

The Impact of the Consumer Protection Act on Franchise Agreements

by

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CHAPTER 1: INTRODUCTION

According to Gerrie Van Biljon, an executive director of Business Partners, an entrepreneurial investment company, the South African franchise sector has enormous potential which can facilitate job creation on the long term and positively influence the economy.¹ Van Biljon adds that during 2008 to 2010 when South Africa was in recession and various other industries showed little growth, if any, the franchise industry contributed to 11.8% of the country's economy, clearly showing the magnitude of this industry especially in times of economic down turn.²

With franchises becoming a popular phenomenon worldwide and regulation of the industry becoming inevitable³ as well as the predominant role this R300bn plus industry⁴ plays in our commerce, the question then presents itself how is this industry regulated?

Instead of enacting legislation particularly dedicated to regulating the franchise industry, the legislature included various provisions relating to franchises in the Consumer Protection Act 68 of 2008 (herein after referred to as the "CPA").⁵

Before the enactment of the CPA the franchise industry was partially regulated by selective portions of legislation intended for other industries, self-regulation by an appropriate regulatory body and, of course, principles of the common law.⁶

In a free-market economy it will be the ideal that there is as little government intervention as possible and it is therefore of utmost importance that the system

¹ Beeld newspaper "SA franchises nog in kinderskoene" (27 May 2013).

² Ibid.

³ Rhodie L and Scriba B "Franchise Agreements and the Consumer Protection Act" (September 2011).

⁴ Thomas S "Selling Power" Financial Mail (11 May 2012) 28.

⁵ Melville NJ "The Consumer Protection Act Made Easy" (2010) Pretoria: Book of Life 109.

⁶ Van Heerden C "Franchise agreements and the Consumer Protection Act: Compliance and Drafting" (June 2012) 5.

which regulates the market place be duly assessed in order to ascertain whether it is flawed before consumer protection legislation is called for and implemented.⁷

Whether the aforesaid due diligence was thoroughly done before the enactment of the CPA remains to be seen, however the *status quo* was found to be wanting, at least by government, and therefore government embarked on a process to enact legislation duly regulating the franchise industry. Pressure from various consumer bodies to right the abuses that were prevalent in business prior to the enactment of the CPA added to government's determination to implement a comprehensive piece of consumer legislation.⁸

The CPA was not enacted overnight but has been a work in progress in the South African legal context for approximately forty years.⁹ Notwithstanding the aforesaid however it had only become an active endeavour to create a comprehensive piece of consumer legislation approximately four years prior to the enactment of the CPA.¹⁰

The product of government's intention, namely "to create and promote an economic environment that supports and strengthens a culture of consumer rights and responsibilities"¹¹ was the CPA.

Before the CPA's enactment there were those who recognised the substantial consumer protection the CPA had to offer and welcomed it, but also warned against the heavy compliance and other burdens that the CPA may impose after its enactment.¹² This compliance and regulatory burdens were anticipated to impose more so on the part of suppliers and franchisors than on consumers and franchisees.

⁷ Woker T "Why the need for consumer protection legislation? A look at some of the reasons behind the promulgation of the National Credit Act and the Consumer Protection Act" (2010) 218.

⁸ Melville NJ "The Consumer Protection Act Made Easy" (2010) Pretoria: Book of Life 1.

⁹ Lester T and Posthumus C "An overview of the Consumer Protection Act" (May 2010).

¹⁰ Melville NJ "The Consumer Protection Act Made Easy" (2010) Pretoria: Book of Life xiii.

¹¹ Explanatory Memorandum on the Objects of the Consumer Bill (2008) 80.

¹² Woker T "Why the need for consumer protection legislation? A look at some of the reasons behind the promulgation of the National Credit Act and the Consumer Protection Act" (2010) 217.

Irrespective of the various speculations of how the CPA would impact consumer trade as it was known to that time it was certain that the CPA would change the way business is done in South Africa.¹³

Consequently the CPA is the first piece of South African legislation regulating the franchise industry by name and in terms of the CPA franchisees are heavily protected.¹⁴ The CPA and Regulations thereto grants substantial new rights to franchisees which is good but will no doubt present a challenge to franchisors necessitating the review of business practices and the re-drawing of various franchise agreements and other ancillary documentation to ensure compliance.¹⁵

Some of the most important aspects the CPA regulates in respect of franchises are:

- (i) the definition of “franchise agreement”,¹⁶
- (ii) that franchise agreements can be terminated within ten business days after signature;¹⁷
- (iii) that a franchisor may not, subject to an exception, require a franchisee to purchase goods or services from specific suppliers;¹⁸
- (iv) that a franchisor may not require a franchisee to agree to purchase any goods or services from a designated third party, unless the goods are reasonably related to the franchisor’s trade marks;¹⁹
- (v) that franchisors are required to make full disclosure to prospective franchisees when selling franchise businesses;²⁰

¹³ Melville NJ “The Consumer Protection Act Made Easy” (2010) Pretoria: Book of Life 1.

¹⁴ Du Preez M “The Consumer Protection Bill: A few preliminary comments” (2009) 76.

¹⁵ Meyer C “Consumer Protection Act regulations an urgent wakeup call for franchisors” (July 2011).

¹⁶ Section 1.

¹⁷ Section 7(2).

¹⁸ Section 13(1).

¹⁹ Section 13(2).

- (vi) that false or misleading representations concerning the performance, characteristics and benefits of the business are not allowed;²¹ and
- (vii) that unfair, unreasonable or unjust contract terms are not allowed.²²

It must also be borne in mind that the law originated in a time prior to the development of large national and multinational companies and when agreements were made between parties with equal bargaining power.²³ With the development of large national and multinational companies a predominant shift occurred in this bargaining power and was the franchise industry not immune to this phenomenon.

The traditionally strong bargaining position that the franchisor had prior to the enactment of the CPA when negotiating franchise agreements has now been altered by, amongst others, the above provisions of the CPA and Regulations thereto.²⁴ This balance, according to some, was sorely needed.²⁵

The purpose of this paper is thus to consider the impact of the CPA upon franchise agreements. In particular the research aim of this paper is the following:

- (i) To give a brief layout of the history, development and nature of franchise agreements.
- (ii) To examine and discuss extensively the impact of the CPA franchise agreements in the South African context;

²⁰ Section 22.

²¹ Section 41.

²² Section 48.

²³ Melville NJ "The Consumer Protection Act Made Easy" (2010) Pretoria: Book of Life 27.

²⁴ Rhodie L and Scriba B "Franchise Agreements and the Consumer Protection Act" (September 2011).

²⁵ Ibid.

- (iii) To identify the various regulatory provisions contained the CPA pertaining franchise agreements;
- (iv) To layout the current challenges created by the CPA bearing on franchise agreements;
- (v) To briefly identify current process, principles and requirements laid down and established by the CPA in order to regulate franchise agreements;
- (vi) To give a brief layout of the different possible developments in light of the CPA;
- (vii) To determine whether the current model and regulatory requirements as provided for in the CPA regarding franchise agreements gives rise to the aim and spirit of the CPA and whether such model and requirements are sustainable under South African law and commerce; and
- (viii) To provide possible solutions to the current challenges experienced by the franchise industry due to the provisions of the CPA.

In light of the above the author of this paper is hoping to find and document the current position as it relates to franchise agreements and provide possible alternatives or suggestions on how the current *status quo* may be positively developed.

In light of the impact the said regulatory provisions have on franchise agreements this paper will be of value in relation to the question of whether the model and requirements that the CPA gives rise to are sustainable and what the future holds for franchise agreements under South African law.

CHAPTER 2: SPECIFIC PROVISIONS RELATING TO FRANCHISE AGREEMENTS UNDER THE CONSUMER PROTECTION ACT

2.1. Introduction

Prior to the enactment of the CPA there was very little legislation specifically governing or effectively regulating franchise agreements. As such the general principles governing the laws of contract, business and commerce, the common law, competition laws and regulations and self-regulation by the Franchising Association of South Africa (herein after referred to as “FASA”) were applied when entering into a franchise agreement.²⁶

The aforesaid general governing principles are those that are almost always found when consumer protection law is examined. These principles were identified as long ago as 1971 in a report compiled by a committee led by Lord Crowther.²⁷ The committee was tasked to compile a report comprehensively examining consumer legislation in the United Kingdom and to provide proposals on how same may be improved.

The Crowther Report, as it became known, found that there are several worldwide trends or similar objectives that can be identified when examining policy considerations underlying consumer legislation. Although this report was mainly concerned with consumer credit legislation, three aspects identified in terms of said report rings true to the essence of any consumer legislation, namely:

- (i) The redress of bargaining inequality between the supplier on the one hand and the consumer on the other;
- (ii) The control of trading malpractices; and

²⁶ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 5.

²⁷ Report of the Committee Consumer Credit, chaired by Lord Crowther Volume 1 (1971).

- (iii) Remedies and the regulation thereof in the event of non-compliance with the relevant consumer legislation.²⁸

In May 2012 the annual turnover of the franchise industry in South Africa was estimated at R300bn, which included fuel sold through franchised filling stations.²⁹ The franchise sector also employs nearly three hundred thousand people in South Africa.³⁰ The important role the franchise industry can play in government's aim to doubling employment to nearly twenty four million within eighteen years must therefore not be underestimated.³¹

Notwithstanding the scale of the industry, however, market participants believed that franchising in South Africa "has not come close to reaching its full potential".³²

Due to the lack of effective regulation and in light of the obvious growing part that the franchising industry plays in the South African economy, the Department of Trade and Industry (herein after referred to as the "DTI") set out to compile a singular piece of legislation that would regulate the franchise industry.

The product of the DTI's aim was certain provisions in the CPA which was promulgated and enacted in two phases. Phase one was the enactment of Chapters 1 to 5 and sections 61 and 120 which became operational from 24 April 2010 and which is known as the early effective date.³³ The remainder of the provisions of the CPA came into operation on 31 March 2011 and the regulations thereto on 1 April 2011 which date became known as the general effective date.³⁴

²⁸ Report of the Committee Consumer Credit, chaired by Lord Crowther Volume 1 (1971) 234.

²⁹ Thomas S "Selling Power" Financial Mail (11 May 2012) 28.

³⁰ Melville NJ "The Consumer Protection Act Made Easy" (2010) Pretoria: Book of Life 109.

³¹ Thomas S "Selling Power" Financial Mail (11 May 2012) 33.

³² Ibid.

³³ Van Heerden C "Franchise agreements and the Consumer Protection Act: Compliance and Drafting" (June 2012) 10.

³⁴ Ibid.

Although the DTI did not compile a piece of legislation dealing exclusively with franchising, substantial provisions are included in the CPA regulating the franchise industry. This is a giant leap forward from the *status quo* before the enactment of the CPA. When looking at similar legislation that has been in operation in Australia for the last 12 years and which have assisted improved standards in this industry,³⁵ the CPA should bode well for the South African franchise industry.

The CPA did however repeal various legislation, whether in part or as a whole, and which will have an impact on the franchise industry. Amongst the most important of these legislation is:

- (i) The Merchandise Marks Act;
- (ii) Business Names Act;
- (iii) Price Control Act;
- (iv) Sale and Service Matters Act;
- (v) Trade Practices Act; and
- (vi) Consumers Affairs (or Unfair Business Practices) Act.³⁶

2.2. Specific provisions

2.2.1. Definition of franchise agreement and franchisee

Right at the outset of the CPA the legislature makes it clear that the franchise industry will hence forth fall under the regulation of the CPA by including a comprehensive definition of what agreements will constitute a franchise agreement in terms of the CPA.

³⁵ Thomas S “Selling Power” Financial Mail (11 May 2012) 32.

³⁶ Melville NJ “The Consumer Protection Act Made Easy” (2010) Pretoria: Book of Life 1.

Accordingly a franchise agreement is defined in section 1 of the CPA as:

“...an agreement between two parties, being the franchisor and franchisee, respectively-

- (a) in which, for consideration paid, or to be paid, by the franchisee to the franchisor, the franchisor grants the franchisee the right to carry on business within all or a specific part of the Republic under a system or marketing plan substantially determined or controlled by the franchisor or an associate of the franchisor;*
- (b) under which the operation of the business of the franchisee will be substantially or materially associated with advertising schemes or programmes or one or more trade marks, commercial symbols or logos or any similar marketing, branding, labelling or devices, or any combination of such schemes, programmes or devices, that are conducted, owned, used or licensed by the franchisor or an associate of the franchisor; and*
- (c) that governs the business relationship between the franchisor and the franchisee, including the relationship between them with respect to the goods or services to be supplied to the franchisee by or at the direction of the franchisor or an associate of the franchisor;...”*

Once a business has complied with the above definition such a business is a franchise.³⁷

From the above it is clear that the definition of a franchise agreement is rather verbose. Although the definition covers the traditional business concept of a franchise agreement it may also include similar provisions in relation to licencing and

³⁷ Melville NJ “The Consumer Protection Act Made Easy” (2010) Pretoria: Book of Life 110.

distribution agreements.³⁸ It should be noted however that the CPA only applies to franchise agreements as defined in the CPA.³⁹

A franchisee is also specifically defined under the definition of consumer in section 1 of the CPA as:

“(A) consumer, in respect of any particular goods or services, means—

...

(d) a franchisee in terms of a franchise agreement, to the extent applicable in terms of section 5(6)(b) to (e)”

When both the above definitions are taken into account one can arrive at the conclusion that the legislature intends to cast a very wide net in terms of the regulation of franchise agreements under the CPA. The provisions in respect of the application of the CPA in terms of section 5 thereof, causing the act to apply to every transaction, unless exempted therefrom, and by specifically including franchisee in the definition under “consumer” supports this submission.

It should further be noted that this is not a new approach and that the legislature applied the same method with the enactment of previous consumer credit legislation like the National Credit Act (hereinafter referred to as the “NCA”).⁴⁰ The purpose of the NCA was also set out in a verbose manner which directly impacts the interpretation and application of the NCA.⁴¹

2.2.2. Application of the CPA

³⁸ Louw L “The CPA and franchise agreements” Without Prejudice (July 2011) 32.

³⁹ Ibid.

⁴⁰ Act 35 of 2005.

⁴¹ Otto and Otto “The National Credit Act Explained” (2013) LexisNexis, 6 & 13.

Section 5 of the CPA duly sets out the application of the CPA. Specific subsections are contained in the sections relating to franchise agreements.

In this regard subsection 7, read together with subsections 6(b) to (e) and having regard to the exemption clause of subsection 2, is of the utmost importance in determining the application of the CPA to franchise agreements.

The relevant subsections read as follows:

“Application of Act

5(2) *This Act does not apply to any transaction—*

...

(b) *in terms of which the consumer is a juristic person whose asset value or annual turnover, at the time of the transaction, equals or exceeds the threshold value determined by the Minister in terms of section 6;...*

(6) *For greater certainty, the following arrangements must be regarded as a transaction between a supplier and consumer, within the meaning of this Act:*

....

(b) *a solicitation of offers to enter into a franchise agreement;*

(c) *an offer by a potential franchisor to enter into a franchise agreement with a potential franchisee;*

(d) *a franchise agreement or an agreement supplementary to a franchise agreement; and*

(e) *the supply of any goods or services to a franchisee in terms of a franchise agreement.*

(7) *Despite subsection (2)(b), this Act applies to a transaction contemplated in subsection (6)(b) to (e) irrespective of whether the size of the juristic person falls above or below the threshold determined in terms of section 6.”*

Currently the threshold as referred to in section 5(7) and as determined by the Minister in relation to section 5(2)(b) is R2mil which means that if a juristic person's annual turnover or asset value at the time of entering an agreement is equal to or more than R2mil, the CPA does not apply.

Notwithstanding the above however and due to the express terms contained in section 5(7), the general exemption of section 5(2)(b) will not apply to franchise agreements which means that the CPA will apply to all franchise agreements irrespective of the size of the entities and the agreement.⁴²

2.2.3. Requirements of franchise agreements

In accordance with the common law and the principle of the sanctity of a contract, a contract validly entered into is binding and enforceable in a court of law.⁴³ A person who signs a written agreement is in terms of the aforesaid principle deemed to be bound by the ordinary meaning and effect of the words contained in such a written contract.⁴⁴

According to general common law principles, a contract is concluded between two parties when all the requirements of a valid contract are satisfied. These requirements are the following:

- (i) the parties must reach consensus;
- (ii) the parties must have contractual capacity;
- (iii) performance must be possible;
- (iv) performance must be determinable;

⁴² Ibid.

⁴³ Melville NJ "The Consumer Protection Act Made Easy" (2010) Pretoria: Book of Life 26.

⁴⁴ Ibid.

- (v) the contract must not be against the law; and
- (vi) formalities, if prescribed by law, must be satisfied.⁴⁵

There are several examples to be found within South African law of formalities being prescribed by legislation before a valid contract will be constituted between the parties. Some of the aforesaid examples are the prescriptive provisions to be found in the Alienation of Land Act⁴⁶ and, to a debatable extend, the NCA.

Section 7 of the CPA has a significant impact on the common law principles and general practices in terms of entering into a franchise agreement. Section 7 sets out prescriptive requirements for a franchise agreement to be valid. It states that:

“7(1) A franchise agreement must—

- (a) be in writing and signed by or on behalf of the franchisee;*
- (b) include any prescribed information, or address any prescribed categories of information; and*
- (c) comply with the requirements of section 22.”*

Section 22, which is discussed in more detail in Chapter 3 hereof, states that franchise agreements must be in plain and understandable language and particularly dictates that a person with average literacy skills and minimal experience as a consumer in terms of the CPA and the relevant transaction can understand the content, significance and importance of the content and provisions of the relevant said agreement.⁴⁷

⁴⁵ Nagel et al “Commercial Law” (2006) LexisNexis, 38.

⁴⁶ Act 68 of 1981.

⁴⁷ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 22.

In addition to the above the CPA in section 7(2) also provides the franchisee with a period of ten business days⁴⁸ in which the franchisee may cancel the agreement without penalty upon due notice in writing to the franchisor. This in effect confers a cooling off right upon the franchisee.⁴⁹ This cooling off right entitles the consumer to rescind from the agreement without committing breach of contract.⁵⁰

Although this cooling off right certainly goes a long way in addressing any bargaining inequality between the parties one cannot help but feel that it does more so on the part of the franchisee. Practically a franchisor may consequently battle to balance his obligations conferred in terms of disclosure prescribed by the CPA⁵¹ and protecting his franchise interests, trade secrets and time spent on training within this initial 10 business day period. The franchisor would effectively be prejudiced by the franchisee that cancels the franchise agreement within the prescribed period but whom he would have disclosed various information to and provided with training.

2.2.4. Regulation 2

Regulation 2 of the CPA is probably one of the most important regulations in respect of franchise agreements. This regulation sets out specifically what a franchise agreement should contain. Section 2 reads as follows:

“Franchise agreements

⁴⁸ Section 2(6) defines business days as follows: *“(6) When a particular number of business days is provided for between the happening of one event and another, the number of days must be calculated by—*

- (a) excluding the day on which the first such event occurs;*
- (b) including the day on or by which the second event is to occur; and*
- (c) excluding any public holiday, Saturday or Sunday that falls on or between the days contemplated in paragraphs (a) and (b), respectively.”*

⁴⁹ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 22.

⁵⁰ Otto JM “Die afkoelreg in die Nasionale Kredietwet en die Wet op Verbruikersbeskerming” LitNet Akademies (March 2012) 24.

⁵¹ Regulation 3.

- 2(1) *This regulation must be read together with sections 7 and 120(1)(e)(ii) of the Act.*
- (2)(a) *Every franchise agreement must contain the exact text of section 7(2) of the Act at the top of the first page of the franchise agreement, together with a reference of the section and the Act.*
- (b) *A franchise agreement must contain provisions which prevent –*
- (i) *unreasonable or overvaluation of fees, prices or other direct or indirect consideration;*
 - (ii) *conduct which is unnecessary or unreasonable in relation to the risks to be incurred by one party; and*
 - (iii) *conduct that is not reasonably necessary for the protection of the legitimate business interests of the franchisor, franchisee or franchise system.*
- (c) *A franchise agreement must contain a clause informing a franchisor that he, she or it is not entitled to any undisclosed direct or indirect benefit or compensation from suppliers to its franchisees or the franchise system, unless the fact thereof is disclosed in writing with an explanation of how it will be applied.*
- (d) *Paragraph 2 of item 3 of Schedule 2 of the Act applies to any pre-existing franchise agreement.*
- (e) *Any provision in a franchise agreement to which these regulations apply which is in conflict with this regulation is void to the extent of such a conflict.*
- (3) *A franchise agreement must as a minimum contain the following specific information –*
- (a) *the name and description of the types of goods or services which the franchisee is entitled to provide, produce, render or sell;*

- (b) *the obligations of the franchisor;*
- (c) *the obligations of the franchisee;*
- (d) *a description of the applicable franchise business system;*
- (e) *the direct or indirect consideration payable by the franchisee to the franchisor;*
- (f) *the territorial rights, if any, granted to the franchisee in detail;*
- (g) *a description of the site or premises and location from which the franchisee is to conduct the franchise;*
- (h) *the conditions under which the franchisee or his, her or its estate may transfer or assign the rights and obligations under the franchise;*
- (i) *a description of the trade mark or any other intellectual property owned by the franchisor, or otherwise licensed to the franchisor which is, or will be used in the franchise, and the conditions under which they may so be used;*
- (j) *if the agreement is related to a master franchise, the master franchisor's identity;*
- (k) *particulars of the initial training and assistance provided by the franchisor and, where the franchisor provides on-going training for the duration of the franchise agreement, a statement that the particulars of such training and assistance will be provided to the franchisee as and when necessary;*
- (l) *the duration and the terms of the renewal of the franchise agreement, provided that such terms and conditions are not inconsistent with the purpose and policy of the Act;*

- (m) *if the franchise agreement provides that a franchisee must directly or indirectly contribute to an advertising, marketing or other similar fund, the franchise agreement must contain clauses informing the franchisee-*
- (i) *of the amount, or if expressed as a percentage, the method of calculation of such contribution;*
 - (ii) *that within six months after the end of the last financial year, the franchisor will provide a franchisee with a copy of a financial statement, prepared in accordance with applicable legislation, which fairly reflects the fund's receipts and expenses for the last financial year, including amounts spent, and the method of spending on advertising and/or marketing of franchisees and the franchise system's goods and services,*
 - (iii) *that, in addition to subparagraph (ii), the franchisor must for every three months period make financial management accounts relating to the funds available to franchisees;*
 - (iv) *that moneys in the fund may not be spent on advertising and marketing of the franchisor's franchises for sale;*
 - (v) *that to the extent that an audit is carried out, a certificate of a registered auditor or accounting officer, as the case may be, confirming that the fund's account has been audited and that the statements, to the best of his or her knowledge, provide a true reflection of the matters stated in this subregulation (m) and where no audit is carried out, a certificate by the accountant that management accounts have been prepared and are correct to the best of the directors' knowledge;*
 - (vi) *that a franchisee can request a copy of the statement and certificate issued in terms of subregulation (v), and that the franchisor must within a reasonable period of such request provide such copies;*

- (vii) *of any contribution to such a fund will be deposited in a separate bank account and used only for purposes of the fund;*
- (viii) *of the franchisor's contribution to such fund, if any; and*
- (ix) *of the fact that the franchisor and or franchisor associated franchised businesses do not enjoy any direct or indirect benefit not afforded to independent franchisees;*
- (n) *the effect of the termination or expiration of the franchise;*
- (o) *extension or renewal terms, or whether there is no option to renew or extend the agreement;*
- (p) *a written explanation of any terms or sections not fully understood by the prospective franchisee upon the prospective franchisee's written request;*
- (q) *the franchisor's legal name, trading name, registered office and franchise business office, street address, postal address, e-mail address, telephone number and fax number;*
- (r) *the name, identity number, town of residence, job titles and qualifications of the franchisor's directors or equivalent officers;*
- (s) *except where the franchisor is a company listed on a stock exchange, details of any proprietor, member or shareholder if they are different from the persons referred to in paragraph (r);*
- (t) *particulars of any restrictions imposed on the franchisee;*
- (u) *the nature and extent of the franchisor's involvement or approval in the process of site selection;*
- (v) *the terms and conditions relating to termination, renewal, goodwill and assignment of the franchise;*

- (w) *the main obligations of the franchisor in respect of initial and on-going training to be provided;*
- (x) *confirmation that any deposits paid by the prospective franchisee will be deposited into a separate bank account and a description of how these deposits will be dealt with;*
- (y) *full particulars of the financial obligations of the franchisee in terms of the franchise agreement or otherwise related to the franchised business including-*
 - (i) *the initial fee payable to the franchisor on the signing of the franchise agreement, including the purpose for which it is to be applied;*
 - (ii) *the funds required to establish the franchised business including, purchase or lease of property, site conversion costs, decor and signage, equipment, furniture, hiring and training of staff, opening stock, legal and financial charges, as may be applicable;*
 - (iii) *the initial working capital, where possible, and the basis on which it is calculated;*
 - (iv) *the total investment required;*
 - (v) *a clear statement as to whether or not any expenses, any salary/wages of employees of the franchised business and the costs of servicing loans are included in the purchase price.*
 - (vi) *the amount of funding that is available from the franchisor, if any, and the applicable conditions;*
 - (vii) *the total amount that the franchisee must contribute towards the necessary funding before borrowing; and*
 - (viii) *on-going amounts payable to the franchisor, with details as to-*

- (aa) *whether the amounts are fixed or variable;*
 - (bb) *whether all or part of the amounts are included in the price of goods or services that must be purchased from the franchisor or other preferred suppliers;*
 - (cc) *the dates, or intervals, at which the amounts fall due; and*
 - (dd) *if any fee is payable in respect of management services provided by the franchisor, details of such services.*
- (4) *A franchise agreement which is renewed after the general effective date is a new franchise agreement for the purposes of subregulations (2) and (3)."*

Regulation 2(2)(a) of the CPA prescribes that every franchise agreement must contain the exact text of section 7(2), which refers to the cooling off right of the franchisee, on the first page of the franchise agreement together with a reference to the section and the Act.

Regulation 2(2)(b) further prescribes that franchise agreements should contain clauses that prevent several listed practices or conditions and then also proceeds to list same accordingly.

In terms of regulation 2(2)(c) above a franchise agreement must also contain a clause informing the franchisor that he or she is not entitled to any undisclosed direct or indirect benefit or consideration from a supplier to its franchisee or the franchise system, unless such a benefit or compensation is disclosed in writing and the benefit or compensation duly explained.⁵²

It is further important to take cognisance of the provisions contained in regulation 2(2)(e). The aforesaid regulation specifically states that any provision contained in a

⁵² Campbell N & Logan S "The Consumer Protection Guide for Lawyers" (August 2011) 25.

franchise agreement that is in conflict with the provisions contained in the regulation that apply in such an instance in terms of the CPA, is void to the extent of such a conflict. The regulatory provisions contained in Section 2(2) thus attempts to limit the benefit that the franchisor will derive from the franchise agreement to that which is contained in the agreement itself.⁵³

Regulation 2(3) of the CPA should be read together with section 7 as it meticulously sets out the minimum content of franchise agreements. The minimum requirements focuses particularly on the financial aspects of franchise agreements but it would now seem that in terms of the CPA more particulars in relation hereto is required than what was the norm in practice.⁵⁴

2.2.5. Regulation 3

Regulation 3 of the CPA requires that a franchisor must give a prospective franchisee a disclosure document that is dated and signed by an authorised officer of the franchisor.⁵⁵

The aim of the disclosure document which the franchisor is expected to provide to the prospective franchisee appears to be predominantly concerned with the financial health of the franchise business holistically.⁵⁶

The disclosure document, which must be provided to the prospective franchisee at least 14 days⁵⁷ before signing of the franchise agreement, must contain the following:

“(a) *the number of individual outlets franchised by the franchisor;*

⁵³ Ibid.

⁵⁴ Louw L “The CPA and franchise agreements” Without Prejudice (July 2011) 33.

⁵⁵ Campbell N & Logan S “The Consumer Protection Guide for Lawyers” (August 2011) 29.

⁵⁶ Louw L “The CPA and franchise agreements” Without Prejudice (July 2011) 33.

⁵⁷ These days are not defined in the regulations and thus appear to be calendar days.

- (b) *the growth of the franchisor's turnover, net profit and the number of individual outlets, if any, franchised by the franchisor for the financial year prior to the date on which the prospective franchisee receives a copy of the disclosure document;*
 - (c) *a statement confirming that there have been no significant or material changes in the company's or franchisor's financial position since the date of the last accounting officer, or auditor's certificate or certificate by a similar reviewer of the company or franchisor, that the company or franchisor has reasonable grounds to believe that it will be able to pay its debts as and when they fall due;*
 - (d) *written projections in respect of levels of potential sales, income, gross or net profits or other financial projections for the franchised business or franchises of a similar nature with particulars of the assumptions upon which these representations are made.*
- (2) *Each page of the disclosure document contemplated in subregulation (1) above must be qualified in respect of the assumptions contained therein."*

In terms of subregulation (3) the disclosure document must also be accompanied by a certificate from the franchisor's auditors or accounting officer certifying that⁵⁸:

- "(a) the business of the franchisor is a going concern;*
- (b) to the best of his or her knowledge the franchisor is able to meet its current and contingent liabilities;*
- (c) the franchisor is capable of meeting all of its financial commitments in the ordinary course of business as they fall due; and*

⁵⁸ Louw L "The CPA and franchise agreements" Without Prejudice (July 2011) 33.

- (d) *the franchisor's audited annual financial statements for the most recently expired financial year have been drawn up—*
- (i) *in accordance with South African generally accepted accounting standards;*
 - (ii) *except to the extent stated therein, on the basis of accounting policies consistent with prior years;*
 - (iii) *in accordance with the provisions of the Companies Act (No. 61 of 1973 or any legislation which replaces this Act), and all other applicable laws; and*
 - (iv) *fairly reflecting the financial position, affairs, operations and results of the franchisor as at that date and for the period to which they relate.”*

In addition to the above and in terms of subregulation 4, the disclosure document must be accompanied by the following:

- “(a) *a list of current franchisees, if any, and of outlets owned by the franchisor, stating, in respect of any franchisee—*
- (i) *the name under which it carries on business;*
 - (ii) *the name of its representative;*
 - (iii) *its physical address; and*
 - (iv) *its e-mail and office telephone number, together with a clear statement that the prospective franchisee is entitled to contact any of the franchisees listed, or, alternatively to visit any outlets operated by a current franchisee to assess the information disclosed by the franchisor and the franchise opportunity offered by it;*

(a) *an organogram depicting the support system in place for franchisees.”*

2.3. Conclusion

The CPA has fundamentally changed the previous essentially self-regulating framework which applied to franchise agreements.⁵⁹ By prescribing formalities and requiring minimum content of franchise agreements duly contained and specifically set out in certain sections of the CPA, the legislature has ensured that a step in the right direction has been taken in relation to regulating this very important business specie in our economic trade.

⁵⁹ Louw L “The CPA and franchise agreements” Without Prejudice (July 2011) 33.

CHAPTER 3: GENERAL PROVISIONS OF THE CONSUMER PROTECTION ACT RELATING TO, OR IMPACTING ON FRANCHISE AGREEMENTS

3.1. Introduction

Notwithstanding the provisions specifically relating to franchise agreements contained in the CPA, as discussed in Chapter 2 hereof, there are also a myriad of other provisions contained in the CPA which directly or indirectly impact on franchise agreements.

The foundation of the aforesaid application can already be found in section 2 of the CPA read together with section 3 of the act and more specifically the following subsections:

“2. (1) This Act must be interpreted in a manner that gives effect to the purposes set out in section 3...

(9) If there is an inconsistency between any provision of this Act and a provision of any Act not contemplated in subsection (8)⁶⁰ —

(a) the provisions of both Acts apply concurrently, to the extent that it is possible to apply and comply with one of the inconsistent provisions without contravening the second; and

(b) to the extent that paragraph (a) cannot apply, the provision that extends the greater protection to a consumer prevails over the alternative provision, provided that in the case of hazardous chemical products only the provisions of this Act relating to consumer redress will apply.

⁶⁰ Subsection 8 states that *“If there is an inconsistency between any provision of Chapter 5 of this Act and a provision of the Public Finance Management Act, 1999 (Act No. 1 of 1999), or the Public Service Act, 1994 (Proclamation No. 103 of 1994), the provisions of the Public Finance Management Act, 1999, or of the Public Service Act, 1994, as the case may be, prevail.”*

- (10) *No provision of this Act must be interpreted so as to preclude a consumer from exercising any rights afforded in terms of the common law.*
3. (1) *The purposes of this Act are to promote and advance the social and economic welfare of consumers in South Africa by—*
- (a) *establishing a legal framework for the achievement and maintenance of a consumer market that is fair, accessible, efficient, sustainable and responsible for the benefit of consumers generally;...*
 - (c) *promoting fair business practices;*
 - (d) *protecting consumers from—*
 - (i) *unconscionable, unfair, unreasonable, unjust or otherwise improper trade practices; and*
 - (ii) *deceptive, misleading, unfair or fraudulent conduct;*
 - (e) *improving consumer awareness and information and encouraging responsible and informed consumer choice and behaviour;*
 - (f) *promoting consumer confidence, empowerment, and the development of a culture of consumer responsibility, through individual and group education, vigilance, advocacy and activism;*
 - (g) *providing for a consistent, accessible and efficient system of consensual resolution of disputes arising from consumer transactions; and*
 - (h) *providing for an accessible, consistent, harmonised, effective and efficient system of redress for consumers.”*

From the above it is clear that the legislature intended to afford the widest possible protection to consumers under the CPA. Consumers, as discussed herein before,⁶¹ include franchisees. It is against this background that the discussion pertaining to various sections providing protection to franchisees, as consumers, and imposing obligations on franchisors, as suppliers, in terms of the CPA, should be viewed.

The discussion that will follow in this chapter duly shows that the CPA is aimed at preventative control in respect of contract terms. This control paradigm is crucial due to the fact that control through other means such as the courts and tribunals, which are reactive in nature, are limited due to amongst other reasons, the costs associated therewith as well as the risk, effort and resources required in respect of dispute resolution and litigation.⁶² It is because of the aforesaid that a number of legal systems, including South Africa, recognise the need for an effective preventative system in respect of unfair terms contained in consumer agreements.⁶³

3.2. Section 22: Right to information in plain and understandable language

In order to achieve a truly balanced relationship between franchisor and franchisee both parties to the agreement needs to fully understand the terms of the franchise agreement being entered into by the said parties.⁶⁴ If one of the parties do not understand the terms of the agreement entered into such a party is disempowered and in an unequal bargaining position in respect of the other contracting party.⁶⁵ In light of the aforesaid the plain language provisions plays a major role in respect of the CPA.⁶⁶

Section 22 of the CPA provides as follows:

⁶¹ Chapter 2 page 4 *supra*.

⁶² Naudé T “Enforcement procedures in respect of the consumer’s right to fair, reasonable and just contract terms under the Consumer Protection Act in comparative perspective” (2010) 515.

⁶³ Naudé T “Enforcement procedures in respect of the consumer’s right to fair, reasonable and just contract terms under the Consumer Protection Act in comparative perspective” (2010) 516.

⁶⁴ Melville NJ “The Consumer Protection Act Made Easy” (2010) Pretoria: Book of Life 157.

⁶⁵ *Ibid*.

⁶⁶ *Ibid*.

- “22. (1) *The producer of a notice, document or visual representation that is required, in terms of this Act or any other law, to be produced, provided or displayed to a consumer must produce, provide or display that notice, document or visual representation—*
- (a) *in the form prescribed in terms of this Act⁶⁷ or any other legislation, if any, or that notice, document or visual representation; or*
- (b) *in plain language, if no form has been prescribed for that notice, document or visual representation.”*

The effect of the wording of section 22 is that the CPA requires that a franchise agreement must be in plain and understandable language in order for an ordinary person, in that instance the franchisee, with average literacy skills and minimal experience in the franchise industry, to comprehend the content, significance and importance of the provisions of the relevant franchise agreement entered into.⁶⁸

It is the responsibility of the franchisor to ensure that the document is in plain and understandable to the type of franchisee that is likely to desire to enter into the relevant franchise agreement.⁶⁹

Section 22(2) goes even further and duly lists the various factors that should be taken into account when determining whether a franchise agreement complies with the above requirements. These factors are:

- “(a) *the context, comprehensiveness and consistency of the notice, document or visual representation;*

⁶⁷ The form of Franchise Agreements is discussed under par 2.3, 2.4 and 2.5 in Chapter 2 hereof.

⁶⁸ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 31.

⁶⁹ Melville NJ “The Consumer Protection Act Made Easy” (2010) Pretoria: Book of Life 114.

- (b) *the organisation, form and style of the notice, document or visual representation;*
- (c) *the vocabulary, usage and sentence structure of the notice, document or visual representation; and*
- (d) *the use of any illustrations, examples, headings or other aids to reading and understanding.”*

Although it is clear that the plain language provisions of the CPA may be interpreted in various ways such interpretation will not be restricted merely to the wording and grammar used in such provisions.⁷⁰ Consequently the plain language provisions will include aspects such as the content, structure and layout of the document and may even take into account elements pertaining to the documents design.⁷¹

The importance of compliance with section 22 is emphasized by both sections 52(2)(g) and 40 respectively⁷² (which will be discussed in more detail herein after). In terms of section 52(2)(g) compliance with section 22 is one of the factors a court must take into account when deciding whether a franchise agreement was entered into in an unfair manner or on unjust terms.⁷³ In some instances this may even contribute to unconscionable conduct as defined in section 40 and may even result in a penalty being imposed on the franchisor in terms of the CPA.⁷⁴

Section 22 thus imposes an obligation on the franchisor to assess the franchisee against the standards set out in said section and to ascertain whether the franchisee would understand the information as far as it related to the franchise agreement and the obligations flowing from the information supplied in terms thereof.⁷⁵

⁷⁰ Melville NJ “The Consumer Protection Act Made Easy” (2010) Pretoria: Book of Life 158.

⁷¹ Ibid.

⁷² Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 32.

⁷³ Ibid.

⁷⁴ Ibid.

⁷⁵ Altini N, Charter C, Jacobs J & Wille D “Consumer Protection Act Matters” (2009) 6.

In addition to the consequences arising from non-compliance with section 22, failure on the part of the franchisor to comply with the requirements of “plain and understandable language” may also leave the franchisor unable to enforce its rights against the consumer as well as the possibility of censure in terms of the enforcement provisions available to the franchisor in terms of the CPA.⁷⁶ The requirements of section 22 also extend to disclosures made by intermediaries or agents of the franchisor and specifically where such an intermediary or agent solicits a franchisee on its behalf.⁷⁷

As with various other similarities with other legislation the plain language provisions contained in the CPA are almost identical to those provisions contained in the NCA and the Companies Act^{78,79} In light of the aforesaid one may revert to authority on the specific provisions in relation to the said acts when seeking further clarity on the plain language provision of the CPA.

3.3. Section 40: Unconscionable conduct

Section 40 prohibits a franchisor from using “*physical force against a consumer, coercion, undue influence, pressure, duress or harassment, unfair tactics or any other similar conduct*” in relation to the following actions:

- “(a) *marketing of any goods or services;*
- “(b) *supply of goods or services to a consumer;*
- “(c) *negotiation, conclusion, execution or enforcement of an agreement to supply any goods or services to a consumer;*

⁷⁶ Altini N, Charter C, Jacobs J & Wille D “Consumer Protection Act Matters” (2009) 7.

⁷⁷ Ibid.

⁷⁸ Act 71 of 2008.

⁷⁹ Melville NJ “The Consumer Protection Act Made Easy” (2010) Pretoria: Book of Life 159.

- (d) *demand for, or collection of, payment for goods or services by a consumer;*
or
 - (e) *recovery of goods from a consumer.*
- (2) *In addition to any conduct contemplated in subsection (1), it is unconscionable for a supplier knowingly to take advantage of the fact that a consumer was substantially unable to protect the consumer's own interests because of physical or mental disability, illiteracy, ignorance, inability to understand the language of an agreement, or any other similar factor."*

A franchise agreement concluded on what is deemed to be unconscionable conduct will result in the agreement to be a prohibited transaction on terms of section 51.⁸⁰ A court will however have to consider the principles, aim and various provisions in terms of the CPA in order to determine whether the relevant franchise agreement falls within the parameters of unconscionable conduct as defined in section 40.⁸¹

In the event that the franchisor, its intermediary or its agent is found to have engaged in unconscionable conduct, the court may make the following orders:

- (i) That the franchisor, its intermediary or its agent restore possession of any property or money to the franchisee; or
- (ii) That the consumer be compensated for any losses in relation to the franchise agreement or the subsequent court proceedings; or

⁸⁰ Section 51(1) states that "A supplier must not make a transaction or agreement subject to any term or condition if—

- (a) its general purpose or effect is to—
 - (i) defeat the purposes and policy of this Act;
 - (ii) mislead or deceive the consumer; or
 - (iii) subject the consumer to fraudulent conduct;.."

⁸¹ Campbell N & Logan S "The consumer protection guide for lawyers" (August 2011) 67.

- (iii) That the franchisor ceases any practice or alters any practice, form or document in order to prevent the franchisor from repetition in future of the unconscionable conduct.⁸²

3.4. Section 41: False, misleading or deceptive representations

In the course of marketing any goods or services, either by words or conduct, section 41 of the CPA prohibits the franchisor from conducting certain actions. Section 41 then proceeds to list these prohibited actions in subsection 1(a) to (c) and well as follows:

- “(a) directly or indirectly express or imply a false, misleading or deceptive representation concerning a material fact to a consumer;*
- (b) use exaggeration, innuendo or ambiguity as to a material fact, or fail to disclose a material fact if that failure amounts to a deception; or*
- (c) fail to correct an apparent misapprehension on the part of a consumer, amounting to a false, misleading or deceptive representation...”*

The above actions once again extend to an intermediary or agent acting on behalf of the franchisee.⁸³

The provisions of section 41 places an onus on the franchisor to remedy any false or misleading apprehension under which a franchisee may labour immediately upon becoming aware of such false or misleading apprehension.⁸⁴

In terms of section 41 false or misleading apprehensions may include the following:

- (i) The franchisor having falsely led the franchisee to believe that:

⁸² Ibid.

⁸³ Section 41(1).

⁸⁴ Campbell N & Logan S “The consumer protection guide for lawyers” (August 2011) 67.

- The particular franchisor has a certain status, affiliation or sponsorship that it does not have; or
- Certain goods pertaining to the franchise agreement are of a particular standard, quality, grade, style or model when it is in fact not; or
- Certain goods are new when it has in fact been used or are reconditioned, except when those goods were only used by the producer, importer, distributor or retailer of such goods for the purposes of testing, service, preparation, shipping or delivery thereof.⁸⁵

3.5. Section 48: Unfair, unreasonable or unjust contract terms

The CPA affords all franchisees the right to terms and conditions in franchise agreements that are fair, reasonable and just.⁸⁶

Consequently section 48 sets a general unfairness standard⁸⁷ prohibiting franchisors from contracting, or offering to contract, on terms that are unreasonable, unfair or unjust.⁸⁸

Section 48 specifically provides that:

- “48. (1) *A supplier must not—*
- (a) *offer to supply, supply, or enter into an agreement to supply, any goods or services—*
 - (i) *at a price that is unfair, unreasonable or unjust; or*

⁸⁵ Ibid.

⁸⁶ Altini N, Charter C, Jacobs J & Wille D “Consumer Protection Act Matters” (2009) 7.

⁸⁷ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 33.

⁸⁸ Naudé T “Enforcement procedures in respect of the consumer’s right to fair, reasonable and just contract terms under the Consumer Protection Act in comparative perspective” (2010) 515.

- (ii) *on terms that are unfair, unreasonable or unjust;*

- (b) *market any goods or services, or negotiate, enter into or administer a transaction or an agreement for the supply of any goods or services, in a manner that is unfair, unreasonable or unjust; or*

- (c) *require a consumer, or other person to whom any goods or services are supplied at the direction of the consumer—*
 - (i) *to waive any rights;*

 - (ii) *assume any obligation; or*

 - (iii) *waive any liability of the supplier,*

on terms that are unfair, unreasonable or unjust, or impose any such terms as a condition of entering into a transaction.”

The aforesaid section gives rise to the question what is deemed to be “unfair, unreasonable or unjust”?⁸⁹ The answer to this question is to be found in the wording of section 48(2) which states that:

“(2) Without limiting the generality of subsection (1), a transaction or agreement, a term or condition of a transaction or agreement, or a notice to which a term or condition is purportedly subject, is unfair, unreasonable or unjust if—

- (a) *it is excessively one-sided in favour of any person other than the consumer or other person to whom goods or services are to be supplied;*

- (b) *the terms of the transaction or agreement are so adverse to the consumer as to be inequitable;*

⁸⁹ Ibid.

- (c) *the consumer relied upon a false, misleading or deceptive representation, as contemplated in section 41 or a statement of opinion provided by or on behalf of the supplier, to the detriment of the consumer; or*
- (d) *the transaction or agreement was subject to a term or condition, or a notice to a consumer contemplated in section 49 (1), and—*
 - (i) *the term, condition or notice is unfair, unreasonable, unjust or unconscionable; or*
 - (ii) *the fact, nature and effect of that term, condition or notice was not drawn to the attention of the consumer in a manner that satisfied the applicable requirements of section 49.”*

Thus terms and conditions may be deemed to be unfair, unreasonable or unjust if it is so skewed to the detriment of the franchisee, and in turn in favour of the franchisor, that it can be seen to be biased or alternatively if the franchisee relied on a deceptive or misleading representation made by the franchisor in concluding the franchise agreement.⁹⁰ In terms of the provisions of the CPA franchisors are also in prevented from marketing any goods or services in and unfair or unjust manner.⁹¹

Deceptive or misleading representations will include words or conduct used by the franchisor concerning a material fact, the use of exaggeration, innuendo, ambiguity or omission on the part of the franchisor to disclose a material fact which may in turn result in deception.⁹²

In addition to the above and where a provision imposes an unusual risk which may result in death or injury the franchisee's attention must specifically be drawn to such provision in plain and understandable language.⁹³ The franchisee's attention will be

⁹⁰ Altini N, Charter C, Jacobs J & Wille D “Consumer Protection Act Matters” (2009) 7.

⁹¹ Campbell N & Logan S “The Consumer Protection Guide for Lawyers” (August 2011) 80.

⁹² Ibid.

⁹³ Altini N, Charter C, Jacobs J & Wille D “Consumer Protection Act Matters” (2009) 7.

deemed to have been drawn to the provision if it is indicated that he had taken note thereof, for example by specifically affixing his signature or initials to the relevant provision.⁹⁴ These provisions must be brought to the attention of the franchisee before the franchise agreement is duly concluded and the franchisee must also be afforded sufficient time to understand the risk.⁹⁵

3.6. Regulation 44: The grey list of contract terms which are deemed to be unfair, unreasonable or unjust

One of the most important mechanisms to effect preventative control in respect of unfair contract terms are lists duly setting out terms that are presumed to be unfair until the relevant supplier or franchisor can convince the court otherwise.⁹⁶

Regulation 44 of the CPA contains a list of contract terms that are commonly found in so called “standard form consumer agreements” and which are deemed to be questionable in terms of the CPA due to the fact that they are onerous and limits the franchisee’s rights resulting in a situation where the franchisee has minimal or no bargaining power.⁹⁷

Although the terms listed in regulation 44 may still be included in franchise agreements the onus will rest on the franchisor to prove that such terms are not unfair in the event of same being challenged by the franchisee.⁹⁸ In addition to the aforesaid the presumption that a term is unfair will only apply in the event that such a term does not pertain to purchases that do not relate to the profession of the franchisee.

⁹⁴ Ibid.

⁹⁵ Ibid.

⁹⁶ Naudé T “Enforcement procedures in respect of the consumer’s right to fair, reasonable and just contract terms under the Consumer Protection Act in comparative perspective” (2010) 535.

⁹⁷ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 37.

⁹⁸ Ibid.

Regulation 44 provides a list of no less than 46 terms that is deemed to be unfair, unreasonable or unjust. The following terms are specifically relevant to franchise agreements:

“44(3) A term of a consumer agreement subject to the provisions of subregulation (1) is presumed to be unfair if it has the purpose or effect of-

- (a) excluding or limiting the liability of the supplier for death or personal injury caused to the consumer through an act or omission of that supplier subject to section 61 (1) of the Act;*
- (b) excluding or restricting the legal rights or remedies of the consumer against the supplier or another party in the event of total or partial breach by the supplier of any of the obligations provided for in the agreement, including the right of the consumer to set off a debt owed to the supplier against any claim which the consumer may have against the supplier;*
- (c) ...*
- (d) limiting, or having the effect of limiting, the supplier's vicarious liability for its agents;*
- (e) forcing the consumer to indemnify the supplier against liability incurred by it to third parties;*
- (f) – (i) ...*
- (j) giving the supplier the right to determine whether the goods or services supplied are in conformity with the agreement or giving the supplier the exclusive right to interpret any term of the agreement;*
- (k) – (o) ...*
- (p) allowing the supplier an unreasonably long time to perform;*

- (q) *allowing the supplier to retain a payment by the consumer where the latter fails to conclude or perform the agreement, without giving the consumer the right to be compensated in the same amount if the supplier fails to conclude or perform the agreement (without depriving the consumer of the right to claim damages as an alternative);*
- (r) *requiring any consumer who fails to fulfil his or her obligation to pay damages which significantly exceed the harm suffered by the supplier;*
- (s) – (u) ...
- (v) *providing that the consumer must be deemed to have made or not made a statement or acknowledgment to his or her detriment, unless –*
 - (i) *a suitable period of time is granted to him or her for the making of an express declaration in respect thereof; and*
 - (ii) *at the commencement of the period the supplier draws the attention of the consumer to the meaning that will be attached to his or her conduct;*
- (w) ...
- (x) *excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, including by requiring the consumer to take disputes exclusively to arbitration not covered by the Act or other legislation;*
- (y) ...
- (z) *imposing a limitation period that is shorter than otherwise applicable under the common law or legislation for legal steps to be taken by the consumer (including for the making of a written demand and the institution of legal proceedings);*

- (aa) *entitling the supplier to claim legal or other costs on a higher scale than usual, where there is not also a term entitling the consumer to claim such costs on the same scale;*
- (bb) *providing that a law other than that of the Republic applies to a consumer agreement concluded and implemented in the Republic, where the consumer was residing in the Republic at the time when the agreement was concluded.”*

It is prudent to note the provisions as set out in Regulation 44(3)(j) and (p) above are provisions specifically relevant to supplier agreements.⁹⁹ In terms of these provisions a supplier must perform in reasonable time and cannot request the consumer to agree to the contrary.¹⁰⁰ Performance outside of the reasonable time period will however be condoned if the non-performance is due to factors that fall outside of the control of the relevant supplier.¹⁰¹

The fact that the legislature has included this grey list supports the spirit, aim and purpose of the CPA and specifically adds to the mechanisms of the act intended to protect consumers and franchisees who are parties to franchise agreements. This grey list also increases the probabilities of the CPA having a fast and preventative effect as franchisors are more likely to remove unfair terms on their own accord if they are given a detailed list, such as the one provided in the CPA, of what terms are deemed to be unfair than if they are merely told in vague terms to “remove unfair terms”.¹⁰²

3.7. Section 55: Consumer’s rights to safe, good quality goods

⁹⁹ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 39.

¹⁰⁰ Ibid.

¹⁰¹ Ibid.

¹⁰² Naudé T “Enforcement procedures in respect of the consumer’s right to fair, reasonable and just contract terms under the Consumer Protection Act in comparative perspective” (2010) 536.

The wording of section 55(2) is very clear and states that:

- “(2) *Except to the extent contemplated in subsection (6), every consumer has a right to receive goods that—*
- (a) *are reasonably suitable for the purposes for which they are generally intended;*
 - (b) *are of good quality, in good working order and free of any defects;*
 - (c) *will be useable and durable for a reasonable period of time, having regard to the use to which they would normally be put and to all the surrounding circumstances of their supply; and*
 - (d) *comply with any applicable standards set under the Standards Act, 1993 (Act No. 29 of 1993), or any other public regulation.”*

Section 55(1) also specifically states that the provisions set out and contained in section 55 does not apply to goods bought in terms of section 45 which pertains to goods purchased at actions as intended in terms of the CPA.¹⁰³

In terms of the common law and a contract of sale of goods, such goods purchased should also be fit for the purpose for which it was intended, failing which the aedilician remedies would be available to the consumer.¹⁰⁴

The effect of the provisions of the CPA however is that a consumer no longer would have to prove that the goods were unfit for the purpose it was intended for at the time of concluding the contract as was the case under common law.¹⁰⁵

¹⁰³ Section 45 states that “*auction*” includes a sale in execution of or pursuant to a court order, to the extent that the order contemplates that the sale is to be conducted by an auction.”

¹⁰⁴ Naudé T “The consumer’s right to safe, good quality goods and the implied warranty of quality under sections 55 and 56 of the Consumer Protection Act 68 of 2008” (2010) 339.

¹⁰⁵ Ibid.

The provisions of section 55 also means that unless a consumer has been expressly informed that the goods purchased are not of a good quality and the consumer in turn having expressly accepted the relevant goods, the consumer has the right to receive goods that are reasonably suited for the purposes they are intended for, of good quality, good working order, free of defects or hazards, usable and durable for a reasonable period having regard to the normal use and the surrounding circumstances of their supply or lease.¹⁰⁶

The following factors may be taken into account when determining whether the goods have met the criteria as set out in section 55:

- (i) The manner in which the goods are marketed and packaged;
- (ii) The purposes for which the goods are marketed and packaged;
- (iii) The use of any trade description or mark;
- (iv) Any instructions or warnings for use of the goods; and
- (v) For what purpose the goods are intended to be used at the time of manufacturing and supply of the goods.¹⁰⁷

In determining whether the goods as supplied in terms of an agreement are reasonably suited for the purposes for which they were generally intended and of good quality, all relevant circumstances surrounding the supply of goods needs to be taken into account.¹⁰⁸ Although the list supplied in this regard in section 55(4) is not exhaustive, it includes the following:

¹⁰⁶ Campbell N & Logan S “The consumer protection guide for lawyers” (August 2011) 87.

¹⁰⁷ Ibid.

¹⁰⁸ Ibid.

- “(a) *the manner in which, and the purposes for which, the goods were marketed, packaged and displayed, the use of any trade description or mark, any instructions for, or warnings with respect to the use of the goods;*
- (b) *the range of things that might reasonably be anticipated to be done with or in relation to the goods; and*
- (c) *the time when the goods were produced and supplied.”*

In addition to all that has been stated above one also needs to take cognisance of the definitions specifically relating to the aspect of safe and good quality goods as set out in section 55(3) and which states as follows:

“55(1) *In this Part, when used with respect to any goods, component of any goods, or services—*

(a) *“defect” means—*

(i) *any material imperfection in the manufacture of the goods or components, or in performance of the services, that renders the goods or results of the service less acceptable than persons generally would be reasonably entitled to expect in the circumstances; or*

(ii) *any characteristic of the goods or components that renders the goods or components less useful, practicable or safe than persons generally would be reasonably entitled to expect in the circumstances;*

(b) *“failure” means the inability of the goods to perform in the intended manner or to the intended effect;*

(c) *“hazard” means a characteristic that—*

- (i) *has been identified as, or declared to be, a hazard in terms of any other law; or*
 - (ii) *presents a significant risk of personal injury to any person, or damage to property, when the goods are utilised; and*
- (d) *“unsafe” means that, due to a characteristic, failure, defect or hazard, particular goods present an extreme risk of personal injury or property damage to the consumer or to other persons.”*

The wording at the outset of section 55(3), i.e. *“component of any goods, or services”* indicates that a non-compliant clause may be severed when the franchise agreement is interpreted or enforced.¹⁰⁹ When reading sections 55(2) and 55(6)¹¹⁰ it is clear that in relation to an agreement to which the CPA applies the common law voetstoots clause will no longer protect a supplier from latent defects.¹¹¹ When having further regard to the discussions pertaining to section 55(2) above it is also clear that the supplier or franchisor will be liable for patent defects unless same was disclosed to the consumer and he accepted same after said disclosure.¹¹²

3.8. Section 56: Implied warranty of quality

Section 56 imposes an implied warranty against defective goods which warranty operates *ex lege*.¹¹³

¹⁰⁹ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 41.

¹¹⁰ Section 55(6) states as follows: *“Subsection (2)(a) and (b) do not apply to a transaction if the consumer—*

has been expressly informed that particular goods were offered in a specific condition; and has expressly agreed to accept the goods in that condition, or knowingly acted in a manner consistent with accepting the goods in that condition.”

¹¹¹ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 44.

¹¹² Ibid.

¹¹³ Ibid.

All goods sold and delivered, whether it is new or used, is subject to a six month warranty of quality subject of course to the exception where the defect was expressly divulged to the consumer and the consumer having expressly accepted the goods subject to said divulged defect.¹¹⁴ The aforesaid provision was inserted in the CPA to dispose of situations where the supplier could limit warranties to extremely short periods or dispose of a basis for claims in terms of the warranty against defective goods.¹¹⁵ Due to the fact that this warranty is implied it does not need to be recorded in an agreement of sale and affords the consumer the right to return defective goods within a period of 6 months after delivery and may then elect whether the consumer wants the goods repaired or replaced.¹¹⁶ This said return or repair is subject to certain conditions.¹¹⁷

Should the consumer elect that the goods be repaired then there will be an implied three month warranty on the said repair.¹¹⁸ It is of importance to take note that suppliers will not be able to contract out of this implied warranty and terms and conditions entered into that are *contra* the provisions of section 56 will be deemed void by the CPA.¹¹⁹

3.9. Direct marketing in terms of the CPA

Although the CPA does not prohibit direct marketing it does provide strict provisions in terms whereof this practice is to be conducted and affords the consumer both the right to restrict unwanted direct marketing as well as a so called cooling-off right.¹²⁰

¹¹⁴ Altini N, Charter C, Jacobs J & Wille D “Consumer Protection Act Matters” (2009) 4.

¹¹⁵ Ibid.

¹¹⁶ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 44.

¹¹⁷ The conditions contained in section 56(1) is found in the latter half of the wording which states that the return or repair as referred to above will apply “...*except to the extent that those goods have been altered contrary to the instructions, or after leaving the control, of the producer or importer, a distributor or the retailer, as the case may be.*”

¹¹⁸ Altini N, Charter C, Jacobs J & Wille D “Consumer Protection Act Matters” (2009) 4.

¹¹⁹ Ibid.

¹²⁰ Van Heerden C “Franchise agreements and the Consumer Protection Act: Compliance and Drafting” (June 2012) 45.

In order to regulate direct marketing practices the CPA contains several sections duly setting out the rights of consumers on the one hand and the obligations of suppliers on the other, i.e. sections 11, 12, 16 and 32.

Section 11(1) states that every person has the right to privacy including “...*the right to—*

- (a) *refuse to accept;*
- (b) *require another person to discontinue; or*
- (c) *in the case of an approach other than in person, to pre-emptively block, any approach or communication to that person, if the approach or communication is primarily for the purpose of direct marketing.”*

Section 12, read together with the applicable regulation notice, prohibits a supplier from engaging a consumer in direct marketing at home on Sundays, Saturdays or public holidays before the hours of 09h00 and after 13h00 or on any other day between the hours of 20h00 and 08h00 unless the consumer has agreed or requested the contrary.¹²¹

Section 16 read together with section 32 deals with the cooling-off right afforded to consumers in the event of direct marketing and the relevant wording of these sections are the following:

“16(3) A consumer may rescind a transaction resulting from any direct marketing without reason or penalty, by notice to the supplier in writing, or another recorded manner and form, within five business days after the later of the date on which—

- (a) *the transaction or agreement was concluded; or*

¹²¹ Section 12.

- (b) *the goods that were the subject of the transaction were delivered to the consumer.*

- (4) *A supplier must—*
 - (a) *return any payment received from the consumer in terms of the transaction within fifteen business days after—*
 - (i) *receiving notice of the rescission, if no goods had been delivered to the consumer in terms of the transaction; or*
 - (ii) *receiving from the consumer any goods supplied in terms of the transaction; and*

 - (b) *not attempt to collect any payment in terms of a rescinded transaction, except as permitted in terms of section 20(6).”*

- “32. (1) *A person who is directly marketing any goods or services, and who concludes a transaction or agreement with a consumer, must inform the consumer, in the prescribed manner and form, of the right to rescind that agreement, as set out in section 16.*
- (2) *If a person who has marketed any goods as contemplated in subsection (1) left any goods with the consumer without requiring or arranging payment for them, those goods are unsolicited goods, to which section 21 applies.”*

The aforesaid sections thus compels the supplier to inform the consumer of this cooling-off right to rescind the agreement resulting from direct marketing within five business days after the transaction was concluded or the goods delivered to the consumer.¹²²

¹²² Campbell N & Logan S “The consumer protection guide for lawyers” (August 2011) 87.

3.10. Conclusion

From the above it is clear that the CPA contains various other provisions in addition to those which specifically bear on franchise agreements and which provide general consumer protection to franchisees and impose obligations on franchisors.

It would seem that the legislature achieves its aim in striving to ensure that franchisees as consumers are afforded numerous rights which they may enforce against franchisors as suppliers. The franchisors on the other hand now become efficiently regulated in terms of these provisions of the CPA.

CHAPTER 4: CONCLUSION

An efficient manner in which a business may expand its operations and for would-be entrepreneurs to get started in business is by utilising the franchise industry.¹²³ Consumer policy contained in legislation like the CPA may be a well-accepted mechanism to promote consumer interests in the marketplace and make business practices in relation to the franchise industry more efficient.¹²⁴

Due to the nature of the franchising relationship, both the franchisor and the franchisee run a variety of risks upon embarking on a franchise agreement.¹²⁵ The franchisor for example, may not recover the investment he has made establishing the franchisee in business or that due to the inefficient manner in which the franchisee operates the franchise, harm is done to the good will of the franchisor resulting in a damaged name.¹²⁶

The franchisee on the other hand is at risk in that the franchisor may have exaggerated the profitability of the franchise, may not properly or effectively market the franchise brand or that all the amounts payable by the franchisee to the franchisor, in respect of initial franchise fees, royalties, purchases and the like, render the franchise unprofitable.¹²⁷ The aforesaid risks were not mitigated by clear and comprehensive legislation prior to the enactment of the CPA.

In light of the massive economic contribution that the franchise industry plays in our South African economy it is surprising that there had not been specific legislation governing the franchise industry before the enactment of the CPA. There was certainly a need for legislation providing carefully structured checks and balances together with safety nets of some sort which took into account both the needs and

¹²³ Melville NJ "The Consumer Protection Act Made Easy" (2010) Pretoria: Book of Life 109.

¹²⁴ Du Preez M "The Consumer Protection Bill: A few preliminary comments" (2009) (1) *Journal of South African Law* 82.

¹²⁵ Van Eeden E "Consumer Protection Law in South Africa" (2009) LexisNexis 212.

¹²⁶ Ibid.

¹²⁷ Ibid.

interests of franchisors as well as franchisees in order to make this free-market franchise industry work.¹²⁸

Certain specific provisions of the CPA now regulate the franchise industry and will the terms and conditions of franchise agreements now have to comply with the provisions of the CPA.¹²⁹

With the enactment of the CPA the law pertaining to franchise agreements was changed in four material ways:¹³⁰

- (i) Compliance with new formalities that the CPA has introduced include that a franchise agreement must be in writing, the content thereof must be in plain and understandable language and the franchise agreement must be signed by the franchisee.¹³¹
- (ii) The inclusion of a mandatory clause in terms of section 7(2) of the CPA drawing the attention of the franchisee to the fact that the franchisee has a statutory cooling off period of 10 business days from date of entering into the relevant franchise agreement and in which period the franchisee may cancel the said franchise agreement without cost or penalty.¹³²
- (iii) The CPA duly provides certain terms that must be included in franchise agreements and also which contract terms may not and will therefore be void if included in franchise agreements.¹³³

¹²⁸ Woker T “Why the need for consumer protection legislation? A look at some of the reasons behind the promulgation of the National Credit Act and the Consumer Protection Act” (2010) *Obiter* 231.

¹²⁹ Rhodie L and Scriba B “Franchise agreements and the Consumer Protection Act” (September 2011).

¹³⁰ Louw L “The CPA and franchise agreements” *Without Prejudice* (July 2011) 32.

¹³¹ *Ibid.*

¹³² *Ibid.*

¹³³ *Ibid.*

- (iv) The CPA also prescribes a so-called disclosure document which must be provided to the franchisee at least 14 business days before the franchise agreement is concluded and which sets out certain information that must be supplied to the franchisee accordingly.¹³⁴

From what has been discussed in this paper it is clear that there are certain provisions of the CPA that apply exclusively to franchise agreements, that there are other provisions that will not apply to franchise agreements and lastly that there are provisions of the CPA that will apply to consumers generally and in consequence of which also to franchisees.¹³⁵

One of the aims of the CPA is to redress the bargaining inequality between franchisee and franchisor which was rife prior to the enactment of the CPA. The reason that a franchisee is now treated as a consumer is to prevent this abuse of a vulnerable franchisee with less bargaining power and who have often invested their life savings in the relevant franchise.¹³⁶

In consequence of the enactment and provisions of the CPA South African consumers, and also franchisees, can be regarded as some of the most protected consumers in the world¹³⁷ with some singing the praises of the CPA as one of the best consumer protection acts on the continent of Africa.¹³⁸

Although most writers referred to in this paper have expressed their view of the interpretations of the provisions of the CPA, the practical effects of franchisors not complying with the said provisions when entering into franchise agreements will only become apparent in years to come.¹³⁹ These effects will become apparent after

¹³⁴ Ibid.

¹³⁵ Van Eeden E "Consumer Protection Law in South Africa" (2009) LexisNexis 218.

¹³⁶ Melville NJ "The Consumer Protection Act Made Easy" (2010) Pretoria: Book of Life 111.

¹³⁷ Lester T and Posthumus C "An overview of the Consumer Protection Act" (May 2010).

¹³⁸ Melville NJ "The Consumer Protection Act Made Easy" (2010) Pretoria: Book of Life xiii.

¹³⁹ Rhodie L and Scriba B "Franchise agreements and the Consumer Protection Act" September 2011.

findings are made by the National Consumer Tribunal, the Consumer Court or the National Consumer Commission.¹⁴⁰

Notwithstanding the various new challenges franchisors are faced with in terms of the burdensome provisions of the CPA, such risks and challenges may be mitigated and managed by carefully assessing the extent to which the CPA impacts on the particular franchise's operations and adapting thereto accordingly.¹⁴¹

Although franchisors and franchisees will both have to familiarise themselves of the provisions of the CPA one should also appreciate that legislation of the nature of the CPA can never be a substitute for good customer relations, proper communication and sound business practises.¹⁴²

In conclusion it is clear that the CPA has forever changed the regulation of the franchise industry. Only time and the consequential interpretation of the provisions of the CPA will tell whether this change brought about is for better or worse for the franchise industry.¹⁴³

¹⁴⁰ Ibid.

¹⁴¹ Meyer C "Consumer Protection Act regulations an urgent wakeup call for franchisors" (July 2011).

¹⁴² Du Preez M "The Consumer Protection Bill: A few preliminary comments" (2009) 76.

¹⁴³ Rhodie L and Scriba B "Franchise agreements and the Consumer Protection Act" (September 2011).

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