WFD Wollermann FRANCHISE DEVELOPMENTS

FINANCIAL DISCLOSURE UNDER THE FRANCHISE CODE - 2020

The Franchising Code of Conduct (“the Code”) which commenced operation on 1 January 2015 required greater financial disclosure by a franchisor.

Decisions need to be made early on, when the franchise documents are being drafted as to what financial disclosure will be given as these matters can delay the roll out of the franchise model

In some cases, there are options to be considered acting for a new or foreign Franchisor ‘s and an existing Franchisors may not wish to disclose their confidential financial accounts to prospective franchisees.

ANNUAL DISCLOSURE REQUIREMENTS:

All Franchisors have four months from the end of each financial year (31st October) to review, update and issue their disclosure documents to their Franchisees and disclose material changes, changes to their existing franchisees and key events such as terminations and defaults.

The Franchisors Director must also provide a statement of financial solvency and include their financial reports for the last two trading years prepared in accordance with the Corporations Act

MARKETING FUND:

Marketing fund financial statement must also be supplied to Franchisees by the 31 October in each year with a marketing fund audit report unless clause 15(2) of the Code applies that is, 75% of franchisees agree **not** to have the fund audited for that financial year. There are fines and penalties for breaches of the Code by the ACCC

WHERE THE FRANCHISOR HAS NOT EXISTED FOR THE PREVIOUS 2 FINANCIAL YEARS:

The Franchisor must supply the following:

- a statutory declaration of solvency by a Director; and
- an independent audit report by a registered Company auditor of the entity’s solvency as at the date of the Directors declaration (“**solvency audit certificate**”).

These are mandatory requirements under the Code and cannot be avoided by franchisors.

- The audit certificate must be provided by a Registered Company Auditor and not just the clients accountant.

- To support the Directors solvency statement the auditor will be required to audit the financial records of the Company, the cost of which ranges from $1,000 - $5,000 depending on the Auditor, complexity of the corporate structure and the years in operation.

The cost to new franchisors to establish their system has substantially increased due to these requirements and there can also be some difficulty in finding an auditor who is prepared to provide the solvency audit certificate.

WFD Wollermann FRANCHISE DEVELOPMENTS

FRANCHISOR IN EXISTENCE FOR MORE THAN TWO YEARS:

A Franchisors Director must provide a statement of solvency as at the end of the last financial year giving the directors opinion as to whether they have reasonable grounds to believe the franchisor will be able to pay its debts as and when they fall due, (that is, the company is solvent).

WHERE THE FRANCHISOR DIDN'T EXIST AS AT THE END OF THE LAST FINANCIAL YEAR:

The Directors statement must be given, as at the date of the Disclosure statement. The Franchisor must provide the financial reports of the franchisor for each of the last two completed financial years (or foreign equivalent financial reports) pursuant to Section 295 and 297 of the *Corporations Act 2011*.

CONSOLIDATED ENTITIES:

If a franchisor is part of a consolidated entity which provides audited financial reports (or the foreign equivalent) and the franchisee requests those financial reports, the franchisor must provide financial reports for each of the last 2 completed financial years prepared by the consolidated entity.

Alternatively, the franchisor may provide a director's statement of solvency supported by a Registered Company Audit (solvency statement) or (foreign equivalent) within four months after the end of the financial year.

Franchisors' may be reluctant to provide copies of their financial reports for a variety of reasons as they may contain confidential and/or commercially sensitive information.
In this case the franchisor will need to provide the auditors solvency certificate supporting the director's declaration.

WHERE THE FRANCHISOR (AND/OR A CONSOLIDATED ENTITY) WAS INSOLVENT IN EITHER OF THE LAST TWO FINANCIAL YEARS THE FRANCHISOR MUST PROVIDE:

- a statement by a Director of the period it was insolvent in the 2 years;
- a statutory declaration by the director of its current solvency; and
- supported by an audit solvency certificate.

CONTINUING DISCLOSURE:

The Code also requires Franchisors to provide continuing disclosure to franchisees if there have been any changes to the company's solvency between the date of the disclosure document and the date it is actually provided to a franchisee.

SUMMARY - WHAT DOES THIS MEAN TO FRANCHISORS?

- For existing Franchisors ensure your financial statements and accounts are up-to-date and completed at the earliest opportunity after the expiry of each financial year;

- The days when a company could delay completion of their financial accounts until March or April the following year are now long gone;
- Franchisors need to engage their accountants early and ensure their financial reports and audit statements are prepared and finalized well prior to 31st October in each year; and
- Franchisors need to ensure they are on top of their management accounts and the directors and management team are aware of these added compliance requirements, and systems are in place to meet them.

A failure to do so, can put a Franchisor at risk of financial penalties under the Code but also delay their ability to roll out new Franchises!

CONTACT:
Robert Toth | rtoth@franchisedevelopments.com.au
Accredited Commercial Law and Franchisee Specialist | Member of the Franchising Council of Australia (FCA) | Member of the International Franchise Lawyers Associations (IFLA)

WFD Wollermann FRANCHISE DEVELOPMENTS