

Is Franchising the Answer for Cannabis Retail in Ontario?

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Doug Ford's radical restructuring of Ontario's recreational cannabis retail regime was welcomed by anyone doubting the prior plan's ability to spur and maintain a vibrant and competitive industry capable of satisfying demand and stamping out the black market. A slow out of the gate provincial pot monopoly would have been an anachronism destined to miss the mark, leaving consumers underserved and disinterested, and shutting out a more capable and dynamic force for growth in the private sector.

While the reversal by Ontario has set the province on a new course, the details of the plan, which will prove to make or break Ford's vision, are sparse and a work in progress. At this point, what's in store for Ontario's pot shops remains hazy.

But, to be successful, the province's pot plan will, at the very least, need to allow for rapid and geographically dispersed brick-and-mortar development, while maintaining essential controls to ensure that rules are followed and vulnerable communities, including youth, are protected.

Those who doubt that a web of independently owned businesses can be successfully managed and responsibly governed, despite being subject to regulatory oversight and centralized controls, should look to the franchising model as a working example. By definition, franchising is a business method used for the distribution of products or services, across a network of independently-owned outlets, linked by essential operating controls, and unified by common brands or trademarks. The brand owner, or franchisor, is responsible to develop and sustain a business system, including demand for its product, which it licenses to its franchisees, who are in turn tasked to establish and operate a branded, local outpost which sells the product in accordance with the system. Franchising is built on – and flourishes as a result of – the very concept of centralized controls governing independent operations.

Franchising has been used for decades to distribute hamburgers, pizza and coffee. More recently, its widespread success and legitimization as a business format has pushed it, in many cases without public recognition, into other less obvious industries, such as hotels, vehicle dealerships and fuelling stations, and even into the gaps in our public services, such as health and child care and education. Using franchising rather than a more ownership-concentrated approach can allow retail business to expand more quickly, with greater diffusion of risk and capital, and with more localized benefits in the form of business ownership, employment and community engagement.

Look no further than McDonald's, Wendy's, Popeye's and Coca-Cola as examples of groups that divested and de-risked as they proceeded with aggressive "refranchising" projects aimed at reducing operating and

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capital costs and widening margins by selling corporate units off as franchised operations.

Retail growth through franchise development brings particular benefits to franchisors, many of whom are not necessarily adept at retail operation, but have developed demand for their products and seek to capture market share by creating branded distribution networks for those products. In recent years, these royalty-generating networks have created immense value and wealth for the private and public owners, with companies such as MTY Food Group building robust and highly profitable branded networks, in part, by acquiring smaller or accretive brands along the way.

These dynamics should make franchising particularly attractive to Canada's burgeoning cannabis industry, which has mostly spent the last few years developing production capacity and now looks to get its wares quickly into a nascent and competitive marketplace.

Franchising is also the catalyst for economic and entrepreneurial dynamism in a class of Canadians who otherwise might not have had the resources or support to go it alone. The systemization and infrastructure offered by franchising allows franchise operators to get into the game, skip the growing pains, and reduce the risk of failure. In the cannabis space, franchising will allow more Ontarians to own a stake in its sale and distribution, granting access to this emerging and lucrative opportunity that would have otherwise been reserved for government or conglomerates. Wanting to maximize that opportunity and protect their investments, franchise operators should be more inclined to operate good businesses and respect the rules.

Regulation is nothing new for franchising in Canada. Today, six provinces, including Ontario, have rigorous franchise laws, which require franchisors to provide substantial pre-contractual disclosure to prospective franchisees and to treat franchisees fairly after the contract is signed. As a result of these laws, franchisors have become increasingly sophisticated and transparent, while power and information has been reallocated to franchisees. With this rigorous regulatory environment in place, franchising as a business method has flourished in Canada, generating established and legitimized commercial and legal approaches that are ready to be adopted by the cannabis industry.

Let's remember that while the road ahead is unclear, not everything about the province's pot plan needs to be built from scratch. Franchising offers immediate and conducive platforms that should be part of any plan Ontario chooses to roll out.

We Can Help

For more information on how Cassels Brock can assist with your franchise and cannabis needs, please contact **Frank Robinson** or another member of our firm's **Cannabis Group** or **Franchising Practice**.

Frank Robinson will be part of an expert panel discussing the intersection of cannabis legalization and franchising at the CFA's Franchise Law Day in Toronto.

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This publication is a general summary of the law. It does not replace legal advice tailored to your specific circumstances.