

ANOTHER FRANCHISOR *FRESHLY SQUEEZED* BY MATERIAL DEFICIENCIES IN ITS DISCLOSURE DOCUMENT

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The Ontario Superior Court's recent decision in *2611707 Ontario Inc., et al v. Freshly Squeezed Franchise Juice Corporation, et al.*, [2021 ONSC 2323](#) ("*Freshly Squeezed*") is another example of the Court applying the test promulgated in *Raibex Canada Ltd. v. ASWR Franchising Corp.*, 2018 ONCA 62 ("*Raibex*")^[1] to determine whether one or more deficiencies in the franchisor's disclosure document entitles a franchisee to the two-year rescission remedy under Section 6(2) of the *Arthur Wishart Act (Franchise Disclosure)*, 2000, SO 2000, c.3 (the "AWA").

The Court in *Freshly Squeezed* relied heavily on the Court of Appeal's decision in *Raibex* in finding that failing to provide complete financial statements and failing to include an Agreement to Lease were material disclosure deficiencies. The Court also found that failing to highlight that the franchised business would be the first to be operated in a non-mall retail environment amounted to failing to disclose a "material fact" (as defined in the AWA).

The Court held that these deficiencies effectively deprived the franchisee of the opportunity of making an informed investment decision and were tantamount to non-delivery of an effective disclosure document, thereby entitling the franchisee to relief under s. 6(2) of the AWA. The Court noted that key to its determination was the fact that the franchisor withheld information that was within its power to disclose.

The Court in *Freshly Squeezed* also confirmed that the test for determining whether the deficiencies in question reach the threshold for a s. 6(2) rescission claim is based on an objective standard, taking into account the facts of each case, including the terms of the franchise agreement. It is not necessary for the franchisee to lead evidence that the material deficiencies caused an *actual* impairment of their ability to make an informed investment decision.

The Rescission Claim

The franchisee entered into a franchise agreement with Freshly Squeezed Franchise Juice Corporation and began operating a unit located in the RioCan Food Hall of Mount Sinai Hospital in March 2018. Less than a year after opening, the franchisee delivered a notice of rescission under s. 6(2) of the AWA. The franchisee argued

four “fatal flaws” or “material deficiencies” to validate its rescission under s. 6(2):

- the franchisor’s certificate required under s. 5 of the AWA only had one director/officer signature (instead of two);
- the financial statement disclosure was incomplete;
- the disclosure document failed to disclose that the franchisor had not yet entered into a head lease; and
- the disclosure was made in a piecemeal fashion.

The franchisee also argued that there were two further deficiencies in respect of the disclosure document that related to undisclosed material facts:

- failure to disclose a partly-executed Agreement to Lease between the landlord and franchisor; and
- failure to disclose that the franchised business would be the first non-mall location within the franchise system.

Location-Specific Disclosure

The franchisee alleged that the franchisor’s failure to disclose that a head lease for the unit did not yet exist, together with the failure to provide contractual protections for the franchisee (should the terms of the head lease be unacceptable) were material deficiencies. The franchisee also alleged that an Agreement to Lease negotiated and signed by the franchisor before the delivery of the Disclosure Document should have been disclosed.

The Court noted that failure to disclose the lack of the head lease was mitigated by the fact that the franchisee was otherwise made aware that there was no head lease. The Court restated that the failure to disclose the partly executed Agreement to Lease in the disclosure document (or at least the material terms of the agreement), in the absence of providing “contractual comfort” to the franchisee (as was the case in *Raibex*) such as giving the franchisee the right to reject a proposed location or elect to receive its money back if the terms of the head lease were unacceptable, was a material deficiency.

The Court also concluded that the fact that this franchised business was the first in a non-mall environment was a material fact that required explicit reference in the disclosure document.

Incomplete Financial Statement Disclosure

The Court in *Freshly Squeezed* confirmed that including prescribed financial statements in a disclosure document is fundamentally important to ensure all franchisees know the complete financial picture of a franchise system.

The franchisee alleged that the financial statements contained in the disclosure document were materially

deficient because they did not include the auditor's notes referenced beside certain line items. The Court accepted the franchisee's allegations and confirmed that franchisors must fully disclose relevant financial information to prospective franchisees so that they can make an informed investment decision. Because the auditor's notes were referenced in the financial statements but were not disclosed, the Court found that the franchisor failed to provide a complete version of the financial statements.

Franchisor's Certificate and Piecemeal Disclosure

The Court held that if a disclosure document is comprehensive and addresses all of the required elements, then the fact that the franchisee received other documents relative to the franchise outside the disclosure document is not inconsistent with the disclosure requirements and does not constitute piecemeal disclosure. As the parties were only relying on the disclosure document as the sole source of disclosure, there was no piecemeal disclosure.

The Court also concluded that the evidence supported that there was only one director and officer of the franchisor at the time of disclosure (and therefore one signature was appropriate), notwithstanding that a corporate profile report at the relevant time indicated otherwise. The franchisor certificate was therefore found to have been signed in compliance with the requirements of the AWA.

Key Takeaways

The *Freshly Squeezed* decision confirms that the failure to disclose complete financial statements and location-specific information are sufficient to ground a rescission claim under s. 6(2).

The Court also confirmed that the *Raibex* test for a rescission claim under s. 6(2) is an objective one that takes into consideration the particular facts of the case. It also suggests that a material fact may relate to something that does not yet exist, such as a head lease; however, failing to disclose such information may be mitigated if there are adequate contractual protections offered to the franchisee in the franchise agreement (such as the ability to reject a proposed location or elect to receive its money back).

[1][ps2id id='1' target='/'] *Raibex Canada Ltd. v. ASWR Franchising Corp.*, 2018 ONCA 62.

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A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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