

Bad Optics: Ontario Court Denies Injunction to Franchisor Seeking to End Royalty Strike

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In *10313033 Canada Inc. v 2418973 Ontario Inc. et al. (Laurier Optical)*, the Ontario Superior Court of Justice confirmed that, while a franchisor seeking to end a royalty strike within its franchise system may be able to obtain an injunction compelling the striking franchisees to pay royalties while litigation is pending, such a request will be denied if the franchisor does not lead evidence that the withholding of royalties will have an irreparable financial impact on the franchise system.¹

Background to the Case: The Royalty Strike by Franchisees

The case arose from a dispute between a majority group of “Laurier Optical” franchisees and their franchisor, 10313033 Canada Inc. (103 Canada). 103 Canada had purchased the assets of the previous franchisor through a court supervised restructuring process under the *Companies’ Creditors Arrangements Act* (CCAA). Following this acquisition, a majority group of franchisees raised concerns with 103 Canada, alleging that the new franchisor had failed to respect its obligations under the franchise agreements and raised questions over the continued enforceability of the franchise agreements and leases assigned to 103 Canada pursuant to the CCAA vesting order. 103 Canada attempted to assuage these concerns through a proposed marketing campaign but was unsuccessful.

The franchisees sought to commence an arbitration over the dispute and began to withhold royalties and other fees owed under their franchise agreements in protest. The franchisees commenced an application seeking the appointment of an arbitrator and 103 Canada simultaneously commenced an action seeking, among other things, an interlocutory injunction compelling the franchisees’ compliance with the terms of their agreements including with respect to the payment of royalties and fees.

The Court’s Decision: No Evidence of Financial Harm, No Injunction

Canadian courts have previously granted injunctions compelling franchisees to comply with the terms of their franchise agreements in the face of “royalty strikes” that threaten to put the franchisor out of business. In 2010, the Court granted such an injunction in *Bark & Fitz Inc. v 2139138 Ontario Inc.*, even though the franchisor in that case had not met all of its obligations to its franchisees.² In *Cash Converters Canada Inc. v 1167430 Ontario Inc.*, an earlier decision not cited in *Laurier Optical*, the Court granted a similar injunction finding that a royalty strike by franchisees was directed at pushing the franchisor into bankruptcy and taking over the system.³

In applying the well established *RJR-Macdonald* test, the Court was satisfied that 103 Canada, like the franchisor in *Bark & Fitz*, had met the first stage of establishing a “serious issue to be tried”. However, unlike the franchisor in *Bark & Fitz*, the Court found that 103 Canada failed to lead sufficient financial evidence demonstrating that the ongoing royalty strike would result in “irreparable harm” sufficient to justify and injunction. While the Court noted that “as a matter of simple logic” the continued royalty strike by a majority of Laurier Optical franchisees could have “a severe, and possibly fatal, impact on the franchisor,” the Court was unable to reach such a conclusion based on the bald statements advanced by the franchisor’s principal that 103 Canada would be unable to meet its financial obligations if royalties continued to go unpaid. Having failed to establish irreparable harm, the Court held that the franchisor’s injunction request should be denied. The Court did note, however, that it would be open for the franchisor to apply again with better evidence of irreparable harm.

With respect to the franchisee’s application to appoint an arbitrator, the court agreed that the dispute should be submitted to arbitration and stayed the franchisor’s court action in favour of arbitration.

Key Takeaways

This decision confirms that franchisors can successfully obtain an injunction compelling franchisees to comply with the terms of their franchise agreements in the face of collective action by franchisees to withhold of royalties. Meeting the injunction test in such circumstances, however, will require detailed supporting documents showing the irreparable financial harm that would result if the royalty strike continues. Absent such evidence, the court will not intervene at an early stage with injunctive relief.

¹ 2018 ONSC 2406, <<http://canlii.ca/t/hrfgz>>.

² 2010 ONSC 1793, <<http://canlii.ca/t/2976g>> [*“Bark & Fitz”*].

³ 2001 CarswellOnt 6096 [*“Cash Converters”*].