

## Legal Protection of the Right to Associate

### A. Introduction

The right to associate freely with others is essential to the health of a democratic society. Indeed, the right of individuals to associate is a fundamental freedom guaranteed by section 2(d) of the *Canadian Charter of Rights and Freedoms*.<sup>1</sup> While the *Charter* aims to protect the freedoms of individuals from the exercise of governmental powers and is therefore not directly applicable to the franchisor-franchisee relationship, the principles that the courts in Canada have developed with respect to the freedom of association, particularly in relation to labour unions, could in time inform to some degree the judicial interpretation of the right of franchisees to associate. In one Ontario decision, the court suggested that this might be the case without deciding the issue.<sup>2</sup>

In the labour context, the right to associate and form unions is the primary tool that employees possess to improve working conditions and enhance their overall economic well-being. Unions are also the means by which workers protect themselves from the perceived excesses of unscrupulous employers. Needless to say, not all employers treat their workers unfairly. The rise of labour unions harkens back to time when the employer-employee relationship was commonly described as that of master and servant. Labour was seen as a tool to be used as the employer saw fit. Those conditions have been ameliorated to a large extent in recent times. Nonetheless, labour unions have retained their prominent position in the Canadian marketplace.

Franchisee associations afford their members similar advantages. To date, four provinces, Ontario, Prince Edward Island, New Brunswick and Alberta, have enacted legislation that governs the franchisee-franchisor relationship. The Manitoba legislature has also put forward a bill regarding franchising. Each imposes pre-contractual disclosure obligations on the franchisor and allows prospective franchisees the opportunity to rescind franchise agreements if the disclosure obligations are not met. Each statute also imposes the duty of fair dealing on parties to franchise agreements. Most importantly from the standpoint of this discussion, all specifically protect the right of franchisees to associate with each other free from interference by the franchisor.

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<sup>1</sup> *Canadian Charter of Rights and Freedoms*, Part 1 of the *Constitution Act, 1982*, being Schedule B of the *Canada Act 1982* (U.K.), 1982, c. 11.

<sup>2</sup> *2038724 Ontario Ltd. v. Quizno's Canada Restaurant Corp.*, 2008 CarswellOnt 1156, 89 O.R. (3d) 252, 56 C.P.C. (6th) 88 (Ont. S.C.J.); reversed 2009 CarswellOnt 2533, 96 O.R. (3d) 252, 70 C.P.C. (6th) 27 (Ont. Div. Ct.); affirmed 2010 ONCA 466, 2010 CarswellOnt 4305, 100 O.R. (3d) 721 (Ont. C.A.).

## **B. Legislation: The Right to Associate**

### **1. Ontario**

The importance of the right of franchisees to associate in the eyes of Ontario lawmakers was evident in the proceedings leading up to the passing of the *Arthur Wishart Act (Franchise Disclosure)*, 2000.<sup>3</sup> Bill 33, which eventually became the Act, was entitled “An Act to require fair dealing between parties to franchise agreements, to ensure that franchisees have the right to associate and to impose disclosure obligations on franchisors.” On the day Bill 33 was passed, one member of the Ontario Legislative Assembly made the following comment:

“We heard far too often in those hearings that one of the single biggest problems franchisees faced was the inability to associate with their peers. In many cases, the franchise agreement expressly prohibited their sharing information, even in some cases sitting down and having a coffee with their colleagues running comparable franchises elsewhere in the province. We think that’s wrong.”

The Legislature followed through with that sentiment and firmly established the right to associate. Section 4 of the Act specifically states:

- “4. (1) A franchisee may associate with other franchisees and may form or join an organization of franchisees.
- (2) A franchisor and a franchisor’s associate shall not interfere with, prohibit or restrict, by contract or otherwise, a franchisee from forming or joining an organization of franchisees or from associating with other franchisees.
- (3) A franchisor and franchisor’s associate shall not, directly or indirectly, penalize, attempt to penalize or threaten to penalize a franchisee for exercising any right under this section.
- (4) Any provision in a franchise agreement or other agreement relating to a franchise which purports to interfere with, prohibit or restrict a franchisee from exercising any right under this section is void.
- (5) If a franchisor or franchisor’s associate contravenes this section, the franchisee has a right of action for damages against the franchisor or franchisor’s associate, as the case may be.”

In plain English, franchisees in Ontario have an absolute right to associate with one another.<sup>4</sup> A franchisor is not at liberty to interfere with that right and any attempt to do so will not be countenanced by the law. Furthermore, a provision in a franchise agreement that purports to prohibit or limit the right will be of no force or effect. Importantly, the Legislature put teeth into this provision by entitling franchisees to sue for damages as a result of a franchisor’s interference with the right.<sup>5</sup> This is a significant aspect of the right to associate. The knowledge that they

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<sup>3</sup> S.O. 2000, c. 3 (the “Ontario Act”)

<sup>4</sup> Although the authors are not aware of any decisions in provinces that do not have franchise legislation that protect the rights of franchisees to associate, the authors believe that the right to associate would likely also be protected by the courts in those provinces.

<sup>5</sup> Although the authors are not aware of any decisions in Canada awarding damages for a franchisor’s breach of a franchisee’s statutory right to associate, the authors believe that a breach of this right constitutes a separate head of

could be taken to court will deter franchisors from attempting to isolate their franchisees or prevent them from reaching out to others within the system for mutual aid and support. Conversely, franchisees should feel more secure with the knowledge that their franchisors cannot prevent them from discussing common issues with other members of the system and that they will not be exposing themselves to potentially damaging litigation if they choose to exercise that right. In addition, the courts appear willing to extend the reach of existing franchising legislation to extra-provincial franchise relationships, at least in certain circumstances. As mentioned previously, the Ontario Court of Appeal has applied the Ontario franchising statute to the relationship between a franchisor and franchisees located outside of Ontario on the grounds that the franchise agreements in question expressly stated that the laws of Ontario governed the relationship.<sup>6</sup>

## 2. Prince Edward Island

The right to associate is found in section 4 of the Prince Edward Island *Franchises Act*.<sup>7</sup> The language of that provision is identical to s. 4 of the Act. Thus, the rights granted to franchisees in Prince Edward Island appear to be the same as those enjoyed by Ontario franchisees.

## 3. New Brunswick

The right to associate embodied in s. 4 of the New Brunswick *Franchises Act* mirrors the language of the Ontario and P.E.I. statutes.<sup>8</sup> As such, the scope of the rights protected by s. 4 appear to be identical to those protected by the corresponding provisions of the Ontario and P.E.I. Acts and will, in all likelihood, be interpreted in a similar manner.

## 4. Manitoba

Although not yet in force, the Manitoba legislature has proposed its own franchise legislation in the form of Bill 15, *The Franchises Act*.<sup>9</sup> Although stated in somewhat different language, the right to associate contained in section 4 of the Bill appears to be identical in substance to the equivalent provisions in the Ontario, PEI and New Brunswick legislation.

## 5. Alberta

Alberta was the first province to enact franchise legislation. The original statute has since been repealed and replaced. The right to associate is found in section 8 of the current *Franchises Act*.<sup>10</sup> The language of that provision differs markedly from the other provincial franchise legislation. Despite the different wording, the Alberta Act also makes it unlawful for franchisors to prohibit franchisees from associating (s. 8(1)) or to penalize those who do so (s. 8(2)). In addition, the Act grants aggrieved franchisees a right to sue franchisors for a breach of the right to associate (s. 11).

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damages much in the same way that a breach of the statutory duty of fair dealing is a separate head of damages. See Abdulhamid Salah and *Salah v. Timothy's Coffees of the World Inc.*, 2010 ONCA 673, 2010 CarswellOnt 7643, 74 B.L.R. (4th) 161, ¶22–30 (Ont. C.A.).

<sup>6</sup> 405341 *Ontario Limited v. Midas Canada Inc.*, 2009 CarswellOnt 6283, 64 B.L.R. (4th) 251 (Ont. S.C.J.); affirmed 2010 ONCA 478, 2010 CarswellOnt 4714, 70 B.L.R. (4th) 1 (Ont. C.A.).

<sup>7</sup> R.S.P.E.I. 1988, c. F-14.1 (the “P.E.I. Act”).

<sup>8</sup> S.N.B. 2007, c. F-23.5 (the “New Brunswick Act”).

<sup>9</sup> C.C.S.M. F156 (the “Manitoba Bill”).

<sup>10</sup> R.S.A. 2000, c. F-23 (the “Alberta Act”).

## 6. Uniform Law Conference of Canada

While none of the other common law provinces or territories has enacted franchise legislation, the Uniform Law Conference of Canada, an organization made up of representatives of the provincial and federal governments whose function is to propose uniform laws in a wide variety of areas for adoption throughout the country, has recommended the implementation of a *Uniform Franchises Act*. The right to associate is contained in section 4 of the proposed statute. The language of that provision is identical to s.4 of the Ontario, PEI and New Brunswick Acts. Although the *Uniform Franchises Act* is only a recommendation and does not carry the force of law, it is strong indication from an important national advisory body that the relationship between franchisors and franchisees should be regulated in a consistent manner and that the right to associate should be enshrined in the law across the country.

### C. The Duty of Fair Dealing

Each of the provincial Acts<sup>11</sup> and the *Uniform Franchises Act*<sup>12</sup> imposes upon the parties to franchise agreements a duty of fair dealing in the performance and enforcement of franchise agreements. The duty applies to all aspects of the parties' respective rights and obligations embodied in the franchise agreement. While the content of this duty has yet to be fully fleshed out by the courts, many members of the legal community have suggested that the duty of fair dealing will inform how the parties will be expected to deal with each other over a wide range of issues. It is also expected that the principles developed by the courts concerning the duty of fair dealing will inform to some extent the judicial interpretation of the right to associate.

The duty of fair dealing in the Ontario, PEI and New Brunswick Acts, the Manitoba Bill and the *Uniform Franchises Act* expressly includes the duty to act in good faith and in accordance with reasonable commercial standards. In contrast, the *Alberta Act* does not define the duty of fair dealing. Interestingly, section 2(c) of that statute states that one of the purposes of the Act "is to provide a means by which franchisors and franchisees will be able to govern themselves and promote fair dealing among themselves." Although this provision does not impose a specific duty on or grant a specific right to either party, it is not expressly limited to the performance and enforcement of franchise agreements. Rather, it appears to be a general interpretive tool to guide the courts in the application of the legislation to particular franchisee-franchisor relationships. None of the other provincial franchising statutes contain a comparable provision.

The terms "good faith" and "reasonable commercial standards" are not defined in the legislation. However, the duty of good faith has been interpreted by the courts. In the seminal case of

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<sup>11</sup> The Ontario Act, s. 3; the P.E.I. Act, s. 3; the New Brunswick Act, s. 3; The Manitoba Bill, s. 3; and the Alberta Act, s. 7.

<sup>12</sup> Section 3.

*Shelanu Inc. v. Print Three Franchising Corp.*,<sup>13</sup> the Ontario Court of Appeal had occasion to consider the duty of good faith in the context of franchise agreements. The court stated that the duty, while allowing each party to act in its own self-interest, imposes on each an obligation to take the legitimate interests of the other into consideration when exercising the powers conferred upon it by the franchise agreement. That is, a franchisor must take the interests of its franchisees into consideration when it decides to act on the terms of the franchise agreement. The converse is equally true and the franchisee must give equal consideration to the interests of the franchisor. The duty of good faith has also been employed by the courts to ensure that the parties to a contract do not act in a way that defeats the objectives of the agreement reached.<sup>14</sup>

Although the decision in *Shelanu Inc. v. Print Three Franchising Corporation* predates the Act, it seems likely that the courts, in Ontario at least,<sup>15</sup> will interpret the statutory fair dealing obligation, which includes the duty to act in good faith, in a manner consistent with statements of the Ontario Court of Appeal. That is, the parties must exercise the rights and comply with the obligations set out in the franchise agreement in a manner commensurate with the duty of good faith. However, there are limits to how the duty of good faith can affect or modify the parties' rights and obligations under the contract. The terms of a franchise agreement freely entered into remain paramount and the duty of fair dealing cannot be relied upon to alter the terms of an agreement that is unimpeachable on other grounds.<sup>16</sup>

Subsection 3(2) of the Ontario, PEI and New Brunswick Acts, and the Manitoba Bill, each grant a party to a franchise agreement the right to bring an action for damages against any other party who breaches the duty of fair dealing in the performance or enforcement of the agreement. To date, the courts in these provinces have not developed an extensive body of case law dealing with the question of damages for breaches of the duty of fair dealing.

However, in one Ontario case,<sup>17</sup> damages for breach of this duty were awarded to a franchisee for the franchisor's failure to provide key information despite repeated requests, for keeping the franchisee in the dark about negotiations between it and the landlord that bore directly on the future of the franchise and for falsely stating that it would require a payment of \$350,000 for the franchisee to take up a new location in the shopping mall in question. Specifically, damages in the amount of \$50,000 were awarded for breach of "the duty of good faith" and for the mental distress. The Alberta Act, in contrast, does not prescribe a remedy that an innocent party can pursue for a breach of duty of fair dealing. Rather, it simply states that "every franchise agreement imposes on each party a duty of fair dealing in its performance and enforcement."<sup>18</sup>

As the courts have yet to fully explore the limits of the fair dealing obligation in any of the provinces that have franchise legislation, it remains to be seen how the duty might interact with

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<sup>13</sup> 2003 CarswellOnt 2038, 64 O.R. (3d) 533, 172 O.A.C. 78 (Ont. C.A.).

<sup>14</sup> *CivicLife.com Inc. v. Canada (Attorney General)*, 2006 CarswellOnt 3769, 215 O.A.C. 43, ¶49 (Ont. C.A.).

<sup>15</sup> For example, see *Salah v. Timothy's Coffees of the World Inc.*, 2009 Carswell- Ont 6470, 65 B.L.R. (4th) 235 (Ont. S.C.J.); affirmed 2010 ONCA 673, 2010 CarswellOnt 7643, 74 B.L.R. (4th) 161 (Ont. C.A.).

<sup>16</sup> *Pointts Advisory Ltd. v. 754974 Ontario Inc.*, 2006 CarswellOnt 5293 (Ont.S.C.J.).

<sup>17</sup> *Salah v. Timothy's Coffees of the World Inc.*, *supra*, note 12.

<sup>18</sup> *Supra*, note 8.

the statutory right of association. That will have to wait until the courts have the opportunity to resolve the issue in the context of a specific factual situation.

#### **D. Judicial Interpretation**

To date, none of the statutory rights of association discussed above has been considered to any great depth by the courts. However, the Ontario Court of Appeal has considered the right to associate in the context of a case regarding the certification of class proceedings. In *405341 Ontario Limited v. Midas Canada Inc.*,<sup>19</sup> franchisees within the system commenced a class proceeding claiming damages from the franchisor allegedly suffered as a result of fundamental changes made by the franchisor to the product supply chain and applied to the court for certification. A subsidiary question arose with respect to a provision in the franchise agreements in question requiring the franchisees to execute a release as a condition of renewing or assigning their franchises. The Court of Appeal specifically stated that a provision in a franchise agreement requiring franchisees to sign such a release, which would have prevented those franchisees from participating in the class proceeding, violated the right to associate contained in section 4 of the Act.<sup>20</sup>

The court from which the appeal was taken, on the other hand, was of the view that the provisions in the franchise agreement requiring franchisees to execute a release as a condition of renewal or assignment were void and of no effect by virtue of subsection 4(4) of the Act to the extent that they interfered with the right to associate.<sup>21</sup> While this conclusion might appear obvious, the Court of Appeal did not go so far and did not conclude that the offending provisions were null and void. The ultimate resolution of the issue will have to wait until a decision is rendered after the trial of the class proceeding.

In another Ontario case,<sup>22</sup> the court considered a provision in a franchise agreement placing a limit on the amount that franchisees could pay for legal and accounting expenses. A dispute arose between the franchisor and the franchisees. The franchisees retained counsel to assist them in resolving the dispute. The franchisor became aware that the franchisees had withdrawn funds from their franchises for legal fees in excess of the stipulated limit. When counsel for the franchisees advised the franchisor that litigation would be commenced if an acceptable resolution to the dispute could not be reached, the franchisor threatened to terminate the franchisees, taking the position that the franchisees were in breach of their agreements by exceeding the allowable limit on legal and accounting fees. The franchisees commenced their action against the franchisor and sought an injunction to prevent the franchisor from terminating the franchise agreements. Although the court did not have to make a final determination on the issue, it stated that there was a serious issue to be tried as to whether the franchisor's proposed termination of the franchise agreements in the circumstances of the case amounted to interference with the franchisees' right to associate.<sup>23</sup>

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<sup>19</sup> 2010 ONCA 478, 2010 CarswellOnt 4714, 70 B.L.R. (4th) 1 (Ont. C.A.).

<sup>20</sup> *Ibid.*, at ¶39.

<sup>21</sup> 2009 CarswellOnt 6283, 64 B.L.R. (4th) 251, ¶22 (Ont. S.C.J.).

<sup>22</sup> *1318214 Ontario Ltd. v. Sobeys Capital Inc.*, 2010 ONSC 4141, 2010 Carswell-Ont 5470, 72 B.L.R. (4th) 110 (Ont. S.C.J. [Commercial List]).

<sup>23</sup> *Ibid.*, at ¶31.



While the scope of the statutory right of franchisees to associate remains as yet uncertain, additional guidance can perhaps be taken from decisions involving labour unions. The Supreme Court of Canada recently reviewed the law regarding collective bargaining and freedom of association under the *Canadian Charter of Rights and Freedoms*.<sup>24</sup> The court recognized that freedom of association had in the past been limited to protecting the basic right of union members to meet. That is, the protection did not extend the actual activities of the union and its members. Breaking with previous case law on the subject, the Supreme Court of Canada extended constitutional protection to collective bargaining, that is, to an important union activity. However, the court was careful to limit the scope of the newly expanded protection to collective bargaining only, which it described as a right to a process, and stressed that such protection did not guarantee a particular economic outcome from the bargaining process.

These principles could have ramifications for franchisee associations. While the various franchise statutes do protect the right to associate, they are silent with respect to the affairs and activities of franchisee associations. It is a significant leap to say that a similar expansion of the right to associate contained in the various franchising statutes will happen in the foreseeable future. However, the same issues that were faced by the Supreme Court with respect to labour unions could arise in the franchise context. Indeed, as stated above, one Ontario court has expressed the view that any exploration of the scope of the statutory right of franchisees to associate will entail principles similar to those developed by the courts in the context of freedom of association under the *Charter*.<sup>25</sup>

Whatever the scope of the right to associate might be, the law is clear that the activities of a franchisee association and its members must be legal. Thus, the members of such an association must not act in a manner that breaches the specific obligations imposed upon them by their respective franchise agreements or under the applicable legislation. If they do, the right of association will afford no protection. By extension, the association and its members cannot act in a way that causes one or more members to breach their agreements without exposing those franchisees to potential litigation.

Accordingly, careful consideration must be given to the obligations imposed upon individual franchisees when developing strategies to deal with issues involving the franchisor. Given the state of law in this area, legal advice is essential.

Another limitation on the activities of a franchisee association is related to what is known as standing. The legal relationship between franchisees and franchisors is governed in most part by the franchise agreement. Franchisee associations are not parties to such agreements and the rights and obligations contained in them apply only to the named franchisee and the franchisor. Thus, a franchisee association cannot take legal action against the franchisor on behalf of a franchisee. Nor can it defend a lawsuit commenced by the franchisor against a particular franchisee. That is not to say, however, that franchisee associations cannot provide support,

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<sup>24</sup> *Health Services & Support-Facilities Subsector Bargaining Assn. v. British Columbia*, 2007 SCC 27, 2007 CarswellBC 1289, [2007] 2 S.C.R. 391 (S.C.C.).

<sup>25</sup> *2038724 Ontario Ltd. v. Quizno's Canada Restaurant Corp.*, *supra*, note 2, (S.C.J.) at ¶66.

financial or otherwise, to franchisees that are experiencing difficulties in their relationship with the franchisor. Indeed, that is their most important role—to act on behalf of their members to advance their interests. By doing so, franchisee associations can exert whatever influence they have to the betterment of their members and, in turn, to the system as a whole.

Similarly, although existing franchise legislation imposes on each party to a duty of fair dealing in the performance and enforcement of franchise agreements, the duty does not extend to franchisee associations. That is the duty of fair dealing does not impose upon a franchisor the obligation to accept the legitimacy of, or communicate with, a franchisee association as being a representative of its franchisees. Furthermore, the prohibition against a franchisor penalizing, attempting to penalize or threatening to penalize a franchisee for exercising the right to associate does not prevent a franchisor from enforcing its rights under a franchisee agreement arising from the breach of the agreement by the franchisee.<sup>26</sup> Franchisee associations may take many forms and perform myriad functions within the broad legal parameters outlined above.

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<sup>26</sup> *Quizno's Canada Restaurant Corp. v. 1450987 Ontario Corp.*, 2009 Carswell-Ont 2280 (Ont. S.C.J.).