

# FRANCHISEES CANNOT CLAIM STATUTORY DAMAGES FOR MISREPRESENTATION WHEN A FRANCHISOR VOLUNTARILY, BUT WITHOUT OBLIGATION, PROVIDES A DISCLOSURE DOCUMENT

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The Ontario Superior Court recently confirmed that a franchisee is not entitled to sue for damages under s. 7 of the *Arthur Wishart Act (Franchise Disclosure)*, 2000, S.O. 2000, c. 3 (the “AWA”) when a franchisor voluntarily, but without obligation under s. 5 of the AWA, provides a disclosure document that contains misrepresentations. The decision in *2101516 Ontario Inc. v. Radisson Hotels Canada Inc.*, 2019 ONSC 3302 is good news for franchisors.

## Background

Section 7 (1) of the AWA provides that if a franchisee suffers a loss as a result of a misrepresentation in a disclosure document or due to the franchisor’s failure to comply with the disclosure obligations mandated by s. 5, it has a statutory right of action in misrepresentation against the franchisor, its associates, agents and every person who signed the disclosure document. Significantly, s. 7 (2) of the AWA provides that a franchisee is *deemed to have relied upon* any misrepresentation contained in a disclosure document. This makes the statutory right of action under s. 7 (1) much easier for a franchisee to establish because, unlike the common law tort of misrepresentation, it does not have to prove that it detrimentally relied on the alleged misrepresentation.

## The Facts in *Radisson Hotels Canada*

The applicant (2101516 Ontario Inc.) spent over \$8 m to purchase a hotel and became a franchisee of Radisson In 2016. Less than a year later, it stopped making royalty payments and subsequently sought to rescind the franchise agreement on the basis of allegedly deficient disclosure by Radisson. The applicant franchisee then commenced an arbitration (the franchise agreement contained a mandatory arbitration clause) for rescission under s. 6, and damages for misrepresentation under s. 7, of the AWA.

The arbitrator ultimately held that Radisson was exempt from the disclosure obligation in s. 5 because the

franchisee invested more than \$5 m in acquiring and operating the franchise in the first year (pursuant to s. 5 (7)(h) of the AWA and s. 10 of O. Reg 581/00). As a consequence of that, the arbitrator dismissed the applicant's rescission claim under s. 6, as well the statutory misrepresentation claim under s. 7, of the AWA. On this last point, the arbitrator concluded that a statutory claim for misrepresentation under s. 7 only arises in relation to misrepresentations contained in a disclosure document that is *required* to be provided under s. 5, but not for those in a disclosure document that was not required to be provided. The arbitrator went on to find that Radisson had validly terminated the franchise agreement due to unpaid royalties and fees, and awarded Radisson damages and legal costs.

The franchisee brought an application for leave to appeal the arbitrator's ruling to the Ontario Superior Court, arguing that the right to damages under s. 7 of the AWA applies to misrepresentations contained in any disclosure document provided to a franchisee, and not simply those required by s. 5 of the AWA to be provided. The court disagreed.

### **The Decision in *Radisson Hotels Canada***

After addressing whether the applicant franchisee has the right to appeal the arbitrator's decision based on the language of the arbitration clause (the court found it had no such right, given that the clause said the arbitral decision "will be final, conclusive and binding"), the court went on to find that the arbitrator's decision regarding s. 7 of the AWA was not only reasonable, but correct.

The court noted that the AWA is designed to address the inequality of bargaining power between franchisees (who are often small, unsophisticated businesses) and franchisors (who are typically commercially sophisticated and better funded). However, the court also noted that although s. 5 of the AWA requires franchisors to provide prospective franchisees with a disclosure document, s. 5 (7) contains several exemptions from this requirement – the purpose for which is to exclude the disclosure obligation where it is not required to correct an inequality of bargaining power. Moreover, the court observed that s. 7 affords a right to damages for losses suffered because of a misrepresentation "contained in the disclosure document", and that "Disclosure document" is defined in the AWA to mean "the disclosure document *required by section 5*" (emphasis added).

Accordingly, the court held that the plain language of s. 7 of the AWA provides the statutory right to sue for misrepresentation only to those franchisees for whom the franchisor is obliged under s. 5 to deliver a disclosure document. As the court put it, to read s. 7 more broadly would make the words "required by section 5" in the definition of disclosure document unnecessary. The court also found that the more broad interpretation suggested by the applicant franchisee would be contrary to the purpose of the AWA by making the right to sue for damages under s. 7 available to commercially sophisticated franchisees "who neither require, nor are entitled, to the assistance of s. 5 to correct the imbalance of bargaining power between prospective franchisees

and franchisors”.

Consequently, the court dismissed the franchisee’s application for leave to appeal and granted Radisson’s cross-application for an order enforcing the arbitral award.

### **Key Take-Aways**

Sometimes out of an abundance of caution and sometimes for other reasons, franchisors provide disclosure documents to prospective franchisees even when one or more of the exemptions from having to do so in s. 5 (7) of the AWA apply. Aside from the large investment exemption in s. 5 (7) (h) referred to above, some of the other exemptions include:

- The grant of a franchise to a person who has been an officer or director of the franchisor or franchisor’s associate for at least six months (s. s. 5 (7) (b));
- Where an additional franchise is granted to an existing franchisee, if the additional franchise is substantially the same as the existing franchise and no material changes have occurred since the existing franchise agreement, or latest renewal or extension, was entered into (s. s. 5 (7) (c)); and
- The renewal or extension of a franchise agreement where there has been no interruption in the operation of the business and no material changes have occurred since the existing franchise agreement, or latest renewal or extension, was entered into (s. s. 5 (7) (f)).

The reasoning in the *Radisson Hotels Canada* case may be of use to franchisors in resisting statutory misrepresentation claims under s. 7 of the AWA when, notwithstanding an applicable exemption, they provide a prospective franchisee with a disclosure document. Although franchisees may still have a common law claim for misrepresentation against the franchisor, to succeed on that they will have to establish that they relied upon the alleged misrepresentation in the disclosure document to their detriment. This will be difficult to do, for example, if the franchisee never read the disclosure document.

by W. Brad Hanna

### **A Cautionary Note**

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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