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INSIGHTS

Another Case of the Accidental Franchisor

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The decision of the Ontario Superior Court of Justice in *Fyfe v. Stephens* (2018 ONCSC 5066) (**Fyfe**) exemplifies the importance of substance over form as it relates to contractual relationships that may or may not be characterized as "franchising arrangements".

In Fyfe, the parties entered into a business agreement regarding “Dial a Bottle” and executed a document entitled “Exclusivity Agreement” (the **Agreement**). Unfortunately, the plaintiffs' business undertaking in connection with the Agreement was not successful and the plaintiffs sought to rescind the Agreement through the *Arthur Wishart Act (Franchise Disclosure)* (Ontario).

The plaintiffs claimed that the Agreement was a franchising arrangement and that they were entitled to rescind the Agreement pursuant to the *Arthur Wishart Act* because they were never provided a franchise disclosure document by the defendant. Accordingly, they could claim from the defendant the following:

1. a refund of any money received from or on behalf of the plaintiffs, other than money for inventory, supplies or equipment;

2. purchase from the plaintiffs of any inventory that the plaintiffs had purchased pursuant to the Agreement and remaining at the effective date of rescission, at a price equal to the purchase price paid by the plaintiffs;

3. purchase from the plaintiffs of any supplies and equipment that the plaintiffs had purchased pursuant to the Agreement, at a price equal to the purchase price paid by the plaintiffs; and

4. compensation from the plaintiffs for any losses that they incurred in acquiring, setting up and operating the franchise, less the amounts identified in (1) to (3) above.

The defendant claimed that a franchise arrangement was never contemplated. The defendant provided the Court with email correspondence between the parties that set out that "Dial a Bottle is not a franchise" and also pointed out to the Court that the Agreement contained a clause where the plaintiffs expressly agreed that they were not purchasing a franchise.

Ultimately, the Court found that the Agreement was, in fact, a franchise agreement. Of upmost importance, the Court ruled that "if the substance of the relationship is a franchise, it matters not whether the parties sign a document called a franchise agreement".

The following indicia was used by the Court in determining that the substance of the parties' relationship was that of a franchise:

1. the plaintiffs were required by contract to make a payment or continuing payment to the defendant in the course of operating the business or as a condition of acquiring the business or commencing operations;

2. the defendant granted the plaintiffs the right to sell, offer for sale or distribute goods or services that were substantially associated with the defendant's trademark; and

3. the defendant exercised significant control over, or offered significant assistance in, the plaintiffs' methods of operations including building, design and furnishings, locations, business organization, marketing techniques and training.

This case serves as a stark reminder that, from a franchising law perspective, it is the substance of a contractual relationship which matters the most. A business which licenses or is considering licensing their system to others should seek legal advice on this matter so as to be fully apprised of the legal requirements underlying their proposed transaction.

Invitation for Discussion:

If you would like to discuss this article in greater detail, or any other business law matter, please do not hesitate to contact one of the lawyers in the Business Law group at Nerland Lindsey LLP.

Disclaimer:

Note that the foregoing is for general discussion purposes only and should not be construed as legal advice to any one person or company. If the issues discussed herein affect you or your company, you are encouraged to seek proper legal advice.