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Franchising in Canada – 2022 Year in Review





Overview

In this update we summarize some of the more significant franchise law cases and legislative developments that occurred in 2022.

Top 6 Case and Legislative Highlights in Franchise Law in 2022

- The Ontario Court of Appeal confirmed in two decisions that franchisees are not required to show that disclosure deficiencies subjectively impaired their ability to make an informed investment decision to succeed in claims for rescission. Following the 2018 Court of Appeal's decision in *Raibex*, there was some uncertainty as to whether fundamental disclosure deficiencies also required subjective proof that the franchisee was unable to make an informed investment decision.
- The first decision reported under New Brunswick's *Franchises Act* discusses the necessity of providing statute-compliant financial statements.¹
- The Ontario Court of Appeal held that continued performance after the expiry of a franchise agreement had the effect of extending the agreement.²
- The Ontario Superior Court of Justice noted that goodwill associated with a trademark can be established by obtaining evidence from potential franchisees.³
- Small business franchisors may be eligible for additional funding and loans due to the amendments to the *Canada Small Business Financing Regulations* and *Canada Small Business Financing Act*.
- The *Single-use Plastics Prohibition Regulations under the Canadian Environmental Protection Act, 1999* has ushered in the prohibition of the manufacture, import and sale of single-use plastics.

Case Law Highlights

Franchise Disclosure Document Deficiencies

In 2022, the courts continued to examine what constitutes a “fatal flaw” or other deficiencies in franchise disclosure documents (“FDDs”) that entitle franchisees to rescind their franchise agreements for up to 2 years after the date of signing. Some of the key cases in this regard are summarized below:

261707 Ontario Inc. v. Freshly Squeezed Franchise Juice Corporation (Freshly Squeezed), 2021 ONSC 2323 aff’d 2022 ONCA 437

The Ontario Court of Appeal (“ONCA”) found that the failure to provide complete financial statements and include an Agreement to Lease were material disclosure deficiencies or “fatal flaws”. Further, the failure to highlight that the franchised business would be the first to operate in a non-mall retail environment amounted to failing to disclose a “material fact” (as defined in the *Arthur Wishart Act (Franchise Disclosure), 2000*, (the “AWA”). These deficiencies entitled the franchisee to rescind the franchise agreement under section 6(2) of the AWA, and the franchisee was not required to provide evidence of *actual* impairment of their ability to make an informed investment decision. Central to the Court’s analysis was the fact that the franchisor withheld information that was within its power to disclose. For a full analysis of the Ontario Supreme Court’s decision, please see our bulletin [here](#).

2483038 Ontario Inc. v. 2082100 Ontario Inc. (Fit for Life), 2022 ONCA 453

The ONCA confirmed that failure to certify an FDD is sufficient to entitle a franchisee to rescind the franchise agreement under section 6(2) of the AWA. Section 7 of the regulation under the AWA requires that every disclosure document include

a signed and dated certificate. In this case, the franchisor only signed one page of the FDD, which did not adequately confirm that the document was accurate and complete. The ONCA noted that where there is a defective certificate, there is no further requirement of the franchisee to demonstrate they were unable to make an “informed investment” in order to be entitled to rescission.

Alphataho Inc., et al v. Maaco Canada Partnership LP, et al., 2022 NBQB 25

In the first reported decision under New Brunswick’s *Franchises Act*, the Court held that the franchisor’s failure to provide statute-compliant financial statements amounted to a fatal defect in disclosure and entitled the franchisee to rescind the franchise agreement. In this case, the franchisor provided financial statements that were older than was required by the *Franchises Act*. While the franchisor argued it could have qualified for an exemption from the financial statement disclosure requirement, the Court held that failure to claim the exemption is “not a mere technical defect”.⁴ When franchisors qualify for and intend to rely on an exemption to disclose financial statements, caution should be exercised before financial statements are automatically included in the FDD. For a full analysis of this decision, please see our bulletin [here](#).

1901709 Ontario Inc. et. al. v. Dakin News Systems Inc., 2022 ONSC 6008

The AWA provides that no FDD is required where the grant of a franchise to a third-party is not effected by or through a franchisor (section 5(7)(a)(iv)). The Court confirmed this exception is inapplicable if the franchisor is involved in the transfer beyond exercising a right to consent. Analysis of this section will consider the “pith and substance” of a transaction to determine if it is truly a mere assignment that falls within the AWA’s exception. In this case, the Court found the franchisor was involved beyond exercising

¹ *Alphataho Inc., et al v. Maaco Canada Partnership LP, et al.*, 2022 NBQB 25.

² *Coffee Time Donuts v. 2197938 Ontario Inc.*, 2022 ONCA 435.

³ *2788610 Ontario Inc. v. Bhagwani*, 2022 ONSC 6098

⁴ *Alphataho v Maaco*, 2022 NBQB 25 at para 52.

a right to consent to the transfer, by requiring the parties to sign a new franchise agreement and pay new consideration as part of its transfer procedure. This demonstrated that the franchisor had “effected” the transfer, rendering the FDD exception in the AWA inapplicable.

Franchise Agreements

This past year, courts also considered the extension of expired franchise agreements by conduct and the governing legislation of arbitration provisions. Two key cases in this regard are as follows:

Coffee Time Donuts v. 2197938 Ontario Inc., 2022 ONCA 435

The ONCA has cautioned that obligations under an expired franchise agreement can be extended by the parties’ conduct. In this case, the ONCA considered evidence that the franchisee continued to pay royalties for a period of time, continued to use “Coffee Time” branding and continued to purchase products from exclusive suppliers. The ONCA accordingly upheld the motion judge’s decision that, although the franchise agreement had expired, the parties’ conduct had the effect of extending the agreement and thereby entitled the franchisor to seek unpaid royalties for periods following its expiry.

Canadian Mortgage Experts Ltd. v. Dominion Lending Centres Inc. 2022 BCSC 911

Franchisors should keep in mind that arbitration provisions in FDDs should be drafted in accordance with the governing legislation’s jurisdictional requirements. Section 12 of British Columbia’s *Franchises Act* provides that “a provision in a franchise agreement that purports to restrict the application of the law of British Columbia or to restrict jurisdiction or

venue to a forum outside British Columbia” is void. In this case, the franchise agreement contained a provision specifying that any disputes were to be resolved by arbitration and governed by the laws of British Columbia. The Court rejected the plaintiffs’ argument that section 12 of the *Franchises Act* prohibits arbitration of franchise disputes and that arbitration is a “venue or forum” outside of British Columbia.

Trademarks

As we know, trademark laws are of critical importance to franchisors. Franchisors should be aware of their rights and responsibilities when dealing with trademarks to ensure that their branding is used in a manner that benefits the franchise system and limits potential infringement. Some notable cases in 2022 include:

2788610 Ontario Inc. v. Bhagwani, 2022 ONSC 6098

A proposed use trademark application does not allow a person to sue for trademark infringement until the trademark is issued. The Divisional Court vacated the motion judge’s interlocutory injunction (which had prohibited the defendants from using “Bombay Frankie”) on the basis that the plaintiff had not yet used the trademark. This case reaffirms that no goodwill can be created through the use of a trademark until the trademark is actually used to sell goods or services.

Of note to franchisors, the Court outlined that goodwill associated with a trademark can be established by obtaining evidence from potential franchisees, as opposed to only from customers or the general public. If a franchisor can demonstrate that their trademark has developed goodwill as a franchising business, this could provide sufficient evidence to meet the serious issue to be tried element of the interlocutory injunction test in a passing-off claim. See our full examination of the decision, as well as the motion judge’s decision, [here](#).

**2799232 Ontario Inc. and Maid Right, LLC,
2022 TMOB 104**

Franchisors should be aware that a trademark must be used with associated services within three years of registration, unless “special circumstances” exist to excuse the lack of use as provided by section 45(3) of the Trademarks Act (the “TMA”). When determining if “special circumstances” exist, courts will consider the length of time for which the trademark has not been used, whether the reasons for non-use are beyond the control of the owner and whether there is a serious intention to resume use in the near future. In this case, the Trademarks Opposition Board found that the combination of the franchisor’s recent acquisition of the assets of a previous owner, complex technical requirements to produce a disclosure document and the existence of a franchise agreement signed shortly before the end of the required three-year period created the necessary “special circumstances” to preserve the registration.

**Beijing Judian Restaurant Co. Ltd. v. Meng,
2022 FC 743**

Intentional filing of an application in Canada for a third party’s foreign mark can be legitimate if there is no reputation for the mark in Canada. However, a registration for a trademark obtained in bad faith will be invalid pursuant to section 18(1)(e) of the TMA. In this case, the Respondent did not have a legitimate commercial intention to use the mark and had only registered the mark in an attempt to profit off the reputation of the Applicant. As the trademark was obtained for the sole purpose of extorting a foreign franchisor when they sought Canadian expansion, the Court invalidated the trademark registration as it was obtained in bad faith.

**Milano Pizza Ltd. v. 6034799 Canada Inc.,
2022 FC 425**

When a licensor does not exert sufficient control over the goods provided or services performed by its licensees, a mark used by a licensee

cannot reach the distinctiveness standard required for trademark registration. In this case, a lack of controlled licensing for a substantial period of time caused the “Milano Pizzeria & Design” trademark to lose its distinctiveness, and therefore its registration. Although this case did not involve a franchise, the Court noted that “[d]epending on the circumstances, a well-structured franchise arrangement can involve the requisite degree of control” required by section 50(1) of the TMA.⁵ Franchise agreements should be drafted to exert sufficient control over franchisees, such that the licensing requirements under the TMA are met with respect to the franchisor’s mark.

**Spagnuolo v. Re/Max Hallmark Realty Ltd.,
2022 FC 416**

Courts may look to the franchise agreement to assess the use and ownership of improvements and modifications of a trademark. In this case, the Trademarks Opposition Board’s decision to reject the opposition of Re/Max Hallmark Realty Ltd.’s registration of the trademark “HALLMARK” was upheld. The Court rejected the Opponents’ alternative argument that the “HALLMARK” trademark was licensed together with “RE/MAX” under a franchise agreement meaning that the basis for filing the application was false. Rather, the franchise agreement did not pertain to the use and ownership of the word “HALLMARK” as it did with respect to “RE/MAX”.

Injunctions to Enforce Restrictive Covenants

Franchisors seeking interlocutory injunctions to enforce restrictive covenants contained in franchise agreements must satisfy a high evidentiary burden in Canada. In 2022, the courts considered the extent of evidence necessary for an injunction, the use of third parties to undermine franchise agreements and circumstances where an injunction will not be an available remedy.

⁵ *Milano Pizza Ltd. v. 6034799 Canada Inc.*, 2022 FC 425, at para 80.

Some of the key decisions in this area are:

***RFSP Equipment v. Singh*, 2022 BCSC 538**

Franchisors considering injunctive relief will be required to advance actual evidence of irreparable harm. This decision considered the actions brought by the two operating arms of Freshslice Pizza against restaurants that had operated as franchisees of the business but had subsequently rebranded. The Court concluded that although there was a strong *prima facie* case, the plaintiffs failed to establish that they would suffer irreparable harm if the injunctions to prevent the restaurants from operating as pizza restaurants in certain locations were refused. “A key consideration was the fact that the defendants had completely rebranded such that there is no possibility the brand, goodwill or reputation of the plaintiff will be affected by the continued operation of the defendants’ restaurants.”⁶

***Garcha Brothers Meat Shop Ltd. v. Singh*, 2022 BCCA 36**

When there is apparent collusion to avoid a restrictive covenant included in a franchise agreement, courts may enjoin third parties acting in concert in this effort. The British Columbia Court of Appeal upheld the lower Court’s finding that an injunction was just and equitable because of the apparent collusion of the defendants to avoid a franchise agreement’s post-termination non-competition provisions. Parties cannot avoid non-competition provisions in their franchise agreements by enlisting third parties to disguise business ownership.

***Kwantlen Pizza Ltd. v. 1253928 BC Ltd.*, 2022 BCSC 1252**

Franchisors should be dissuaded from seeking an injunction against a party that has already carried out essentially, what the court order would ask of them. Like the *Garcha* case above, the plaintiff sought to enforce a restrictive covenant. The Court noted the defendant had subsequently rebranded and no longer

associated itself with the plaintiff’s brand, and rejected broadening the injunctive relief order to terms that the parties did not agree to. Injunctive relief cannot be granted over an alleged past wrong as opposed to a “continuation or perpetuation of an ongoing scheme”.⁷

***Turtle v. Valvoline Canadian Franchising Corp.*, 2021 SKCA 76**

An individual cannot be bound by a restrictive covenant in a franchise agreement if they did not sign personally or act as a guarantor. In this case, a franchisee sold their oil change business to the plaintiff purchaser, and then subsequently started a new oil change business. The issue on appeal was whether the lower Court correctly granted an injunction against the director of both defendant companies restraining the operation of the new competing business. The Saskatchewan Court of Appeal noted that the Chambers judge’s analysis of the franchise agreement did not account for the notion of independent corporate personality, and erred in concluding the plaintiff had a strong case against the defendant director.

***Groupe Daoust/Forget inc. c. Nettoyeurs 888 Décarie inc.*, 2022 QCCS 3589**

This Quebec case illustrates how franchisees cannot unilaterally stop respecting obligations in their franchise agreements on the grounds that they were not properly informed of a subsequent transfer of the franchise network to a new purchaser. The Superior Court granted the franchisor’s request for an injunction to order the six franchisee defendants, who were working in a concerted effort, to reinstate the Daoust/Forget banners at their respective establishments and to comply with their payment obligations. While the franchisees claimed their previous franchise agreements were unenforceable given that they were never informed of a transfer of the franchise network, the Court considered evidence that the franchisees, at least tacitly, continued doing business with the new purchaser for seven continuous years.

⁶ *RFSP Equipment v. Singh*, 2022 BCSC 538, at para 106.

⁷ *Kwantlen Pizza Ltd. v. 1253928 BC Ltd.*, 2022 BCSC 1252, at para 36.

When evaluating the criterion of “irreparable harm”, the Court explained that since the legal advisor representing the six franchisee defendants was also acting for 30 other franchisees who had not yet chosen to proceed with unilateral termination, refusing to grant the injunction would strengthen the likelihood and risk that the 30 other franchisees would also elect to unilaterally terminate their agreements. This would constitute serious and irreparable prejudice to the franchisor.

Duty of Good Faith

The duty of good faith was considered in the franchise context in several 2021 decisions, which remain the latest key decisions on this topic. Franchisors should keep these general principles in mind when performing duties and exercising contractual rights under franchise agreements. A failure to renew an agreement that does not contain an express right of renewal does not constitute a breach of the duties of fair dealing and good faith (*FPMG Hospitality Inc. v. Recipe Unlimited Corporation*, 2021 ONSC 7156). The Ontario Court of Appeal also held that a desire to end a contractual relationship then “pouncing” on the earliest opportunity to do so will not necessarily lead to a finding of bad faith (*2161907 Alberta Ltd. v. 11180673 Canada Inc.*, 2021 ONCA 590).

The Ontario Court of Appeal also considered the following principles in the licensing context which are applicable to contracts generally (*2161907 Alberta Ltd. v. 11180673 Canada Inc. (“Tokyo Smoke”)*, 2021 ONCA 590 – see our full analysis [here](#)):

- Courts are more likely to make a finding of honest mistaken belief (as opposed to a finding of bad faith) where termination is rooted in the negotiated contractual terms

- Terminations which are made arbitrarily, capriciously, unreasonably or dishonestly are more likely to be viewed as made in bad faith
- A party who seeks to end a relationship with a counterparty can take the opportunity to do so when a valid reason is presented, and this does not necessarily constitute bad faith

Notable Legislative Changes Impacting Franchisors

Some of the key legislative developments in 2022 that may be of interest to franchisors include:

Canada Small Business Financing Regulations and Canada Small Business Financing Act

On July 4, 2022, the amendments to the *Canada Small Business Financing Regulations* and *Canada Small Business Financing Act* came into force. Small business franchisors will now benefit from “additional financing products, new class of loans, increased loan amounts and terms, improved loan conditions and decreased administrative burden.”

Bill 96 -An Act respecting French, the official and common language of Québec

An Act respecting French, the official and common language of Quebec became law in Quebec on June 1st, 2022. Bill 96 introduces changes regarding the translation of commercial contracts, the use of trademarks and public signage and creates new workplace language rules to further emphasize the use of the French language within the province. Many new requirements have been introduced which will impact contractual relationships between franchisors and franchisees.

Competition Act

Section 45(1.1) of the Competition Act will come into force on June 23, 2023. The provision will make it an offence to fix wages or terms of conditions of employment and to enter into no-poaching agreements. Franchisors should be aware of the potential consequences of a breach of the provision. The penalty for an offence under this provision includes up to 14 years imprisonment and/or a fine at the court's discretion.

Trademarks Regulations

Public consultations are being conducted by the Canadian Intellectual Property Office in relation to the proposed amendments to the Canadian *Trademarks Regulations*. The purpose of the proposed amendments is to provide the Canadian Trademarks Opposition Board with “the tools needed to discourage undesirable behaviors in proceedings, protect confidential evidence and manage complex cases.”⁸ The amendments would give the Register of Trademarks three new authorities: (1) awarding costs, (2) granting confidentiality orders, and (3) case managing proceedings. See a full summary [here](#).

Bill 64 – An Act to modernize legislative provisions as regards the protection of personal information (Quebec)

Franchisors and franchisees based in Quebec that collect, use and disclose personal information should be aware of changes brought forward by Bill 64. The amendments will come into force over the period of September 22, 2022 to September 22, 2024. Of note, amendments to the private sector law, *Act respecting the protection of personal information in the private sector* that came into force on September 22, 2022, include the following:

- Requirement to appoint a person in charge of the protection of personal information
- Requirement to report “confidentiality incidents” in the case of serious injury
- New exception to use of personal information without consent in a contemplated commercial transaction

See McMillan's bulletin from October 2021 [here](#) when the bill received assent, for a further discussion of the amendments.

Single-use Plastics Prohibition Regulations under the Canadian Environmental Protection Act, 1999

Franchisors in the food and grocery industry should be aware of the federal government's new regulations prohibiting the “manufacture, import and sale of single-use plastic checkout bags, cutlery, foodservice ware made from or containing problematic plastics, ring carriers, stir sticks, and straws.”⁹ The coming into force of the prohibitions will take place starting from December 20, 2022 up until December 20, 2025.

Bill C-27 – Digital Charter Implementation Act, 2022

The Federal Government introduced Bill C-27 on June 16, 2022 in the House of Commons. The proposed Acts aim to modernize and build on current privacy legislation. The proposed Acts are: *The Consumer Privacy Protection Act* (CPPA), *The Personal Information and Data Protection Tribunal Act* (PIDPTA), and *The Artificial Intelligence and Data Act* (AIDA). The Bill is currently at second reading in the House of Commons. Franchisors should keep an eye out for future obligations that may arise pursuant to these proposed Acts, including any legislative changes by provinces in an effort to align with the federal Acts.

⁸ The Canadian Intellectual Property Office, *Consultation Document, Proposed Amendments to the Trademarks Regulations and Draft Practice Notices Pertaining to Proceedings Before the Trademarks Opposition Board*, available [here](#) (accessed December 18, 2022).

⁹ Government of Canada, *Single-Use Plastics Prohibition Regulations*, available [here](#) (accessed December 18, 2022).

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