

All in the Family: Not When it Comes to Franchise Law

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As franchise practitioners are aware, franchise legislation across Canada (“**Canadian Franchise Legislation**”) provides for an exemption from a franchisor’s obligation to provide a disclosure document in respect of the sale of an additional franchise to an existing franchisee.¹

In the recent case of *Taprobane Group Holdings Ltd. v. Brownies Foods Ltd.*,² the British Columbia Supreme Court denied Brownies Foods Ltd.’s (the “**Franchisor**”) an exemption from the obligation to deliver a disclosure document by strictly interpreting which persons constituted the franchisee. The denial meant that Taprobane Group Holdings Ltd.’s (the “**TGH**”) right to rescind was upheld.

FACTS

The facts of the case are relatively straightforward. The Franchisor had executed two franchise agreements:

- 1) Franchise Agreement dated April 2019, with Taprobane Foods Limited (“**TFL**”) for the operation of a Brownies Chicken and Seafood restaurant in Maple Ridge, BC. Devin Amerasinghe and his wife, Iromie Amerasinghe were the directors, and shareholders of TFL.
- 2) Franchise Agreement dated May 30, 2022, with TGH for the operation of a Brownies Chicken and Seafood restaurant in Mission, BC. Devin Amerasinghe and his wife, Iromie Amerasinghe, as well as their son, Adrian Amerasinghe, were the directors, and shareholders of TGH.

The Franchisor failed to provide a disclosure document to either TFL or TGH, or their respective directors or shareholders. The Mission Franchisee delivered a notice of rescission on or about October 28, 2022, on the basis that the Franchisor had failed to provide a disclosure document as required by section 5 of the *Franchises Act* (BC).

THE PARTIES’ POSITIONS

The Franchisor asserted that it was exempt from the obligation to deliver a disclosure document pursuant to the exemption found in ss. 5(8)(c) of the *Franchises Act* (BC) since:

¹ Arthur Wishart Act (Franchise Disclosure), 2000, R.S.O. 2000, c 3; ss. 5(1)(c) Franchises Act, R.S.A. 2000; ss. 5(7)(c), ss. 5(7)(c), Franchises Act, R.S.P.E.I. 1988, c F-14.1; ss. 5(11)(c), The Franchises Act, C.C.S.M. 2012, c F156; ss. 5(8)(c), Franchises Act, R.S.N.B. 2014, c 111; and ss. 5(8)(c) Franchises Act, R.S.B.C. 2015, c 35 (Can. B.C.).

² 2023 BCSC 227.

- 1) the principals of TGH were the same as that of TFL;
- 2) it did not know that Adrian, being the son of TFL's principals (Mr. and Mrs. Amerasinghe), was also a director and shareholder of TGH;
- 3) it believed that TGH was a holding corporation for TFL; and
- 4) the *Franchises Act* (BC) is designed to protect prospective franchisees who have limited knowledge of the franchisor, disclosure was not required since Mr. and Mrs. Amerasinghe were entirely familiar with the Franchisor, having operated a Brownies Chicken and Seafood restaurant for almost two (2) years.

In response, TGH argued that it was a separate legal entity with different directors and shareholders.

THE LAW

The court took into account the following legal principles:

- A) A franchisee means a person to whom a franchise is granted; this is set forth in ss. 1(1) of the *Franchises Act* (BC);
- B) A franchisor is required to provide a franchisee with a disclosure document; this is set forth in s. 5 of the *Franchises Act* (BC);
- C) A franchisee has a right to rescind a franchise agreement within two years if a franchisor fails to provide a disclosure document; this is set forth in s. 6 of the *Franchises Act* (BC);
- D) Subsection 5(8)(c) of the *Franchises Act* (BC) provides an exemption for the grant of an additional franchise to an existing franchisee if:
 - (i) the additional franchise is substantially the same as the existing franchise that the franchisee is operating, and
 - (ii) there has been no material change since the existing franchise agreement, or latest renewal or extension of the existing franchise agreement, was entered into; and
- E) The burden of proving an exemption or exclusion from the requirement or provision under the Act is on the party claiming the exemption; this is set forth in s. 14 of the *Franchises Act* (BC).

THE DECISION

The Court granted TGH's application to rescind, narrowly interpreting the definition of "franchisee". The court concluded that TGH was not a person to whom a franchise had been previously granted, and thus was not an "existing franchisee". As evidence of the foregoing the court stated that TGH had no prior legal relations or connection to the Franchisor and that even though there was some overlap in the share ownership and directorships with TFL, the two corporations were separate and distinct entities.

PRACTICE TAKEAWAYS

It is unclear whether the court held that the exemption in ss. 5(8)(c) of the *Franchise Act* (BC) was not available because TGH was a separate legal entity which had "no prior legal relations or connection to the Franchisor", which would be the case in most every circumstance in which an existing franchisee uses a newco to enter into a franchise agreement, or whether it was because Adrian was a director and shareholder of TGH but not of TFL. There was no indication in the decision as to what percentage ownership Adrian had in TGH.

To rely on the additional grant exemption found in Canadian Franchise Legislation, franchisors and their lawyers should make sure that both the franchisee corporation which signs the second franchise agreement, and the principals who will operate the second franchise, are the same as the first franchisee. Of course, franchisors, and their lawyers, must also ensure that there has been no material change since the date of the first franchise agreement.