Five tips for franchise agreements

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South Africa has some great homegrown franchises – Mugg and Bean, Steers, Debonairs and Nandos, to name a few. South Africa is also no stranger to international franchise groups, such as McDonalds, KFC, Wimpy and SPAR, although there has been an increase in the number of international franchises investing in South Africa in recent years.

The Consumer Protection Act, No 68 of 2008 ("CPA") is the first piece of legislation in South Africa that specifically regulates franchise agreements. The CPA prescribes certain minimum requirements for franchise agreements, as well as certain information that must be disclosed prior to a franchise agreement being signed. It is important that all franchise agreements comply with the CPA as provisions in franchise agreements may be declared to be void for non-compliance.

Below are five tips to ensure that your franchise agreement complies with the CPA:

1. Make sure you meet the minimum requirements

The CPA prescribes "minimum requirements" for franchise agreements. These requirements, which are set out in the Regulations to the CPA, set out mandatory terms (i.e. terms which must be included) and prohibited terms (i.e. terms which must not be included). They also prescribe that franchise agreements must be drafted in simple and plain language so as to be easily understood. Legal jargon must be avoided unless absolutely necessary.

2. Include prescribed minimum information

The CPA prescribes minimum information that must be included in a franchise agreement. Most of this minimum prescribed information is fairly general in nature and would be contained in the franchise agreement in the ordinary course (for example, name and description of the types of goods or services that the franchise relates to, the obligations of the franchisor and franchisee, and any territorial rights). There are, however, certain more unusual requirements in relation to prescribed information, which information would not necessarily be contained in a franchise agreement in the ordinary course (for example, the qualifications of the franchisor's directors, and details of the members/shareholders of the franchisor). These more unusual requirements must be kept in mind when preparing a franchise agreement.

3. Prepare a disclosure document

The CPA requires the franchisor to provide certain minimum prescribed information to the franchisee in a disclosure document delivered to the franchisee prior to the signature of the franchise agreement (including a list of current franchisees, if any, and of outlets owned by the franchisor; the direct contact details of the existing franchisees; an organogram depicting the support system in place for franchisees; and an auditors certificate confirming that that the franchisor's audited annual financial statements are in order). This information is intended to provide the franchisee with enough information about the franchise, its financial viability and potential business success so as to enable the franchisee to make an informed decision as to whether or not he/she wishes to "acquire" the particular franchise.

4. Prepare a non-disclosure agreement

It is important to ensure the protection of confidential information which may be disclosed to the prospective franchisee during the preliminary stages of negotiating and concluding a franchise agreement. This may include, for example, the growth of the franchisor's turnover, and written projections in respect of levels of potential sales, income and profit. Although not a requirement under the CPA, it is advisable for a franchisor to ensure that a prospective franchisee executes an appropriate confidentiality agreement prior to being sent the disclosure document.

5. Beware the "cooling-off" period

It is important to bear in mind that a franchisee has an entitlement under the CPA to cancel a franchise agreement without cost or penalty within 10 business days after signing such agreement, by giving written notice to the franchisor.