

 **FRANCHISING ALERT**

**I have heard of the term “Churning” – what does it mean?**

**Churning**

This is the practice by which a Franchisor either:

- (a) terminates a Franchise Agreement due to alleged breaches by a Franchisee; or
- (b) the Franchisor unreasonably refuses to renew a Franchise Agreement.

The Franchisor then moves to take over the franchised business or on-sell it without paying fair compensation to the Franchisee for the goodwill or the Franchisee's fitout or plant & equipment.

Not only is this financially detrimental and emotionally draining to the existing Franchisee who's Franchise Agreement has been terminated (or not renewed), but the new Franchisee is then exposed to the same potential risk themselves. It can become a vicious cycle where by Franchisee's are just turned over one after the other – hence the word “churning”.

Unscrupulous Franchisors may go as far as to deliberately undermine franchisees so they fail, enabling the Franchisor to resume the franchisee's business and then re-sell it. By doing this, the Franchisor gets the benefit of recurring Franchise fees each time a franchise is turned over.

Churning may also come about where Franchisors embark in the practice of buying back Franchisee businesses (usually for less than the market value) – that franchised business then forms part of the Franchisor's company-owned outlets. Typically Franchisor's would target more profitable Franchisee businesses with the end purpose on mind of increasing the Franchisor's profits.

Proving that a Franchisor has deliberately acted to enable the failure of a Franchisee may not always be easy to achieve.

Thankfully, not all Franchisors are unscrupulous. But if you are looking to enter into a franchise it is important to look out for signs of this type of behaviour. Enquiries you can make may include:

- Obtaining appropriate professional advice;
- Carrying out thorough due diligence of the Franchisor and franchise system;
- Checking the Disclosure Document for details of Franchise terminations, surrenders, transfers and the like – especially if it involves the same territory or buy-backs by the Franchisor;
- Contact existing/previous Franchisees of the system and ask them for their experiences dealing

with the Franchisor and the system.

There are legal remedies available if you are the victim of churning or suspect the Franchisor is undermining you or your business.

Any enquiries about franchising can be directed to Raymond Duffy, Associate on 07 3233 9909 or email: [raymond@mdl.com.au](mailto:raymond@mdl.com.au)