franchise Networks and Public Bureaucracies

It has been said in relation to the values underpinning administrative law that

[t]here seem to be few, if any, aspects of economic activity in contemporary society that are not supervised by some kind of statutory [ie without an element of choice] regulator with *powers to grant, withhold, suspend or cancel licences to engage in such activity and to approve or withhold approval for particular transactions*.²¹

Here the parallel with franchising is striking, as the emphasised words describe the powers franchisors possess to grant a franchise. And having done so, to amend the grant, revoke it, provide assistance to or sanction myriad transactions by their franchisees (such as purchasing stock from a third party or providing the franchise agreement as security for a loan). A franchise agreement and its accompanying documents create an environment of private regulation with the franchisor acting as both regulator and arbiter. Spencer argues that ‘discretion facilitates action on improper considerations, and permits the substitution of subjective, personal standards for agreed-upon ones’.²² Uncertainty results from the current environment. For example, whilst the issues in *Automasters Australia Pty Ltd v Bruness Pty Ltd* were considered in the context of an express term of ‘absolute good faith’,²³ contained in cl 15 of the Automasters franchise agreement, this standard was diluted by the franchisor being obliged to do no more than ‘use its best endeavours to promote the performance and success of the franchise business’.²⁴

¹⁹ Ibid.

²⁰ Ibid 54.

²¹ Chief Justice Robert French, ‘Administrative Law in Australia: Themes and Values’ in Matthew Groves and H P Lee (eds) *Australian Administrative Law: Fundamentals, Principles and Doctrines* (Cambridge University Press, 2007) 15, 15 (emphasis added).

²² Spencer, above n 18, 56.

²³ *Automasters Australia Pty Ltd v Bruness Pty Ltd* [2002] WASC 286 (4 December 2002) [14] (*‘Automasters’*).

²⁴ Ibid.

We contend that objective standards of fairness and reasonableness now exist in Australian administrative law²⁵ — unlike perhaps in the United Kingdom — and that the developing doctrine of good faith in Australia replicates essentially the same standard. This article evaluates the validity of this proposition by examining its application to franchisor-franchisee relationships. Before exploring the approaches within administrative law, we will examine two current private law tools: unconscionability and good faith.

III THE SEARCH FOR SOLUTIONS

In a celebrated passage, Paul Finn (formerly a judge of the Federal Court of Australia) hints at the existence of a spectrum from self-interested behaviour (which nonetheless disallows exploitative conduct) to good faith and finally completely selfless behaviour encompassed by the fiduciary standard.²⁶ Andrew Terry and Cary Di Lernia observe that ‘clear dividing lines between concepts along that continuum are seldom provided’.²⁷ Nevertheless, several doctrinal tools have been employed or proposed to deal with the continuum in the context of franchise relationships. Here we consider two of these: the extant unconscionable conduct and current common law, and the new statutory duty of good faith.

A Unconscionable Conduct

Unconscionable practices by franchisors were first brought to the attention of Australia’s federal government in the 1976 ‘*Swanson Report*’.²⁸ These practices were cast as being ‘unfair or deceptive acts or practices’.²⁹ The Swanson Committee shied away from the notion of sanctioning unfair conduct because of the potential for the word ‘unfair’ to introduce uncertainty into commercial transactions. Peter Reith introduced a package of reviews in 1997 called ‘New Deal: Fair Deal — Giving Small Business a Fair Go’. By mid-1998 the *TPA* had been amended by the addition of s 51AC,³⁰ which prohibited unconscionable conduct in business-to-business transactions and the enactment of the mandatory *Trade Practices (Industry Codes – Franchising) Regulations 1998* (Cth) (‘*Code*’). Interestingly, as

²⁵ *Minister for Immigration and Citizenship v Li* (2013) 249 CLR 332, 337–52 (French CJ).

²⁶ Paul D Finn, ‘The Fiduciary Principle’ in T G Youdan (ed) *Equity, Fiduciaries and Trusts* (Carswell, 1989) 1, 4.

²⁷ Andrew Terry and Cary Di Lernia, ‘Franchising and the Quest for the Holy Grail: Good Faith or Good Intentions?’ (2009) 33 *Melbourne University Law Review* 542, 555.

²⁸ Trade Practices Act Review Committee, *Report to the Minister for Business and Consumer Affairs* (Australian Government Publishing Service, 1976) (‘*Swanson Report*’).

²⁹ *Ibid* 66.

³⁰ Now *CCA* sch 2 s 22.

deduced from the ‘fair go’ wording of the 1997 review, the concept of ‘fairness’ was the topic of the debate. At the 11th hour it was decided to use the expression ‘unconscionable conduct’ rather than ‘fairness’ in the new legislation in order to

build on the existing body of case law which [was seen to have] worked with respect to consumer protection provisions of the [TPA] and which [it was thought] will provide greater certainty to small businesses in assessing their legal rights and remedies.³¹

Whether conduct was unconscionable was to be ‘determined by examining all the circumstances of the case’³² with regard to listed non-exclusive, discretionary, cumulative criteria.³³ The franchisees’ sunk investment could arguably be taken into consideration as an aspect of measuring the extent to which the supplier (franchisor) acted in good faith under sch 2 s 22(1)(l) of the *CCA* when evaluating the unconscionability of a franchisor’s conduct. Nevertheless, this aspect of a franchisee’s vulnerability has yet to be considered.

However, uncertainty about the scope and application of the unconscionable conduct standard has continued, as evidenced by the seven government franchising and unconscionable conduct inquiries since 1998.³⁴ The Senate Standing Committee on Economics in December 2008 conducted a review on ‘[t]he need, scope and content of a definition of unconscionable conduct for the purposes of Part IVA of the [TPA]’. Notably, it was loath to attribute the fact that ‘there [had] only been two successful findings under section 51AC over the past decade’³⁵ to any overall improvement in conduct of businesses. It attributed the low number of successful prosecutions to the courts’ narrow interpretation of s 51AC. Because the legislative prohibition of unconscionable conduct in business transactions is not limited to the traditional equitable categories of special disadvantage, ‘the courts have come to different understandings of what constitutes “unconscionability”’.³⁶ The difficulties are, as Terry and Di Lernia maintain, compounded by the inclusion of the extent to which the parties acted in good faith as one of the criteria for determining whether unconscionable conduct has taken place. Since Terry and Di Lernia’s 2009 observations, s 21 of sch 2 (the unconscionable conduct provision of the *CCA*) replaced s 51AC of the *TPA*. In the new section, the definition of a ‘business consumer’ (found in the old s 51AC of the *TPA*) became the definition of a ‘customer’ (per the new s 22 of sch 2

³¹ Commonwealth, *Parliamentary Debates*, House of Representatives, 30 September 1997, 8767 (Peter Reith).

³² Explanatory Memorandum, Trade Practices Amendment (Fair Trading) Bill 1997 (Cth) 1.

³³ See *Australian Consumer Law* sch 2 n 22(1)(a)–(k) and sch 2 s 22 (2)(a)–(k).

³⁴ See *Matthews Report*, *WA Inquiry*, *SA Inquiry*, *Cth Inquiry* and *Wein Review*. See also Senate Standing Committee on Economics, Parliament of Australia, *The Need, Scope and Content of a Definition of Unconscionable Conduct for the Purposes of Part IVA of the Trade Practices Act 1974* (2008).

³⁵ *Ibid* 31.

³⁶ Terry and Di Lernia, above n 27, 555.

of the *CCA*). A new concept applicable to unconscionable conduct was included in s 21(4) stating that:

...

- (b) this section is capable of applying to a system of conduct or pattern of behaviour, whether or not a particular individual is identified as having been disadvantaged by the conduct or behaviour; and
- (c) in considering whether conduct to which a contract relates is unconscionable, a court's consideration of the contract may include consideration of:
 - (i) the terms of the contract; and
 - (ii) the manner in which and the extent to which the contract is carried out;and is not limited to consideration of the circumstances relating to formation of the contract.

It is too early to conclude whether the 'system' or 'pattern' envisaged in s 21(4)(b) will be interpreted to encompass franchise-wide systems or patterns, or whether it will be interpreted as system or pattern of unconscionable conduct within the performance of an individual contractual relationship. Notably, the 'good faith' criterion has been retained in the *CCA* list of factors that can indicate the presence or absence of unconscionable conduct.

Elisabeth Peden warns that the pre-occupation with developing a doctrine of good faith in Australia (which is discussed further below) has had perverse effects in encroaching on and distorting existing unconscionability doctrines as well as diminishing contractual certainty, stating that:

it seems that with the recent decisions on good faith, the judges are moving closer to the position where they will interfere with the exercise of rights or powers because of unreasonableness, rendering unconscionability unnecessary ... this current position is robbing contract law of certainty in relation to what restrictions a court might impose on contracting parties seeking to exercise rights.³⁷

It is in order to address these uncertainties that we examine the principles underlying control of administrative power. It will be seen that similar difficulties afflict administrative law, in particular the criticism made by scholars that reasonableness review lacks certainty and transparency.³⁸ Despite these obstacles, we argue that administrative law principles provide a framework as to how contractual provisions of uncertain ambit are *applied* — something traditional doctrines such as unconscionability struggle with — and ought therefore not to be disregarded too readily.

³⁷ Elisabeth Peden, 'When Common Law Trumps Equity' (2005) 21 *Journal of Contract Law* 226, 249.

³⁸ Jonathan Morgan, 'Against Judicial Review of Discretionary Contractual Powers' [2008] *Lloyd's Maritime and Commercial Law Quarterly* 230, 231.

B Good Faith

Much ink has been spilt by Australian jurists and commentators in examining the role that the doctrine of good faith plays in contract generally,³⁹ and in the context of franchising specifically.⁴⁰ The failure to achieve greater symmetry in the franchisor-franchisee relationship has led to calls by some⁴¹ for an explicit enactment of a duty of good faith into franchise agreements as a panacea to the power imbalance. Good faith as a solution has also been criticised as Australia does not possess a settled jurisprudence in relation to the doctrine.⁴² The imposition of an implied term of good faith has been cast as a ‘backward step’.⁴³ In the United States, the content and meaning of the previously settled concept of good faith is being questioned.⁴⁴ In the following sections we will venture some observations on this point.

1 Good Faith at Common Law

Our discussion primarily relates to franchise agreements. In the seminal non-franchise case of *Renard Constructions (ME) Pty Ltd v Minister for Public*

³⁹ See generally cases listed in Terry and Di Lernia, above n 27, 546–8. See also Bill Dixon, ‘Common Law Obligations of Good Faith in Australian Commercial Contracts — A Relational Recipe’ (2005) 33 *Australian Business Law Review* 87; Elisabeth Peden, ‘Implicit Good Faith — or Do We Still Need an Implied Term of Good Faith?’ (2009) 25 *Journal of Contract Law* 50; and Suzanne Corcoran, ‘Good Faith as a Principle of Interpretation: What is the Positive Content of Good Faith?’ (2012) 36 *Australian Bar Review* 1.

⁴⁰ See, eg, *Burger King Corporation v Hungry Jack’s Pty Ltd* (2001) 69 NSWLR 558 (*‘Burger King’*) and *Far Horizons Pty Ltd v McDonalds Australia Ltd* [2000] VSC 310 (18 August 2000) (*‘Far Horizons’*).

⁴¹ Elizabeth Crawford Spencer, Submission No 39 to Parliamentary Joint Committee on Corporations and Financial Services, *Inquiry into Franchising Code of Conduct*, 1 January 2008, 34–5; *SA Inquiry*, above n 10, 56–9, citing Frank Zumbo, Submission No 43 to the Economic and Finance Committee, *Franchises*, 3 March 2008. See also Philip Coleman, Submission No 16 to Government of Department of Industry, Innovation, Science, Research and Tertiary Education, *Review of the Franchising Code of Conduct 2013*, 12 February 2013, 5–7 and Elizabeth Spencer and Simon Young, Submission No 25 to Department of Industry, Innovation, Science, Research and Tertiary Education, *Review of the Franchising Code of Conduct 2013*, 14 February 2013.

⁴² Terry and Di Lernia, above n 27, 542 and *SA Inquiry*, above n 10, 56–7, citing Franchise Council of Australia, Submission No 17 to the Economic and Finance Committee, *Franchises*, 21 January 2008.

⁴³ Peden, above n 39, 53.

⁴⁴ See Howard O Hunter, ‘The Growing Uncertainty about Good Faith in American Contract Law’ (2004) 20 *Journal of Contract Law* 50 for a discussion of the range of interpretations of the concept of good faith that US courts are adopting in relation to the concept of good faith in contracts. See also Corcoran, above n 39, 6.

Works,⁴⁵ the majority of the New South Wales Court of Appeal found an implied term that the principal had to act in good faith and reasonably. However, Meagher JA in the minority found a more straightforward basis for the ruling namely: that the non-compliance by the principal with an express term of the contract could be taken to require the principal to act on accurate information when forming a view as to whether the contractor had shown cause for the principal to cancel the contract.⁴⁶

To Suzanne Corcoran good faith is conduct that is appropriate; '[t]o be appropriate the result must not be absurd and should also be fair and balanced in the circumstances'.⁴⁷ Her comments relate to the interpretation of contracts that may 'involve determining what the parties would credibly have agreed upon had they turned their minds to the question'.⁴⁸ To this point the analysis does not do franchise contracts, or other voluntarily executed, but non-negotiated, relational, commercial contracts, any disservice. But, as Corcoran continues, 'the principle of good faith is a guide to judging what can credibly be advanced as to a permissible motivation'.⁴⁹ We will see in Part III B (3) an example of a permissible motivation for one party being far outside the contemplation of the other.

Difficulties exist in attempting to introduce the concept of good faith into contractual relationships. First, the actual *mechanism* for introducing the duty must be settled; and secondly, the *content* of the duty must be defined.

In relation to mechanism, Bill Dixon identifies two 'quite disparate' approaches by courts: terms that reflect the presumed intention of the parties (that are dependent on the circumstances of each case) and terms based on imputed intention; that is, implied

⁴⁵ (1992) 26 NSWLR 234; see also the summary of the long-running *Renard* saga in John Ingold, 'The Renard Saga — The High Court Refuses Leave to Appeal' (1993) 28 *Australian Construction Law Newsletter* 70, 70–1, where Ingold notes:

The Minister had improperly exercised the power to terminate the contractor's employment under cl 44.1, thereby repudiating the contract. Priestley and Handley JJA thought that the principal had to act reasonably under cl 44.1, both when considering the cause shown by the contractor and then, at the next stage, when considering whether to exercise the power to take over the works or cancel the contract. In this case, the Minister had not acted reasonably. Meagher JA thought that there was no requirement that the principal act under cl 44.1 in an objectively reasonable manner. However, he thought that the principal could not be "satisfied" within the meaning of cl 44.1 if he did not comprehend the factual background on which satisfaction is required. Here, the principal's mind was "so distorted by prejudice and misinformation that he was unable to comprehend the facts in respect of which he had to pass judgment". Meagher JA thus came to the same result as the majority, that there had been an invalid exercise of the power under cl 44.1 and that the Minister had thereby repudiated the contract.

⁴⁶ *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234, 276.

⁴⁷ Corcoran, above n 39, 8.

⁴⁸ *Ibid* 8.

⁴⁹ *Ibid*.

by law as a legal incident of a particular class of contract.⁵⁰ The need in the first approach to satisfy the five criteria in *BP Refinery (Westernport) Pty Ltd v President, Councillors and Ratepayers of the Shire of Hastings*⁵¹ ensures this high hurdle will be unlikely to be cleared where the contract has ‘efficacy’ without implying good faith. Further, in relation to any specific action it is likely that a franchisor and its franchisees have differing presumed intentions.

The second approach must also satisfy two requirements; an identifiable class of relationships and necessity. In terms of the present discussion, it has been judicially observed that ‘the classes of contracts in which the law will imply terms are not closed’.⁵² It is not therefore farfetched to suggest that contracts that confer significant powers and discretions on the party drafting the contract, but not on the other, constitute such a class. The second requirement is ‘necessity’.⁵³ It must be established that ‘[u]nless such a term be implied, the enjoyment of the rights conferred by the contract would or could be rendered nugatory, worthless or perhaps be seriously undermined’.⁵⁴ However, Dixon suggests that wider considerations of policy have also been used to support the implication of contractual terms as a matter of law.⁵⁵ In the franchising context these might include (a) the vulnerability of a class such as franchisees, (b) the standard form nature of agreements and (c) the need to protect franchisees from discriminatory treatment. These considerations would be balanced against the interests of the franchisees in having the integrity of the franchise system maintained by the franchisor. Similar policy considerations inform decision-makers in the public sphere.

Besides disapproving of such a wider ground, Dixon is critical of the manner in which courts in Australia have played fast and loose with the grounds for implying good faith as an obligation in contracts. He notes that consideration of the class of contract attracting the obligation and the necessity test are often ignored.⁵⁶ In addition, he states that the use of vulnerability as a test ‘raises doctrinal issues of ...

⁵⁰ Bill Dixon, ‘Good Faith in Contractual Performance and Enforcement — Australian Doctrinal Hurdles’ (2011) 39 *Australian Business Law Review* 227, 233.

⁵¹ (1977) 180 CLR 266, 283. These are listed by Lord Simon of Glaisdale as:

(1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; (3) it must be so obvious that ‘it goes without saying’; (4) it must be capable of clear expression; (5) it must not contradict any express term of the contract.

⁵² *Castlemaine Tooheys Ltd v Carlton & United Breweries Ltd* (1987) 10 NSWLR 468, 487 (Hope JA).

⁵³ Dixon, above n 50, 234.

⁵⁴ *Byrne v Australian Airlines Ltd* (1995) 185 CLR 410, 450. See also *Liverpool City Council v Irwin* [1977] AC 239.

⁵⁵ Dixon, above n 50, 234. See also *Hughes Aircraft Systems International v Airservices Australia* (1997) 76 FCR 151, 194–5.

⁵⁶ Dixon, above n 50, 238.

the interplay between common law and equitable remedies'.⁵⁷ Dixon's objections have less cogency if the outcomes are seen as applications of fundamental principles, such as the administrative law based duty to act rationally. For example, *Vodafone Pacific Ltd v Mobile Innovations Ltd*⁵⁸ might better be seen as a case involving abuse of or failure to exercise a particular discretion rather than the more strained finding of breach of an implied term to act in good faith.

The second difficulty identified by Dixon, Peden and other commentators is the content of the duty of good faith where it does exist:

'[w]e caution anyone who is confident about the meaning of good faith to reconsider', write two leading American scholars, White and Summers ... So far the courts have not offered much by way of explanation of the content of the implied term of good faith, other than emphasising that it requires contracting parties to act reasonably, at least when exercising express rights and discretions. Although there are many recent cases in which judges have expressed the requirement of good faith in terms of 'reasonableness', the concept of good faith is still not unambiguous.⁵⁹

In particular, there appears to have been a "blurring" between the different standards of reasonableness, unconscionability and good faith'.⁶⁰ Many instances involving unconscionability in fact concern the exercise of contractual powers and discretions. The discussion that follows will also demonstrate that cases involving the alleged failure to act in good faith in franchising relationships also concerned the exercise of contractual powers and discretions. These common features hint at fundamental underlying behaviour — in the form of use of discretionary powers in a way that neither the weaker party nor the drafter originally intended — that also exists in the administrative law arena.

The administrative law framework exhibits many characteristics of these contractual doctrines. However, it contains both procedural requirements, as to fairness, as well as substantive requirements of honesty and rationality which are explored in Part IV. The utility of these doctrines for the exercise of contractual powers and discretions by franchisors in particular is examined in Part V.

2 *Legislative Definition of Good Faith*

Witnesses before several inquiries into franchising in Australia have opposed the introduction of an explicit defined duty of good faith⁶¹ being adopted thus

⁵⁷ Ibid 241.

⁵⁸ [2004] NSWCA 15 (20 February 2004).

⁵⁹ Peden, above n 37, 234 (citations omitted).

⁶⁰ Ibid 245.

⁶¹ The ACCC is opposed to imposing a general obligation to act in good faith via the *Code* for three reasons: (1) The potential impact on the operation of the *Code* and the work of the ACCC; (2) The degree of uncertainty about the interpretation that may

far.⁶² As a concession to the repeated calls for implementation of a specific good faith requirement, the *Code* was amended in 2010 by the introduction of cl 23A, which states: ‘[n]othing in this code limits any obligation imposed by the common law, applicable in a State or Territory, on the parties to a franchise agreement to act in good faith.’⁶³

It ‘preserves and recognises any developments in the case law on the concept of “good faith”’.⁶⁴ The reasons given for the then rejection of a more explicit standard in the *Code* are instructive. Whereas it was regarded as desirable to insert a set of statutory examples of ‘unconscionable conduct’, this was not thought possible ‘with a concept like “good faith” ... which is an overarching principle guiding how parties *should* behave to each other’.⁶⁵ Another reason, articulated by Bryan Horrigan, was that apart from in New South Wales, the doctrine of good faith has not found general recognition throughout Australia.⁶⁶ Indeed Horrigan argued that there needed to be a more developed body of law on which a statutory definition could draw before a definition was viable, and that to attempt a definition before this would add uncertainty.⁶⁷

create ambiguity and confusion and increase conflict, and (3) The fact that nothing currently prevents parties from contractually agreeing to act in good faith: Australian Competition and Consumer Commission, Submission No 60 to the Parliamentary Joint Committee on Corporations and Financial Services, *Inquiry into Franchising Code of Conduct*, September 2008, 19.

⁶² See, eg, *Matthews Report*, above n 10, 13 where recommendation 25 states: ‘A statement obligating franchisors, franchisees and prospective franchisees to act towards each other fairly and in good faith be developed for inclusion in Part 1 of the Code’. Two years later, the *Opportunity not Opportunism Report* recommended that a clause be inserted into the *Code* prescribing a good faith Standard of Conduct for franchisors, franchisees and prospective franchisees in ‘relation to all aspects of a franchise agreement’: at 115. It should also be noted that the Franchise Agreements Bill 2011 (WA) incorporating good faith before the Western Australian legislature was only defeated by one vote. Section 11 would have defined the duty to act in good faith as to the duty to ‘act fairly, honestly, reasonably and cooperatively.’ Section 2 would have required parties to a WA franchise agreement to act in good faith:

- ...
- (a) in any dealing or negotiation in connection with —
 - (i) entering into or renewing the agreement; or
 - (ii) the agreement; or
 - (iii) resolving, or attempting to resolve, a dispute relating to the agreement; and
 - (b) when acting under the agreement.

⁶³ Introduced by *Trade Practices (Industry Codes — Franchising) Amendment Regulations 2010 (No 1)* (Cth).

⁶⁴ Explanatory Statement, Select Legislative Instrument 2010, No 125 (Cth) 5.

⁶⁵ Senate Standing Committee on Economics, above n 34, 40 [5.42] (emphasis in original).

⁶⁶ *Ibid.*

⁶⁷ *Ibid* 40 [5.43].

These objections make the proposed approach advanced in Part V of this article more pertinent. It provides not merely a stopgap solution to the deficits identified above, but principles against which to evaluate conduct as being ‘in good faith’ and ‘fair’.

3 *Good Faith following the 2013 Government Review*

In 2013, the Australian government commissioned another review of the *Code*.⁶⁸ Despite concerns over ‘good faith’, the 2013 reviewer recommended the introduction of an express obligation to act in good faith into the *Code*.⁶⁹ This recommendation was adopted and implemented in 2014 to replace the 1998 *Code*. The 2014 *Code* now provides:

6 Obligation to act in good faith

Obligation to act in good faith

- (1) Each party to a franchise agreement must act towards another party with good faith, within the meaning of the unwritten law from time to time, in respect of any matter arising under or in relation to:
 - (a) the agreement; and
 - (b) this code.

This is the ***obligation to act in good faith***.

Civil penalty: 300 penalty units.

- (2) The obligation to act in good faith also applies to a person who proposes to become a party to a franchise agreement in respect of:
 - (a) any dealing or dispute relating to the proposed agreement; and
 - (b) the negotiation of the proposed agreement; and
 - (c) this code.

Matters to which a court may have regard

- (3) Without limiting the matters to which a court may have regard for the purpose of determining whether a party to a franchise agreement has contravened subclause (1), the court may have regard to:
 - (a) whether the party acted honestly and not arbitrarily; and
 - (b) whether the party cooperated to achieve the purposes of the agreement.

Franchise agreement cannot limit or exclude the obligation

- (4) A franchise agreement must not contain a clause that limits or excludes the obligation to act in good faith, and if it does, the clause is of no effect.
- (5) A franchise agreement may not limit or exclude the obligation to act in good faith by applying, adopting or incorporating, with or without modification, the

⁶⁸ *Trade Practices (Industry Codes — Franchising) Regulations 1998* (Cth) (‘Code’).

⁶⁹ *Wein Review*, above n 10, x–xi.

words of another document, as in force at a particular time or as in force from time to time, in the agreement.

Other actions may be taken consistently with the obligation

- (6) To avoid doubt, the obligation to act in good faith does not prevent a party to a franchise agreement, or a person who proposes to become such a party, from acting in his, her or its legitimate commercial interests.
- (7) If a franchise agreement does not:
 - (a) give the franchisee an option to renew the agreement; or
 - (b) allow the franchisee to extend the agreement;

this does not mean that the franchisor has not acted in good faith in negotiating' or giving effect to the agreement.⁷⁰

Clause 6 applies to 'parties to a franchise agreement'. It would afford franchisees no protection from decisions made by an ultimate owner of the franchise network. Significantly, many franchisors become insolvent.⁷¹ Therefore, in the context of insolvency cl 6 is problematic. An administrator is an agent of the insolvent party.⁷² The duty to act in good faith would be extended to an administrator of the franchisor or franchisee in any matter relating to the franchise agreement. An administrator has, however, an overriding duty under the *Corporations Act 2001* (Cth) to 'assist the creditors in recovering'⁷³ moneys owed to them. Clause 6(2) would give the counterparties of the insolvent party an entirely wrong expectation about the duty the administrator owed them.

This takes us to cl 6(6). It is hard to see how a franchisor would do anything other than prioritise its own interests ahead of the franchisees' interests if it could meet the good faith standard by acting purely in its own commercial interests. Clause 6(6) would not, for example, change the outcome for the franchisee in *Meridian Retail Pty Ltd v Australian Unity Retail Network Pty Ltd*⁷⁴ where the franchisor was pursuing legitimate commercial objectives. A by-product of the franchisor's decision to exit the franchise model was that the franchisee lost the right to sell insurance products that accounted for 80 per cent of its revenue.⁷⁵ This rendered the franchisee business unviable. This would have been acceptable under cl 6(6). One can only speculate on the consequences of McDonald's telling its franchisees they could now sell everything except burgers, fries and Happy Meals®.

⁷⁰ *Competition and Consumer (Industry Codes — Franchising) Regulation 2014* (Cth) sch 1 div 3, cl 6.

⁷¹ Buchan, above n 9, 115–17.

⁷² *Corporations Act 2001* (Cth) s 437B.

⁷³ Christopher Symes and John Dunns, *Australian Insolvency Law* (LexisNexis Butterworths, 2009) 240.

⁷⁴ [2006] VSC 223 (21 June 2006).

⁷⁵ *Ibid* [6].

It is submitted that in light of the above, neither good faith, as an evolving common law standard, nor good faith in cl 6, can satisfactorily address the *ex post* legitimate expectations of franchisees. American commentator Howard Hunter put his finger on the problem when he observed that '[t]he substance of good faith derives from the expectations of the parties as expressed in the agreement itself, and so the scope of what is meant by good faith will change from agreement to agreement and party to party'.⁷⁶

An assessment of good faith in the performance of a franchise agreement, based on the flawed premise that both parties contributed to the content of the franchise agreement, is doomed. Further, not only does the notion change from agreement to agreement, but also from context to context.

C Influence of Statutes on Common Law

A fruitful line of inquiry relevant to the present article, but beyond its immediate scope, is the influence of statutory principles or the policies underlying statutes on the development of common law principles. The concept was explained by Lord Diplock in *Erven Warnink BV v J Townend & Sons (Hull) Ltd* as follows:

Where over a period of years there can be discerned a steady trend in legislation which reflects the view of successive Parliaments as to what the public interest demands in a particular field of law, development of the common law in that part of the same field which has been left to it ought to proceed upon a parallel rather than a diverging course.⁷⁷

Professor Atiyah has questioned whether the courts may 'justify jettisoning obsolete cases, not because they have been actually reversed by some statutory provision, but because a statute suggests that they are based on outdated values?'⁷⁸

The question has been answered affirmatively in New Zealand⁷⁹ and in the United States.⁸⁰ However, two important qualifications to the doctrine were stated by the United States Supreme Court: the courts must ensure the express limits on the changes implemented by legislation do not thereby imply approval of the common law as it applies beyond those limits, and secondly, they must ensure the protection of the doctrine of precedent and the validity of certainty in the law.⁸¹

⁷⁶ Hunter, above n 44, 51.

⁷⁷ [1979] AC 731, 743.

⁷⁸ P S Atiyah, 'Common Law and Statute Law' (1985) 48 *Modern Law Review* 1, 6.

⁷⁹ See Gehan N Gunasekara, 'Judicial Reasoning by Analogy with Statutes: Now an Accepted Technique in New Zealand?' (1998) 19 *Statute Law Review* 177.

⁸⁰ *Moragne v States Marine Lines*, 398 US 375 (1970).

⁸¹ *Ibid* 351.

When applied to franchising the relevance of these concepts is evident. As we have seen, there has been a steady legislative trend in Australia, however, the fulfilment of this change has been left largely up to the courts. Given the encapsulation of the doctrine of good faith within that of unconscionability, it is no longer possible to argue that the provisions pertaining to unconscionable conduct⁸² and the parallel provisions of the *Code* – many catalogued below and requiring in essence fairness and transparency in dealings between franchisors and franchisee – signify legislative endorsement of the existing common law governing these relationships.

Against this backdrop particularly, attention is now turned to administrative law principles and their potential to provide criteria that would enable a common law court to measure whether discretion granted within a franchise relationship had been exercised within appropriate parameters.

IV RELEVANT ADMINISTRATIVE LAW JURISPRUDENCE

We outline below the main categories triggering the opportunity for, and the mechanisms enabling, review of administrative decisions. We suggest these afford alternative benchmarks against which franchisors could test their intended exercise of discretions.

A Limits on the Use of Discretion

Administrative decisions may proceed along two lines: review or appeal. A review to examine the legality of a decision focuses on the decision-makers' powers or authority, and on whether the decision was made within the authority conferred (*intra vires*) or was beyond its ambit (*ultra vires*).⁸³ Appeal, on the other hand, involves examining not just the legality of a decision, but its merits. This distinction has ramifications in the context of questioning commercial decisions such as those made by franchisors. A court examining a franchisor's abuse of a decision-making power conferred by contract ought not to question the decision's commercial or strategic merits. However, a court can legitimately inquire whether the decision was *intra vires* – within the scope of the power conferred by the contractual provision that confers the power in question.

The fundamental values of administrative law require decision-making authorities to be 'lawful, to act in good faith, to be [procedurally] fair and to be rational'⁸⁴ in the exercise of their powers. Franchisors are arguably, in a practical sense, in the position of decision-makers *vis-a-vis* franchisees, and exercise authority over them. A court assessing the validity of the exercise of the franchisor's powers under the agreement

⁸² *CCA* sch 2 s 22.

⁸³ *Attorney-General (NSW) v Quin* (1990) 170 CLR 1, 35–6 (Brennan J). See also Greg Weeks, 'Litigating Questions of Quality' (2007) 14 *Australian Journal of Administrative Law* 76.

⁸⁴ French, above n 21, 23.

is essentially involved in a process of construction not dissimilar to that involving the exercise of statutory powers.

B *Good Faith, Lawfulness and Rationality, Errors of Law and Fact Finding and Fairness*

The administrative law principles of good faith, lawfulness and rationality, errors of law and fact finding, and fairness are summarised below. In Part V we demonstrate how these principles could guide franchisors in their exercise of contractual discretions.

1 *Good Faith*

In the administrative law sphere good faith requires that decisions are made honestly and conscientiously.⁸⁵ However, under Australian administrative law, good faith signifies a broader concept than narrow dishonesty. Thus, decisions need to be made within the scope of the grant of power under which they are made. An unlawful delegation of the exercise of a power, or abdication of discretion, would constitute a breach of this requirement. There must be ‘an honest or genuine attempt to undertake the task’ to which the decision-maker has been assigned.⁸⁶ For Lord Russell, unreasonableness was found where delegated laws were ‘partial and unequal in their operation as between different classes: if they were manifestly unjust; if they disclosed bad faith; [or] if they involved such oppressive or gratuitous interference with the rights of those subject to them as could find no justification in the minds of reasonable men’.⁸⁷

Two related criteria for review — when an administrative decision-maker acts under dictation or adopts overly rigid policies — are also relevant in the context of franchising. Franchise systems are hierarchical with national, regional and master franchisees having discretion to make decisions affecting franchisees. Corporate governance principles do not underpin the relationships between players in franchise systems.⁸⁸ Where a decision-maker adopts an overly-rigid policy preventing the exercise of discretion based on the merits of individual cases, this can be challenged through judicial review. For example, a government policy that there would be no additional universities in New Zealand conflicted with a legitimate expectation that a tertiary institution’s application for university status would be properly considered.⁸⁹

⁸⁵ Ibid.

⁸⁶ *NAAP v Minister for Immigration and Multicultural and Indigenous Affairs* [2002] FCA 805 (26 June 2002) [41] (Hely J).

⁸⁷ *Kreuse v Johnson* [1898] 2 QB 91, 99–100 (Lord Russell) cited in *Minister for Immigration and Citizenship v Li* (2013) 249 CLR 332, 365.

⁸⁸ Buchan, above n 9, 101–9.

⁸⁹ *Unitec Institute of Technology v Attorney-General* [2006] 1 NZLR 65. We note that the doctrine of legitimate expectation has been questioned in Australia. See also *Mercury Energy Ltd v Electricity Corporation of New Zealand Ltd* [1994] 2 NZLR 385, as discussed in Janet McLean ‘Contracting in the Corporatised and Privatized Environment’ (1996) 7 *Public Law Review* 223.

It is easy to envisage similar instances occurring within the franchising framework: for example, as occurred in *Burger King*, where the franchisor adopted the strategy of not approving recruitment of franchisees by its Australian area developer in the Burger King system (discussed below).⁹⁰

Courts are reluctant to find the existence of bad faith in its narrow meaning of dishonesty or impropriety, and plaintiffs therefore rarely succeed on this ground. It has on occasion arisen in the franchising context.⁹¹ For administrative lawyers, good faith means more than the ‘mere absence of dishonesty’.⁹² Wade and Forsythe state ‘[a]gain and again it is laid down that powers must be exercised reasonably and in good faith. But, in this context, “in good faith” means merely “for legitimate reasons”’. Contrary to the natural sense of the words they import no moral obliquity’.⁹³

In other words, good faith requires consideration of the ‘purposes and criteria that govern the exercise of the power’.⁹⁴ This in turn necessitates consideration as to the lawfulness of the power’s exercise (its terms and scope) and the rationality of the decision (whether relevant criteria were considered and irrelevant ones discarded). These further grounds for judicial review and their relevance to franchise relationships will be examined next.

2 *Lawfulness and Rationality*

In considering whether a decision-maker has abused a discretionary power, the administrative courts may consider whether the person has acted lawfully and rationally. Lawfulness and rationality often overlap although this bar is also set high:

Lack of rationality may manifest in illogicality that fails to take into account mandatory relevant considerations. In such a case, there may be an error of law for failure to apply statutory criteria or an improper exercise of power. Or it may yield a decision so unreasonable that no reasonable person could have made it. A factual finding without any evidentiary base may be irrational and reviewable ...⁹⁵

We note that courts reviewing administrative decisions regard such matters as capable of measurement. Whether this basis for review is also capable of application to contractual performance and enforcement is contentious with strong opposition

⁹⁰ *Burger King* (2001) 69 NSWLR 558.

⁹¹ *Automasters* [2002] WASC 286 (4 December 2002). *Contra* discussion below of the franchisor’s conduct in *Far Horizons* [2000] VSC 310 (18 August 2000) in Part V.

⁹² French, above n 21, 28.

⁹³ William Wade and Christopher Forsyth, *Administrative Law* (Oxford University Press, 10th ed, 2009) 354.

⁹⁴ French, above n 21, 29.

⁹⁵ *Ibid* 24.

being put forward to such an extension.⁹⁶ We suggest, however, that such opposition largely stems from misapprehension as to whether the grounds for review are the so-called ‘broad’ or ‘narrow’ ‘*Wednesbury*’ grounds.⁹⁷

Thus, Morgan has no quarrel with application of the broader *Wednesbury* criteria to the exercise of contractual powers, writing:

It is orthodox in examining the way the decision has been taken (and so is, in that sense, “procedural”) rather than the quality of the decision arrived at. It requires the courts to decide, by interpretation of the relevant statutory power, which matters must be taken into account by the decision-maker, and which must not: and then to see that these have or have not been considered, accordingly. The court must also consider the motivation behind the decision, to see that this accords with the purpose for which the statutory power has been conferred.⁹⁸

By contrast, Morgan finds the narrow formulation of *Wednesbury* unreasonableness — a decision so unreasonable that no decision-maker could make it⁹⁹ — objectionable ‘because it apparently enables the courts to review the substance of a decision, rather than focusing upon the decision-making process’.¹⁰⁰ We agree that application of this standard to the exercise of contractual powers would be ‘destructive of party autonomy and commercial certainty’.¹⁰¹ We contend that the more orthodox *Wednesbury* formula does have its counterpart in the construction of contractual provisions conferring powers on one party.

Indeed the example cited by Morgan supports our thesis and is not dissimilar to ones found in the franchise arena. *Lymington Marina Ltd v MacNamara*¹⁰² involved a contractual licence and its terms permitting the licensee to sub-licence its rights under it. In construing the wording of the licence the court ruled the only permitted criterion was the suitability of the proposed sub-licensee and that the commercial interests of the marina were not a relevant criterion. The statutory matrix overlaying franchise relationships (for instance a franchisee’s rights to assign its interests) in Australia contains similar criteria.¹⁰³

Further, we cannot take exception to Morgan’s injunction that courts ‘must give full effect to a contractual term drafted to exclude any judicial review of discretion,

⁹⁶ Morgan, above n 38.

⁹⁷ Named after the decision of *Associated Provincial Picture Houses Ltd v Wednesbury Corporation* [1948] 1 KB 223 (‘*Wednesbury*’).

⁹⁸ Morgan, above n 38, 233.

⁹⁹ *Wednesbury* [1948] 1 KB 223, 229 (Lord Greene MR).

¹⁰⁰ Morgan above n 38, 234.

¹⁰¹ *Ibid* 235. See also *Minister for Immigration and Citizenship v Li* (2013) 249 CLR 332 (French CJ) in relation to the narrow version of unreasonableness.

¹⁰² [2007] EWCA Civ 151.

¹⁰³ *Code* cl 20(3).

such as one conferring “absolute discretion”,¹⁰⁴ although we do not believe such broadly worded terms are desirable in franchise agreements as they can corrode relationships and trust. Neither do we support his overall conclusion that ‘the courts should go further and disclaim any jurisdiction to review the exercise of contractual discretions’.¹⁰⁵ Leaving solutions to the market alone, as he suggests, has clearly not worked where franchising is concerned, as evidenced by the large number of inquiries and legislative interventions in Australia.¹⁰⁶ The remainder of this article therefore proceeds on the basis that the broad *Wednesbury* grounds for reviewing the exercise of discretion have relevance to the exercise of contractual powers.

3 *Errors of Law and Fact-Finding*

Although being a common ground for review in administrative law, it may be thought that errors of law are unlikely to arise in a franchise relationship. Consider, however, the requirement in franchise operating manuals that franchisees must comply with all relevant health and safety regulations. An arbitrary decision by the franchisor that these requirements have not been complied with may amount to an error of law. In addition, a ‘conclusion of a fact-finding body can sometimes be so unsupportable — so clearly untenable — as to amount to an error of law’.¹⁰⁷ We suggest this thinking may be extended to decisions made by a franchisor.

Fact-finding is likely to be contentious where franchise relationships are involved. Franchisors and their agents are empowered to make findings of fact concerning aspects of the franchisee’s performance. A ‘carrot and stick’ approach sometimes involves franchisees being rewarded for attaining standards and criteria set by the franchisor, or penalised for failing to attain them. Often, however, the exercise of important rights and remedies hinges on findings of fact by a franchisor; these include the franchisee’s right to renew or assign the franchise and, most importantly, the franchisor’s right to terminate the franchise.

The criteria for fact-finding and grounds for its review devised by administrative lawyers could assist in franchising. It has been said that fact-finding falls into two categories in administrative law. In the first, the decision-maker is given the power to decide whether the requisite state of affairs exists — in other words to find out the actual facts.¹⁰⁸ As long as the fact-finding process is valid the actual finding cannot be challenged as this would amount to questioning its merits as opposed to its legality.¹⁰⁹

¹⁰⁴ Morgan, above n 38, 241.

¹⁰⁵ Ibid 242.

¹⁰⁶ See Schaper and Buchan, above n 1, Table 3 for a full list of reviews into the Australian franchising sector.

¹⁰⁷ *Bryson v Three Foot Six* [2005] NZSC 34, [26]. See also *Australian Broadcasting Tribunal v Bond* (1990) 170 CLR 321, 355–6.

¹⁰⁸ Geoff Airo-Farulla, ‘Reasonableness, Rationality and Proportionality’ in Matthew Groves and HP Lee (eds), *Australian Administrative Law: Fundamentals, Principles and Doctrines* (Cambridge University Press, 2007) 212, 216.

¹⁰⁹ Ibid.

In the second category, however, the power itself is contingent on the objective existence of the requisite facts:

the requisite state of affairs is a ‘jurisdictional’ fact on which the power’s existence depends. A decision maker who acts on the basis of an incorrect finding that the fact exists has made a legal error about the power’s existence. Similarly, a decision maker who refuses to act, on the basis of an incorrect finding that the fact does not exist, has also made a legal error about the power’s existence.¹¹⁰

The distinction has arisen in franchising disputes such as the *Far Horizons* case in Part V.

4 *Fairness*

Administrative law requires that decisions be reached fairly, meaning that they are made impartially and are seen to be impartial, after affording a proper opportunity to those affected to be heard.¹¹¹

We can also reflect on the main rationale for the bias rule which is to encourage *good* decision-making, that is, rational decisions based on accurate findings of fact.¹¹² Such decisions are inherently likely to be superior to those influenced by ulterior considerations. Of course, in the franchising context, the franchisor’s self-interest may well be one relevant consideration although it ought not to be the only one. Researchers have pointed to the perverse economic incentives franchise relationships afford for inefficient decision-making by franchisors that are able to leverage the sunk costs of franchisees.¹¹³ This explains why franchisees may remain in business despite incurring losses.

Besides impartiality, the second major requirement of fairness is the requirement to follow due process and to afford the subject of the decision an opportunity to put forward their case. As Cameron Stewart states:

Procedural fairness is due where a person enjoys a substantial benefit and expects that it will continue... if a decision is made to take away the benefit, the decision maker is bound to hear the side of the person enjoying the benefit before they make the decision.¹¹⁴

¹¹⁰ Ibid 217–18.

¹¹¹ French, above n 21, 15, 23.

¹¹² Matthew Conaglen, ‘Public-Private Intersection: Comparing Fiduciary Conflict Doctrine and Bias’ [2008] *Public Law* 58, 73.

¹¹³ See generally Hadfield, above n 6, 951–2; Roger D Blair and Francine Lafontaine, *The Economics of Franchising* (Cambridge University Press, 2005).

¹¹⁴ Cameron Stewart, ‘The Doctrine of Substantive Unfairness and the Review of Substantive Legitimate Expectations’ in Matthew Groves and H P Lee (eds), *Australian Administrative Law: Fundamentals, Principles and Doctrines* (Cambridge University Press, 2007) 280-1.

The application of this principle to the circumstances where decisions are made by franchisors that affect franchisees is obvious. This is the case not only when penalties are imposed on a franchisee for non-compliance with the system, but in a myriad other instances where decisions are made by a franchisor that impact substantially on the benefits conferred by the grant.¹¹⁵

Where a franchisor exercises the right to terminate a franchise it is a requirement in Australia under the *Code* that the franchisee is given an opportunity to remedy the deficiency.¹¹⁶ This is not the same as a right to a hearing, but it is implied that the franchisee will have the opportunity to communicate the fact and degree to which it has remedied any deficiency. In *Automasters*, discussed in Part V, it transpired that the franchisor had pre-judged the question of termination, being motivated by extraneous factors. The case squarely satisfies even the subjective requirement of honesty advocated by Hooley as a basis for controlling contractual discretion.¹¹⁷ By way of contrast, in *Far Horizons*, the franchisor was not only transparent as to its decision-making processes but afforded ample opportunity to the franchisee to put its case.

A major tenet of administrative law is the balance struck by the courts between the decision's fairness and the public interest in upholding the administrator's decision, even when it is unfair.¹¹⁸ In the franchise context public interest is akin to the interests of the franchise system as a whole, assuming the system is viable. Sometimes, a decision may appear to be unfair to a particular franchisee. When viewed from the point of view of the entire system, however, the decision may be justified. What this also suggests is that, when undertaking decisions prejudicial to its franchisees, a franchisor ought to consider not just its self-interest but rather the integrity of the franchise system. This should be balanced against factors relevant to the franchisee such as the amount of its non-recoverable sunk costs.

C Accommodating Flexibility

Administrative law allows administrative decision-makers the flexibility to innovate and to adopt changes dictated by policy needs and other considerations. A decision-maker will, for instance, often amend guidelines as to how to comply with a policy. Once again, we believe that the framework provided by administrative law is adaptable to afford franchisors the freedom to make changes in response to market conditions, and to innovate, whilst ensuring that the value of fairness is preserved. As mentioned earlier, Aronson notes that 'the majority in the High Court of Australia decision *NEAT Domestic Trading Pty Ltd v AWB Ltd*¹¹⁹ "specifically reserved for future consideration the question of whether a private

¹¹⁵ For instance to vary the territory or increase royalties and advertising levies.

¹¹⁶ *Code* cl 21(2)(b).

¹¹⁷ Hooley, above n 2.

¹¹⁸ Stewart, above n 114, 283.

¹¹⁹ (2003) 216 CLR 227, 297 [49]–[50] (Gleeson CJ, McHugh, Hayne and Callinan JJ).

sector body might be reviewable”.¹²⁰ We suggest that franchisors present this opportunity.

V FRANCHISE DISCRETIONS THROUGH AN ADMINISTRATIVE LAW PRISM

Franchisors need clarity; so do franchisees. There is some English authority for the view that ‘administrative law principles are applicable in the consideration of [contract based] discretions’.¹²¹ For example, in *Paragon Finance Plc v Nash*¹²² the English Court of Appeal had to decide whether a mortgagee’s discretion to vary interest rates was subject to an implied term fettering its exercise. The Court found there was an implied term that the mortgagee was bound not to exercise the discretion ‘dishonestly, for an improper purpose, capriciously or arbitrarily’.¹²³ An example of capricious behaviour was given where interest rates were raised because of the colour of the borrower’s hair and an example of an improper purpose would be where interest rates were raised ‘to get rid of’ a nuisance borrower.¹²⁴ Hooley notes, in the context of genuinely negotiated contracts that ‘it can rarely be the intention of the parties that [apparently unfettered contractual discretion] may be exercised without restraint’.¹²⁵ Later English cases have cast doubt on the width of the Court’s dicta however.¹²⁶

On the other hand it is now beyond doubt that in Australia, at least, the prevailing common law and statutory matrix have in substance resulted in principles akin to those existing in administrative law being applicable also in the franchising context. For example the *Code* stipulates that franchisors must not unreasonably withhold consent to the transfer of a franchise,¹²⁷ and stipulates criteria that may be considered by a franchisor in withholding or giving assent for a franchisee to transfer the franchise. The list¹²⁸ contemplates the addition of other criteria in the franchise agreement.

¹²⁰ Mark Aronson, ‘Is the ADJR Act Hampering the Development of Australian Administrative Law?’ (2005) 12 *Australian Journal of Administrative Law* 79, 88–9. See also for a discussion of *NEAT Domestic Trading Pty Ltd v AWB Ltd* (2003) 216 CLR 277. The case is of particular relevance to franchising, as the defendant was a statutorily created monopoly. A franchisor that is a supplier to its franchisees enjoys a role as a privately created monopoly vis-a-vis its franchisees. Its monopoly activities are subject to the lightest regulatory scrutiny via the process under s 47 of the *CCA* for notification of exclusive dealing that, without having been notified, would be a breach of the Act.

¹²¹ Peden, above n 37, 238.

¹²² [2002] 2 All ER 248.

¹²³ *Ibid* 261 (Dyson, Astill and Thorpe LLJ).

¹²⁴ *Ibid*.

¹²⁵ Hooley, above n 2, 67.

¹²⁶ See, eg, *Compass Group UK and Ireland Ltd (t/a Medirest) v Mid Essex Hospital Services NHS Trust* [2013] EWCA Civ 200.

¹²⁷ *Code* cl 20 (2)–(3).

¹²⁸ Relating to such matters as the qualifications and suitability of the transferee and the transferor’s discharge of all outstanding obligations to the franchisor.

How far such additional criteria may go before being ultra vires the requirement to be ‘reasonable’ is pertinent to the discussion undertaken in this article.

Jeannie Marie Paterson notes that ‘courts have drawn on principles familiar in the context of judicial review of the exercise of administrative power, to require contracting parties to conform to basic standards of good decision-making’.¹²⁹ A court may find that the exercise of discretion is impliedly subject to constraints. It is in this context that the legal principles informing the exercise of the franchisor’s discretionary power might draw on the criteria traditionally drawn upon in judicial review cases. We now consider examples of how the principles outlined in Part IV could clarify how the same issues may be resolved in complex private law franchise relationships.

*Automasters*¹³⁰ is a case spanning practically all the grounds traditionally pertinent to judicial review, including good faith, lawfulness, rationality and fairness. A franchisor had sought to terminate a franchise agreement despite an independent quality assessment recommending otherwise, and even though it was not satisfied the information on which the decision was based was accurate. Furthermore, the franchisor was motivated by irrelevant matters.¹³¹ Finally, the decision was procedurally unfair as the franchisor withheld details of an independent quality assessment report favourable to the franchisee, and failed to attend mediation as required by the *Code*.

Unsurprisingly, the Court found the franchisor acted unconscionably under s 51AC of the *TPA*. Had the franchisor been guided by the grounds of judicial review it would have been clear which considerations it could have taken into account.

An application of the good faith concept in the franchising arena can be seen in a United States decision. In *Dunfee v Baskin-Robbins Inc*,¹³² site location decisions under the franchise agreement remained exclusively with the franchisor, and any site relocation had to be authorised by a Baskin-Robbins Vice President. The plaintiff, whose existing site had become unsuitable, sought relocation. The Vice President was never consulted. Instead, the District Manager, after consulting with Baskin-Robbins’ Divisional Manager, advised (on the basis of erroneous information) that the relocation was not possible. Although the plaintiff succeeded on the basis the franchisor was in breach of the covenant of good faith and fair dealing implied into commercial dealings in the United States,¹³³ it would equally have been possible to challenge the outcome as an unlawful delegation were administrative principles applied. Besides improper delegation, the decision to deny relocation was also procedurally unfair under administrative law criteria: not only did Baskin-Robbins fail to

¹²⁹ Jeannie Marie Paterson, ‘Implied Fetters on the Exercise of Discriminatory Contractual Powers’ (2009) 35 *Monash University Law Review* 45, 47.

¹³⁰ [2002] WASC 286 (4 December 2002).

¹³¹ *Ibid* [210]. Justice Hasluck found these to be the franchisee’s laying of criminal charges against a former manager, one of the franchisor’s favourites and the franchisee’s complaint to the Australian Competition and Consumer Commission.

¹³² 720 P 2d 1148 (Mont, 1986).

¹³³ Now found in *Uniform Commercial Code*, 1 UCC § 304 (2001).

follow its own procedure for considering site relocations, but the franchisee was given inaccurate information as to the basis on which the decision had been made.

In *Dunfee v Baskin-Robbins Inc* it was also found that an alternative arguable basis for the liability of the franchisor was that it owed fiduciary duties to the franchisee in respect of the head lease. Despite discretion and power imbalances being a major focus of fiduciary duties, the imposition of such duties within franchising relationships has been rare.¹³⁴ Cases where fiduciary duties have been found to arise are outliers and involve, usually, aspects peripheral to the franchise agreement itself. One such example (as discussed below) is *Burger King*,¹³⁵ which involved a franchisee being cut out of a prospective joint venture involving a third party and the franchisor, amongst other matters.

Even here, the analogy with public law principles affords an opportunity for comparison. Although there have been instances where decisionmakers have been found to be in the position of a fiduciary these have been restricted to a narrow range of circumstances such as where an administrative discretion to apply funds exists.¹³⁶ An example was where a council was found to owe a fiduciary duty to ratepayers as to how rates moneys were spent.¹³⁷ In the franchising context it will be argued below that the enhanced transparency mandated by the disclosure provisions of the *Code* and the accountability this engenders largely removes the pressure for courts to import fiduciary duties into franchise relationships. On the other hand the *principle* of transparency can be seen to underlie both fiduciary relationships and administrative law in these instances.

A franchisor's discretionary contractual powers are often worded in identical terms to statutory powers employing unmistakably discretionary language such as 'may'. Consider, for example, the power to terminate a franchisee's grant for breaches of the agreement. It has been observed in relation to administrative law that '[e]ven the most discretionary powers are not taken to be arbitrary powers'.¹³⁸ In other words, 'discretionary powers must be exercised according to legal principles'.¹³⁹ We suggest that the principle could be similarly applicable where powers emanate from franchise agreements. In considering the *lawfulness* of a franchisor's actions, consideration

¹³⁴ A claim that the franchisor owed fiduciary duties in connection with obtaining a lease for the franchisee was unsuccessful in *Blackmore Laboratories Ltd v Diskin Pty Ltd* [1989] NSWSC (20 December 1989) [7] where McLelland J held that the franchise agreement did not permit such a term to be implied.

¹³⁵ (2001) 69 NSWLR 558.

¹³⁶ See Christine Brown, 'The Fiduciary Duty of Government: An Alternate Accountability Mechanism or Wishful Thinking?' (1993) 2(2) *Griffith Law Review* 161, 175.

¹³⁷ *Bromley LBC v Greater London Council* [1983] AC 768, 815 (Lord Wilberforce).

¹³⁸ Matthew Groves and H P Lee, 'Australian Administrative Law: The Constitutional and Legal Matrix' in Groves and Lee (eds), *Australian Administrative Law: Fundamentals, Principles and Doctrines* (Cambridge University Press, 2007) 3.

¹³⁹ Louise Longdin, *Law in Business and Government in New Zealand* (Palatine Press, 2006) 119.

ought to be given to the terms in which the franchisor's powers are framed and the constraints expressly or implicitly imposed upon them.

In the franchising context, lawfulness would require examining whether the franchisor's actions are authorised by the franchise agreement. This is a matter of construction but not always a straightforward one.¹⁴⁰ The franchisor's decision would be lawful by analogy with an administrative law paradigm, provided it complied with the framework created by the grant of the power under which the decision is made.¹⁴¹ This would take account of the kinds of changes in the external environment contemplated, for instance, by the operating manual.

A somewhat different issue arises when the franchisor's conduct does not emanate from the agreement, operating manual or other document but amounts to simple commercial pressure-tactics and leveraging off the franchisee's weak *ex ante* bargaining position. While we would not suggest stifling the normal 'give and take' of commerce or negotiating tactics that occur in the commercial world,¹⁴² the reality is that opportunistic behaviour by franchisors is a concern where much of the interaction between franchisor and franchisee takes place 'off the [formal] contract'.¹⁴³

Where the franchisor's conduct is connected to the exercise or threatened exercise of discretionary powers, review of the franchisor's actions ought to be permitted. It is precisely in these circumstances that the public law analogies are useful. A focus on the terms of the contractual discretion lends greater certainty than reliance on the 'unconscionable conduct' standard which, ultimately, suffers from the same deficiency as the Chancellor's foot.

A franchisor may have a contract-based discretion to determine facts and to make a decision based on its findings. For example, in *Far Horizons*¹⁴⁴ a franchisor's decision not to grant an existing franchisee an additional store licence was found

¹⁴⁰ See, eg, *Maranatha Ltd v Tourism Transport Ltd* (Unreported, High Court of New Zealand, Rodney Hansen J, 3 April 2007) where a franchisor decided that the cost of an airport licence fee (which the franchisor had previously absorbed) should in future be passed on to franchisees and ultimately to customers through a 'user pays' surcharge when they used the franchisees' airport shuttle services. The franchise operating manual was altered to require that the user pays surcharge set by the franchisor would apply. In addition, the franchisees were required to display and use the franchisor's current maximum fare schedule. This case has been analysed in Gehan Gunasekara, 'Standard Form Commercial Contracts, Unilateral Variation and the Legal Response: the Case of Franchising' (2007) 13 *New Zealand Business Law Quarterly* 263. In *Meridian Retail Pty Ltd v Australian Unity Retail Network Pty Ltd* [2006] VSC 223, Dodds-Streeton J determined that the franchisor had acted within the discretionary wording of the franchise agreement, and had not acted in bad faith.

¹⁴¹ French, above n 21, 23.

¹⁴² *Australian Competition and Consumer Commission v G C Berbatis Holdings Pty Ltd* (2003) 214 CLR 51.

¹⁴³ Hadfield, above n 6, 928.

¹⁴⁴ [2000] VSC 310 (18 August 2000).

to have been made in good faith. An equally valid interpretation of the franchisor's power to grant the licence would be to ask whether the decision had been made in a *fair* manner? It had been. The franchisor, McDonald's, has a procedure for determining which franchises met the criteria for additional stores: regular QSC¹⁴⁵ assessments with feedback being given, and franchisees being graded. Under McDonald's documented policy:

An 'expandable' franchisee was one whose existing units had regularly earned at least a B grade on QSC. He or she also had to have sufficient financial and management resources to support expansion, in addition to a good record of community involvement and an attitude of cooperation with the company and other franchisees.¹⁴⁶

In *Far Horizons*, an existing licensee would qualify as eligible to take a further licence where they satisfied the McDonald's requirements in respect of seven specified criteria. One of these was the extent to which the franchisee had demonstrated a 'positive' outlook on McDonalds and its system, a criterion which had not been met by the plaintiff.¹⁴⁷ The analogy with judicial review suggests that, provided consideration had been given to the listed criteria, it would be injudicious for a court to question a franchisor's determination of the matter. The decision in *Far Horizons* indicates the judge was cognisant of precisely this danger:

My task is not to determine whether Mr Tregurtha was correct in his assessment of Mr Hackett on Positive Contribution. I am to decide whether there was material upon which Mr Tregurtha could have made the decision he reached and, even so, whether the decision was based on irrelevant or improper considerations.¹⁴⁸

Certain procedural steps must be taken before a franchisor can exercise the right to terminate.¹⁴⁹ Significantly, courts have found as a matter of construction that termination has not been reasonable where the franchisor failed to give the franchisee prior notice and an opportunity to rectify breaches.¹⁵⁰

It might be questioned whether any instances arise in franchise relationships involving the second category of *fact-finding*; that is, the franchisor's right to exercise the power in question depends on the prior existence of the fact from an objective standpoint.

¹⁴⁵ The acronym means Quality, Service and Cleanliness.

¹⁴⁶ John F Love, *McDonald's: Behind the Arches* (Bantam, revised ed, 1995) 398.

¹⁴⁷ [2000] VSC 310 (18 August 2000) [108].

¹⁴⁸ *Ibid* [70].

¹⁴⁹ Steps are usually set out in the relevant individual franchise agreement and, as applicable, in cl 27, 28 or 29 of the *Code*.

¹⁵⁰ See generally *Dymocks Franchise Systems (NSW) Pty Ltd v Todd* [2004] 1 NZLR 289, 309 (Lord Browne-Wilkinson), affirming the statements made by the New Zealand Court of Appeal; in this regard, see *Bilgola Enterprises Ltd v Dymocks Franchise Systems (NSW) Pty Ltd* [2000] 3 NZLR 169, 184 (Henry J).

An example is *KA Old v Snack Systems Limited*,¹⁵¹ where the franchisor's decision to withhold consent to the assignment was effectively quashed because a breach of the agreement had not been objectively established.

A separate criterion for review would be whether the franchisor acted *fairly*? Such an approach would offer an alternative to the legislative responses to reducing asymmetry that have been adopted in Australia. These have focused on enhanced disclosure, for example, of the circumstances in which franchisors have previously unilaterally varied agreements.¹⁵² This approach is reactive rather than prospective and offers less protection to franchisees than would simply requiring franchisors to act fairly.

The first element of administrative fairness – that there is no bias in decisions – is problematic where franchisors, often, are their own arbiters. For example a franchisor might determine whether franchisees have complied with the system or met franchisor-set criteria for obtaining some benefit. This is particularly the case when a franchisor has, as is likely, a pecuniary interest in the outcome. The franchisor may thus be incentivised to decide in a particular manner.¹⁵³ In *Picture Perfect v Camera House Ltd*,¹⁵⁴ for example, the franchisor used its powers to prescribe approved suppliers to change the franchisees' supplier of film products to a related company of the franchisor following a change in its ownership. The Court accepted, in interlocutory proceedings, that an arguable case existed that the purpose of the contractual power was to enable bulk buying advantages for franchisees and was not solely to benefit the franchisor or its related company. This was an instance of possible bias. The principle is thus relevant in the franchise context.

Ascertaining whether some types of decision might have been biased has been made easier by the *Code*. Franchisors are required to disclose such matters as franchisor ownership of interests in suppliers from which franchisees are required to acquire goods or services, and whether franchisors will receive any financial benefits from suppliers.¹⁵⁵ This does not prevent franchisors from making biased decisions about matters that fall outside the wording of the *Code*. An example is the decision by REDgroup Retail Pty Ltd, owner of franchisors Angus & Robertson, to appoint administrators when book retailing was in decline. The administrators concluded 'it is difficult to maintain an argument that the Group was insolvent for any material period prior to 17 February 2011'.¹⁵⁶ Administrators are placed in an awkward

¹⁵¹ (Unreported High Court of New Zealand, Master Towle, 10 August 1994).

¹⁵² *Code* cl 17A (inserted by *Trade Practices (Industry Codes-Franchising) Amendment Regulations 2010 (No 1)* (Cth)).

¹⁵³ Longdin, above n 139, 129.

¹⁵⁴ [1996] 1 NZLR 310.

¹⁵⁵ *Code* sch 1 cl 9(c), (j).

¹⁵⁶ S Sherman, J Melluish and J Lindholm, 'REDgroup Retail Pty Limited and Associated Companies (Administrators Appointed): Report by Administrators Pursuant to Section 439A(4)(a) of the *Corporations Act 2001*', (Ferrier Hodgson, 25 July 2011) 6.

position as they are bound by the *Code* but as previously noted, have concurrent overriding statutory duties under the *Corporations Act 2001* (Cth).

The disclosure obligations of the *Code* serve another purpose. Although they constitute a discrete obligation, breach of which may result in the granting of statutory remedies,¹⁵⁷ it has been observed from the public law standpoint that ‘disclosure is not an obligation, but rather a mechanism for obtaining insulation against the effects of bias law’s disqualification rule’.¹⁵⁸ It is unsurprising, then, that much franchise regulation is aimed at disclosure, particularly where conflicts are perceived to arise through franchisors having economic interests in third parties that franchisees are required to buy from. Disclosure, in these instances, removes the sting of any complaint that may otherwise arise, confirming that Australian franchise regulation conforms to the bias paradigm.

The objection that franchisors will always be found to be biased due to having a significant pecuniary interest in the exercise of their discretion can be met by the observation that, as is the case in the administrative law field, the basis for judicial intervention rests on a different ground such as improper purpose or taking into account an irrelevant consideration. Two examples will suffice.

The first example where bias arose was *Burger King*,¹⁵⁹ the culmination of a protracted dispute between Burger King and its Australian franchisee/area developer. Under a ‘Development Agreement’, Hungry Jacks was required to develop a stipulated number of restaurants each year. Having resolved to remove Hungry Jacks and resume control of the chain directly, Burger King imposed a ‘third party freeze’ by not approving recruitment by Hungry Jacks of franchisees. This ensured breach, by the latter, of its Development Agreement. Although the New South Wales Court of Appeal held that the agreement was subject to implied terms of cooperation, reasonableness and good faith, the case can also be seen as an example of procedural unfairness through lack of impartiality, in addition to irrationality due to the franchisor being influenced by improper considerations.

By contrast, the franchisor in *Far Horizons*, discussed above, ensured that the decision not to offer the additional licence was procedurally fair. Thus, the

decision as to Positive Contribution was not that of Mr Cork [a regional manager who had dealt with the franchisee]; it was [McDonalds director of operations] Mr Tregurtha’s decision. There is no evidence of personal antipathy between Mr Tregurtha and Mr Hackett...no evidence that Mr Tregurtha’s decision was the result of some direction from above or that it was affected by his knowledge that Mr Cork, and perhaps those above him, wanted to discipline Mr Hackett.¹⁶⁰

¹⁵⁷ See generally Australian Consumer Law sch 2 ch 5; *Master Education Services Pty Ltd v Ketchell* (2008) 236 CLR 101.

¹⁵⁸ Conaglen, above n 112, 69 (citations omitted).

¹⁵⁹ (2001) 69 NSWLR 558.

¹⁶⁰ *Far Horizons* [2000] VSC 310 (18 August 2000), [69].

VI DOCTRINAL ISSUES

Two doctrinal matters will be addressed before we conclude. First, administrative law might be said to be distinguishable from contract law due to the role played by consent in the case of the latter. However, franchise agreements do not reflect a negotiated bargain between parties; they reflect the intention of the drafting party.¹⁶¹ Just as legislative intent is that of the drafter at the time of enactment and cannot readily be changed *ex post*, the same applies in the sphere¹⁶² of standard form relational contracts. This is even more so where the legislative provision is of wide ambit, conferring discretion on a party to enact subsidiary legislation: the discretion given should not be unfettered and absolute, whether the provision conferring it emanates in contract or statute.¹⁶³ Any scrutiny of the exercise of discretion must, likewise, examine the purpose for which the discretion was conferred.

Some might argue that an application of substantive standards not apparent on the terms of the contract undermines the balance of interests struck by the parties (as encapsulated in the express terms of the franchise agreement). Therefore, such standards interfere with the basic autonomy of the contracting parties. But, as we have seen, franchise agreements are essentially incomplete and are incapable of encapsulation through express terms alone.¹⁶⁴ It may be then that the balance of interests struck by the parties requires resort to the very types furthering the fundamental purpose of the contract rather than detracting from it.

A second, related issue is that courts often apply a de facto ‘business judgment rule’ to decisions made by franchisors, effectively quarantining them from scrutiny.¹⁶⁵ To Hadfield, this approach by courts is flawed as it fails to take account of the economic imperatives present in the relational arrangements that underpin franchising.¹⁶⁶ The rule is also inappropriate as it focuses exclusively on the franchisor’s interests (‘one half’ of the franchise relationship in Hadfield’s words) as opposed to recognising the mutually co-operative nature of the interests that underlie the business format.¹⁶⁷ We agree with Hadfield in this regard.

¹⁶¹ Spencer, above n 18, 35.

¹⁶² See generally Stephen J Choi and G Mitu Gulati, ‘Contract as Statute’ (2006) 104 *Michigan Law Review* 1129.

¹⁶³ See *Minister for Immigration and Citizenship v Li* (2013) 249 CLR 332, 348–9 [23]–[25] (French CJ).

¹⁶⁴ Hadfield, above n 6.

¹⁶⁵ *Ibid* 980–4.

¹⁶⁶ *Ibid* 983.

¹⁶⁷ *Ibid*.

VII CONCLUSION

Writing extra-judicially, the Chief Justice of the High Court of Australia observed:

Nature demonstrates that apparent complexity can be generated by uncomplicated rules. Fractal forms based on simple interactions are to be found in plants, animals, clouds, snowflakes, population patterns and galaxies. ... Like organic and inorganic forms in nature, the apparent complexities of different areas of the law, whether they be statute or judge-made, are frequently generated by a few underlying principles.¹⁶⁸

In this article, we have shown the truth of this statement in relation to the basic principles underlying administrative law and the principles of contractual interpretation underlying franchising agreements. We have shown that standards akin to those found in public law have been applied to the exercise of contractual powers under franchise agreements. Corcoran identifies that ‘public law is the most obvious area to impose statutory good faith obligations [in legal relationships] because the relative position of the actors tend to be such that the possibilities for abuses of power are strong’.¹⁶⁹

This article has shown that the possibilities, and the incentives, for abuses of power by franchisors (and even master franchisees), are equally compelling.

Sir Robin Cooke has stated that ‘the judicial role is ... to ensure that those responsible for decisions in the community do so in accordance with law, fairly and reasonably’.¹⁷⁰ We contend this is a principle capable of wider application, and ought to inform the interpretation of contractual powers of decision where a decision-maker acts in an administrative capacity. We have demonstrated the application of the principle to franchising relationships which fall squarely within this category.

The advantage of an approach based on administrative law principles is that it avoids having to determine whether the implication is through law or by fact — a distinction that has bedeviled Australian courts.¹⁷¹ It also relieves the courts of having to determine whether the relationship between franchisor and its franchisees is a fiduciary one. If it were then each would be bound to take account of the ‘legitimate interests of the other party’.¹⁷² The common law approach, and that enshrined in the 2014 *Code*, fall short because both provide an escape hatch for the contracting party that can justify its lack of good faith on the ground that the exercise of the particular

¹⁶⁸ French, above n 21, 15.

¹⁶⁹ Corcoran, above n 39, 11.

¹⁷⁰ R Cooke ‘The Struggle for Simplicity in Administrative Law’ in M Taggart (ed), *Judicial Review of Administrative Action in the 1980s* (Oxford University Press, 1986) 5, 16–17.

¹⁷¹ See generally discussion in the cases cited by Dixon, above n 50, 235–7.

¹⁷² Corcoran, above n 39, 11.

discretion was for ‘legitimate commercial interests.’¹⁷³ This justification does not support a discretion evaluated against administrative law benchmarks.

At the same time, recourse to administrative law approaches preserves many of the best features of each mechanism by allowing the factual circumstances of each case to be taken into account along with broader issues of policy. In *Council of the City of Sydney v Goldspar Australia Pty Ltd*, Gyles J observed that

[t]he best way for a single judge to travel through this thicket [of varying opinions about implying terms as to reasonableness and good faith] is to concentrate upon the particular contractual provision in question, the particular contract, in the particular circumstances of the case.¹⁷⁴

This indeed is the same process that occurs when a court reviews a decision made by an administrator in a public law context.¹⁷⁵

In the franchising context the franchisor’s powers and discretions are usually stated in very broad terms. Does this mean the powers they confer are unlimited? As Shellar JA stated in *Alcatel Australia Ltd v Scarcella*, employing the reasoning of Barwick CJ in *Pierce Bell Sales Pty Ltd v Frazer*:¹⁷⁶

[i]f a contract confers power on a contracting party in terms wider than necessary for the protection of the legitimate interests of that party, the courts may interpret the power as not extending to the action proposed by the party in whom the power is vested or, alternatively, that the powers are being exercised in a capricious or arbitrary manner for an extraneous purpose, which is another way [sic] of saying the same thing.¹⁷⁷

The principles governing administrative law are generally well understood, whatever labels might be attached to them. Ultra vires has been described as the central principle of administrative law.¹⁷⁸ A logical application has been to examine what actions of a franchisor are within the powers conferred by the agreement, taking into account restrictions that may be imposed by the *Code*. We have seen that other principles of wide application in both public and private spheres include the requirement to act rationally, honestly and in a manner that is procedurally fair. In relation to franchising, we have argued that the criteria for judicial review provide an alternative framework for the courts to review the exercise of contractual rights by franchisors, in addition to that provided by the much-misunderstood doctrine of good faith in contractual performance and enforcement.

¹⁷³ *Competition and Consumer (Industry Codes — Franchising) Regulation 2014* (Cth) sch 1 div 3, cl 6.

¹⁷⁴ (2006) 230 ALR 437, 499.

¹⁷⁵ See generally Weeks, above n, 83.

¹⁷⁶ (1973) 130 CLR 575, 587.

¹⁷⁷ (1998) 44 NSWLR 349, 368.

¹⁷⁸ Wade and Forsyth, above n 93, 35.

We propose that clarity as to how discretion will be exercised enables both parties to align their expectations accurately. Franchisees need to appreciate that good faith and fairness cannot apply at all times, and to all parties. They do, however, need to know when it is reasonable to expect a franchisor will operate in good faith and fairly, and what that behaviour looks like. Neither the common law concept of good faith, nor the 2014 statutory measure can be the panacea their protagonists believe they will be. If, on the other hand, a franchisor's conduct was able to be assessed against the benchmarks of administrative law principles, their discretions would be able to remain in place – no change would be required to their standard contracts. But, there would be clear boundaries to curtail how they could interpret and use discretions.

Much of the uncertainty and conceptual confusion still surrounding good faith dissipates when it is observed that decisions based on it are in fact based on a more fundamental foundation of principles that also underlie administrative law. These principles would afford greater certainty to franchisors, franchisees and the courts when a dispute arises over the manner in which a franchisor exercises discretion. At the very least, it gives flesh and blood to the abstract notion of good faith. From a practical standpoint, being able to draw on administrative law paradigms in addition to contractual ones would help mediators and courts in assessing which actions of franchisors are legitimate.

In this article, we have shown that the ability to balance competing principles allows flexibility to courts when devising solutions in specific situations — such as relational contracts. As principles such as fairness under administrative law can be given greater or lesser weight than other competing principles — such as the common law principle of sanctity of contract — flexibility can be afforded to courts beyond strict adherence to the doctrine of *stare decisis* and traditional contract law doctrine.

We acknowledge that ‘judicial review is not quite as powerful in practice as it is in theory’.¹⁷⁹ However, the existence of the standard for reviewing unreasonableness is comforting. We believe it is timely for a conversation to take place between administrative law and private law. Franchise contracts provide an ideal starting place.

¹⁷⁹ H W Arthurs, ‘The Administrative State Goes to Market (and Cries “Wee, Wee, Wee” All the Way Home)’ (2005) 55 *University of Toronto Law Journal* 797, 798.

