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What Happens When a Franchise Agreement Ends - Part Three: Rescission



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In our previous posts (See [Part 1](#) and [Part 2](#)), we reviewed restrictive covenants and cancellation rights under franchise laws. In a recent decision of the Ontario Court of Appeal, the dispute focused on the right of rescission. As the court put it, the case of *Caffé Demetre Franchising Corp. v. 2249027 Ontario Inc.*, [2015 ONCA 258](#) "is another case from the franchise world involving whether the franchisor met its disclosure obligations...."

Specifically, the franchisee complained that the franchisor's disclosure document was deficient - so deficient, in fact, that it entitled the franchisee to rescind the franchise agreement. In the disclosure document, the franchisor failed to disclose ongoing litigation commenced by the franchisor against a competitor. Was this failure a material deficiency giving rise to a right of rescission?

A disclosure document must disclose "all material facts." A material fact is described in the legislation as any information about the business or operations of the franchisor, or about the franchise system "that would reasonably be expected to have a significant effect on the value or price of the franchise to be granted or the decision to acquire the franchise."

The Court in *Caffé Demetre Franchising Corp.* decided that the failure to disclose the franchisor's litigation was a deficiency but not "sufficiently significant" that the franchisee was entitled to a right of rescission. To qualify as a deficiency that gives rise to a right of rescission, the disclosure document must suffer from "stark and material deficiencies," such that a Court can conclude that it amounts to no disclosure at all. It is worth noting that the court was clear that litigation must be disclosed if it falls within the description contained in s. 2(5) of the Ontario regulations (the equivalent in Alberta is the *Franchises Regulation*, Alta Reg 240/1995), which mandates disclosure of any past or pending lawsuit or court order which involves allegations of "misrepresentation, unfair or deceptive business practices," including a failure to provide proper franchise disclosure. If the litigation in question involved any of these issues, then the decision would have been different.

What are the lessons? Franchisees should be very careful and conduct their own thorough investigations and due diligence before formalizing a franchise agreement, as even material deficiencies in the disclosure may not empower the franchisee to rescind the agreement. Of course, both parties should always seek appropriate legal advice when entering into and concluding franchising relationships in Alberta.

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