



# RAISING THE BAR

IFA LEGAL SYMPOSIUM  
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# Basics Track: Registration and Disclosure

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# Agenda

- Definition of a Franchise
- History and Purpose of Franchise Laws
- Franchise Disclosure Requirements
  - Federal and State Requirements
  - Drafting Tips
  - Timing and Delivery
- Registration Requirements
  - Registration States and Filing Requirements
  - Renewals
  - Amendments
- Exemptions from Registration and Disclosure

# Definition of a Franchise

*Trademark License*

*Promise of Substantial Assistance or Right to Control*

*Fee in Excess of \$570 during the first six months of operation*

## 3 Elements of a Franchise Relationship:

1. Trademark License
2. Seller Provides Significant Assistance in or Seller has Right to Control Franchisee's Method of Operation
3. Fee (>\$570 During First Six Months of Operation)

# History and Purpose of FTC's Franchise Rule

- Advent of Franchise Regulations in the 1970s
- FTC Adopts Franchise Rule in 1979
- FTC's Disclosure Mandate
  - Provide Franchisees with Sufficient Information to Make Informed Purchasing Decisions
  - “Informed investors can determine for themselves whether a particular deal is in their best interest.”
- FTC Adopts Amended Franchise Rule in 2007

# FTC Franchise Rule Scope

- Regulates Franchising at Federal Level
- Regulates Franchising in:
  - All 50 states
  - District of Columbia
  - All U.S. territories
- Anti-Waiver: If it walks and talks like a “franchise” – it’s a franchise
- No Private Right of Action

# State Regulation of Franchise Sales

- Disclosure Required (State-Specific Disclosures Often Required)
- Pre-Sale Registration of Franchise Offering
  - Enables State Regulators to Review Disclosures for Compliance
- Private Right of Action
- Regulatory Authorities Empowered to Conduct Investigations
- NASAA Guidelines on Disclosure and Registration

# The FDD

- 23 Item Disclosure describing material terms of the Franchise Relationship
  - Material Contracts
    - Franchise Agreement
    - Development Agreement
    - Technology Agreement(s)
    - Guaranty
    - Service Agreements
  - Financial Statements
  - Lists of Current and Former Franchisees
  - Other Key Information



# Timing for Delivery

- Must have a full 14 calendar days to review the FDD before signing or paying consideration
- Do not count the date of FDD Receipt or the date of signature
- Start counting on the day after the date listed on the FDD Receipt
- Be cognizant of state first personal meeting and 10 business day rules
- 7 calendar day rule for agreement delivery (use same counting method)

**May** **2018**

**FDD DELIVERY CALENDAR**

Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
		1	2 DELIVERY DATE	3	4	5
6	7	8	9	10	11	12
13	14	15	16	17	18	19
20	21	22	23	24	25	26
27	28	29	30	31		

Red arrows indicate a 14-day period starting from the delivery date (May 2nd) and ending on May 16th. A green arrow indicates the sign date on May 17th.

# Disclosure

- Prospective Franchisee: “Any person (including any agent, representative, or employee) who approaches or is approached by a franchise seller to discuss the possible establishment of a franchise relationship.”
- Disclose FDD upon “reasonable request” from prospective franchisees
- One Document Rule

# State Disclosure

- Different Timing Required in Specific States:
  - NY: Earlier of 10 business days or “first personal meeting”
  - IA: Earlier of 14 calendar days or “first personal meeting”
  - MI: 10 business days
  - First Personal Meeting: A face-to-face meeting between a franchisor/franchise broker and prospective franchisee to discuss sale or possible sale of a franchise.

# E- Disclosure

- Delivery Format and E-Disclosure
  - Electronic disclosure includes disclosure by email, over the internet (through a franchisor's website or the website of a third-party vendor), and by CD-ROM
  - Non-editable format recommended
  - Advise of FDD formats before delivery (even if paper is the only option)

# Disclosure Rules of the Road

- ✓ Complete FDD in PDF Format or Hard Copy
- ✓ Complete FDD with Print Toggle on Receipts
- ✗ Complete FDD with Print Toggle on FDD Cover Page
- ✗ CD-ROM Containing FDD with Hard Copy Printed Receipts
- ✗ CD-ROM or Email Containing FDD Booklet and Separate .PDF Receipts
- ✗ Audio, Video, or other Multi-Media

# Federal FDD Requirements

- Drafting Tips and Tools
- Federal Cover Page
- Items 1-11
- Items 12-23

# Drafting Tips and Tools

- Plain English
- Addressing Specific Items
- Negative Responses
- Cross-References
- FTC Resources
- NASAA Resources

# Federal Cover Page

- FTC Required Statements
- Total Investment Information
- Availability of FDD in Other Formats
- Issuance Date



# FDD Items 1-4

- Item 1 – Franchisor/Parents/Predecessors/Affiliates
- Item 2 – Business Experience
- Item 3 – Litigation
- Item 4 – Bankruptcy

# FDD Items 5-8

- Item 5 – Initial Fee
- Item 6 – Other Fees
- Item 7 – Estimated Initial Investment
- Item 8 – Restrictions on Sources of Products and Services

# FDD Items 9-11

- Item 9 – Franchisee’s Obligations
- Item 10 – Financing
- Item 11 – Franchisor’s Assistance, Advertising, Computer Systems, and Training

# FDD Items 12-14

- Item 12 – Territory
- Item 13 – Trademarks
- Item 14 – Patents, Copyrights, and Proprietary Information

# FDD Items 15 & 16

- Item 15 – Obligation to Participate in the Actual Operation of the Franchised Business
- Item 16 – Restrictions on What the Franchisee May Sell

# FDD Items 17 & 18

- Item 17 – Renewal, Termination, Transfer, and Dispute Resolution
- Item 18 – Public Figures

# FDD Item 19 – Financial Performance Representations

- Review FTC Requirements and NASAA FPR Commentary
- Reasonable Basis
  - Representative Group
  - Time Period
  - # and % of Outlets Achieving the Stated Performance
  - Median/Average (also High/Low for Gross Sales)
  - Other Material Information
- Substantiation

# Item 20

- Item 20 – Outlets and Franchisee Information
  - Table 1 - Systemwide Outlet Summary
  - Table 2 - Transfers
  - Table 3 - Franchisee-Owned Outlets
  - Table 4 - Company-Owned Outlets
  - Table 5 - Projected Openings
  - Contact information for current and former franchisees



# Items 21-23

- Item 21 – Financial Statements
  - Phase-in of Audited Financials for New Franchisors
- Item 22 – Contracts
- Item 23 – Receipts

# State-Specific Disclosure Requirements

- Jurisdiction of State Franchise Laws –  
No Federal Pre-emption
- Examples of State-Specific Disclosures
- State Cover Page/Risk Factors/NASAA Proposal
- State Addenda
- State Timing Issues

# State Franchise Registrations

- 14 states – Jurisdiction
- NASAA
- Filing Requirements
- Review Process/Comment Letters
- Strategies for Registration Process

# FDD Renewal / Amendment Process

## Federal Requirements

- Renewal
  - 120 days after fiscal year end
- Amendment
  - Quarterly to reflect any “material change”
  - FPRs: immediately notify prospect of change

## State Requirements

- Renewal
  - 90 to 120 days after fiscal year end
  - Prior to anniversary date
- Amendment
  - Promptly
  - Occurrence of material change
  - 30 days

# Navigating Franchise Exemptions

- Fractional Franchise
- Minimal Franchise Fee
- Large Franchisee
- Large Investment
- Others

# Additional Filing Requirements

- Advertising
- Franchise Sellers / Brokers

# Questions?

