ADVANCED DISCLOSURE ISSUES:
PUSHING THE ENVELOPE

Jamila Granger
Krispy Kreme
Winston-Salem, North Carolina

Benjamin A. Levin
Hyland Levin LLP
Marlton, New Jersey

Charles S. Modell
Larkin Hoffman Daly Lindgren Ltd.
Minneapolis, Minnesota

October 13 - 15, 2010
The Hotel Del Coronado
San Diego, California

©2010 American Bar Association
TABLE OF CONTENTS

I. INTRODUCTION .......................................................................................................................... 1

II. THE AMENDED FRANCHISE RULE AND DISCLOSURE REQUIREMENTS .......... 2
    A. Payment to or Binding Agreement with the Franchisor or Affiliate .................3
    B. What is a Binding Agreement that Triggers FDD Disclosure? .........................3
    C. How Did the Commission Protect the Prospective Franchisee Under the
        Amended Franchise Rule? .......................................................................................4
    D. Drafting a Non-Binding Letter of Intent (LOI) or Term Sheet .........................5

III. CHANGING THE ANALYSIS: THE REGISTRATION STATES ......................... 6

IV. IS AN EXEMPTION AVAILABLE? ................................................................................ 7
    A. Amended Franchise Rule: Large Franchise Investment Exemption ...............7
    B. Amended Franchise Rule: Large Franchisee Exemption .................................8
    C. State Law Exemptions .............................................................................................9

V. REMEDYING PRE-SALE DISCLOSURE VIOLATIONS ........................................ 10
    A. Violations That Are Easy to Remedy ..............................................................11
    B. Violations That Are More Difficult to Remedy ..............................................11
    C. Violations That May Be Impossible to Remedy ..............................................11

VI. POST-SALE DISCLOSURE ISSUES ............................................................................. 12
    A. Transfers .............................................................................................................12
        1. When does a transfer of a franchise trigger FDD disclosure? ......................12
        2. How does the analysis differ when the franchise is in a Registration State?........13
    B. Renewals .............................................................................................................15
        1. When does renewal of a franchise agreement trigger FDD disclosure? ..........15
        2. When disclosure is not possible, are there any other options? .................16
3. How does the analysis differ when the franchise is in a Registration State?

4. What best practices should franchisors implement?

VII. UNIQUE DISCLOSURE ISSUES

A. Disclosing Multiple Concepts In One Franchise Disclosure Document

1. When Is It Permissible To Use a Single FDD?

2. When Is It Practical To Have Multiple FDDs?

B. Financial Performance Representations – How Can A Franchisor Properly Provide Information That Is Not In The FDD?

1. Financial Representations that Fall within Specific Exceptions to the Amended Franchise Rule

2. Financial Representations That Are Not Financial Performance Representations

3. Exempt Transactions

4. A Word of Caution

C. Phase-In Of Audited Financial Statements

VIII. CONCLUSION

Appendix A - Form Letter of Intent
Appendix B - Registration States Transfer and Renewal Exclusions and Exemptions
ADVANCED DISCLOSURE ISSUES: PUSHING THE ENVELOPE

INTRODUCTION

We all aspire to be careful and thoughtful franchise lawyers. We keep up with the latest developments, let our clients know what they can and cannot do, and generally err on the side of being (somewhat) conservative. The authors of this paper, however, have been charged with throwing away all conservative notions and addressing how the franchise regulatory envelope can be pushed. The following discussion describes just a few areas of franchise disclosure compliance that may be susceptible to more enterprising legal advice.

Imagine you are sitting at your desk on a Friday afternoon at 6:00 PM. You are looking forward to the weekend. The phone rings. Against your better judgment, you answer the call. One of your clients is in a meeting with some other business people. They want to make a deal that day. The transaction involves a franchise. The facts may vary.

- The client is a successful restaurant operator who has been approached by some affluent customers wanting to be the first franchisee. They know there are no franchise documents created, but they want to tie-up rights to develop franchises in a certain territory.

- The client engaged you two weeks ago to create a Franchise Disclosure Document ("FDD") in compliance with the amended Franchise Rule, 16 C.F.R. Part 436 (the "Amended Franchise Rule"). You have not yet completed the document. The client has a prospect who wants to give him/her $25,000 as an initial fee to open the first unit. The client tells you he will use the money to pay for your work in drafting the FDD.

- The client has an FDD, but has not registered the offering in a particular state, which regulates the franchise sales process (the “Registration States”). A prospect wants to buy a multi-unit development deal in that Registration State.

- You have filed an FDD in a particular Registration State, but are awaiting comments. The client does not want to wait any longer; he/she needs a deal done today.

- The client’s FDD is stale, outdated, needs to be revised, needs to be renewed.

---

1 You can view the Amended Franchise Rule online at http://ecfr.gpoaccess.gov/cgi/t/text/text-idx?c=ecfr&tpl=/ecfrbrowse/Title16/16cfr436_main_02.tpl.

2 California, Illinois, Indiana, Maryland, Minnesota, New York, North Dakota, Rhode Island, South Dakota, Virginia and Washington require franchise offerings to be registered with state administrators before the “offer” or “sale” of a franchise. Hawaii, Michigan and Wisconsin and have varying state specific filing requirements before an offer or sale of a franchise may be made in the state. Hawaii has a filing and (informal) administrative review process before an offer or sale may take place. Oregon makes it a deceptive practice to fail to disclose properly.
What do you do? It depends. First, you have to ask yourself three initial questions:

(1) Is the proposed transaction subject to the Amended Franchise Rule or a Registration State?
(2) If a Registration State is involved, has that state’s franchise law been recently amended to follow the Amended Franchise Rule regarding disclosure?
(3) Is an exemption available, and if so, how does that exemption impact your advice?

THE AMENDED FRANCHISE RULE AND DISCLOSURE REQUIREMENTS

The Amended Franchise Rule did away with the “first personal meeting” requirement and now provides for more precise guidance on when an FDD must be given to a prospective franchisee.

The Amended Franchise Rule provides that franchisors must furnish prospective franchisees with an FDD at least 14 calendar days before the prospective franchisee signs a binding agreement with, or makes any payment to, the franchisor or an affiliate in connection with the proposed franchise sale. The 14 day period begins the day after delivery of the FDD. The signing of a binding agreement or receipt of payment by the franchisor or an affiliate can take place on the fifteenth day after delivery. This ensures that prospective franchisees have at least a full 14 days in which to review the disclosures (the so-called “cooling off period”).

Absent an exemption (which is discussed later in this paper), it is an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act 15 U.S.C. Section 45, for any franchisor to fail to furnish a prospective franchisee with a copy of the franchisor's current FDD as described above. Part 436 of the Amended Franchise Rule substantially revised the original Rule’s timing for making franchise disclosures. Under the original Franchise Rule (the “Original Franchise Rule”), franchisors had to furnish prospective franchisees with a disclosure document at the earlier of two time periods: (1) the first personal (face-to-face) meeting; or (2) “the time for making disclosures,” which was defined as 10 business days before the execution of the franchise agreement or payment of any fees in connection with the franchise sale. The Amended Franchise Rule changed the timing provision in two respects: elimination of the “first personal meeting” disclosure trigger and replacement of the 10-business day trigger with a 14 calendar-day disclosure trigger.

In making these changes, the Federal Trade Commission (the “Commission”) stated that a first personal meeting trigger alone did little to ensure that a prospective franchisee will receive disclosures early in the sales process and while at the time the Original Franchise Rule was promulgated it may have been routine, or perhaps necessary, to have a face-to-face meeting early on, that is no longer true. Today, a franchisor and a prospect may have numerous telephone conversations or send documents to each other via fax or e-mail long before any personal meeting occurs. The Commission observed that the first personal meeting trigger had become largely obsolete and should be deleted.³

a. **Payment to or Binding Agreement with the Franchisor or Affiliate**

Initially, the proposed Amended Franchise Rule triggered disclosure based on a franchisor’s knowledge of a prospective franchisee’s signing of a binding agreement or payment of consideration to anyone (not just the franchisor or an affiliate). Following input from several commentators, the Commission revised the final version of the Amended Franchise Rule to delete the knowledge requirement and changed the final provision to specify that disclosure must be made at least 14 calendar days before the “prospective franchisee” signs a binding agreement with or makes any payment to, the franchisor or an affiliate in connection with the proposed franchise sale.

This language makes clear that payments to, or agreements with, third parties do not trigger the franchisor’s disclosure obligation because a franchisor cannot control, or does not necessarily know, when a prospective franchisee may proceed to pay or make a commitment to third parties. Payments or agreements that a prospective franchisee voluntarily makes on his or her own in connection with a possible purchase of a franchise do not trigger disclosure.4

b. **What is a Binding Agreement that Triggers FDD Disclosure?**

During the Amended Franchise Rule rulemaking process, a well known franchise firm urged the Commission to clarify in the Compliance Guides that the 14-day disclosure period requirement is not violated by a confidentiality agreement signed by the franchisor and the prospective franchisee. The firm maintained that prospective franchisees often sign confidentiality agreements in the course of negotiations with franchisors. The firm stated that while the signing of a confidentiality agreement is in connection with the proposed franchise sale, it does not bind the prospective franchisee to purchase the franchise or to undertake other obligations, such as the signing of a lease. The firm urged clarification that the term “binding agreement” in the 14-day rule is limited to franchise agreements or other agreements that commit the prospective franchisee to purchase a franchise. The Commission agreed stating that “[a] confidentiality agreement—often signed by prospective franchisees before being granted access to the franchisor’s operations manual and other proprietary information—may be a necessary initial step in the sales process, but is not the type of agreement that triggers disclosure obligations. This assumes, however, that the confidentiality agreement contains no other agreements that, in the absence of the confidentiality agreement, would trigger disclosure, such as a lease agreement.”5

If confidentiality agreements do not trigger FDD disclosure, then what other kinds of agreements or other documents can be signed by the franchisor and prospective franchisee in the absence of FDD disclosure? Let’s push the envelope. The execution of a non-binding letter of intent or the creation of a “term sheet” in which neither the franchisor nor the prospective franchisee is committed to the sale or purchase of a franchise should not trigger FDD disclosure under the Amended Franchise Rule.

---


5 FTC Statement, 72 Fed. Reg. at 15470 n. 266.
There is some case support for this position. In Ross v Culver Franchising System, Inc., plaintiffs had signed a “preliminary agreement” with the franchisor and paid a $5,000 application fee, but understood there were many steps remaining in the franchise approval process. The necessary steps in the process were not completed and a franchise agreement was never signed. When the franchisor awarded a franchise to another and returned the plaintiffs’ application fee, the plaintiffs sued alleging violations of the Illinois Franchise Disclosure Act for unlawful termination, breach of contract (including breach of the preliminary agreement) and fraud. The Illinois Federal Court granted defendants’ motion for summary judgment on all counts. With respect to the breach of contract claims, the Court ruled that under Illinois law, if the later execution of a formal agreement is a condition precedent to the formation of a binding contract, no prior writing will create an effective contract.

c. How Did the Commission Protect the Prospective Franchisee Under the Amended Franchise Rule?

As reflected in the FTC Statement, the Commission shared some expressed concerns that a franchisor could unfairly influence a prospective franchisee’s decision before the prospect receives the franchisor’s disclosures. Since only binding agreements or payments to a franchisor or an affiliate trigger disclosure obligations, the prospective franchisee may incur costs and make various payments to third parties in connection with a possible purchase of a franchise without the benefit of pre-sale disclosures. Additionally, some argued that by encouraging a prospect to incur expenses before disclosure, the prospect might feel obligated to go through with the deal without a thorough due diligence investigation.

To address this concern, the Commission adopted the FTC Staff Report recommendation of a new provision to prohibit franchise sellers from refusing to honor a prospective franchisee’s reasonable request for a copy of the franchisor’s disclosure document during the sales process. Section 436.9(e) of the Amended Franchise Rule specifies that it is an unfair or deceptive practice to “[f]ail to furnish a copy of the franchisor’s disclosure document to a prospective franchisee earlier in the sales process than required under [16 C.F.R.] § 436.2 of this part, upon reasonable request.”

This new provision does not mean that a franchisor must tender a disclosure document to any person who may desire a copy. Rather, it applies where the parties have already conducted specific discussions or negotiations or otherwise taken steps to begin the sales process. The Commission observed that this provision enables a prospective franchisee to ask to see a copy of the FDD before agreeing to travel to company headquarters or spending other money during the pre-sale process. The Commission observed that this added protective feature would likely impose only a de minimis burden, if any, on franchisors, who presumably,

6  2004 WL 1898235 (N.D. Ill.)
7  72 Fed. Reg. at 15469.
8  16 C.F.R. 436.9(e).
have a disclosure document already prepared when discussing a sale with a prospective franchisee.\(^\text{10}\)

Referring back to the original questions posed above, does a new franchisor risk committing an unfair or deceptive practice to engage in sales discussions with a prospective franchise in the absence of having an FDD completed, or if completed, not having a current version of its FDD? Maybe.

The Division of Marketing Practices in the Bureau of Consumer Protection of the FTC prepared Amended Franchise Rule Frequently Asked Questions (“FAQs”) following promulgation of the Amended Franchise Rule.\(^\text{11}\) FAQ #14 gives some guidance to a franchisor if a prospective franchisee “reasonably requests” a copy of the FDD early in the sales process when the franchisor’s FDD is no longer current, and the franchisor is in the process of updating its FDD or state registration applications are pending. FAQ #14 states that franchisors may provide its then-current version of the FDD, but, in order to avoid possible misrepresentations, FTC Staff stated that “best practice” would be for franchisors to advise the prospective franchisee that the franchisor is preparing a revised FDD which will be available to the prospect when issued or registered with the applicable Registration State. FAQ #14 does not address the situation when the initial FDD has not yet been drafted. Would the result be the same? What would best practices be for a franchisor in that situation? A suggested course of action for the client may be the following: (1) do not sign a binding agreement that commits a prospective franchisee to buy a franchise; (2) do not take any money from the prospective franchisee; (3) give accurate information on the status of your FDD; (4) give the FDD when completed; and (5) following the appropriate “cooling off period”, proceed.

d. **Drafting a Non-Binding Letter of Intent (LOI) or Term Sheet**

Franchising and franchise relationships have changed dramatically over the last 25 years. Many franchisees are more sophisticated. Many proposed franchise transactions (multi-unit developing, master franchising) are more sophisticated transactions. There are a multitude of transactions that are subject to franchise disclosure laws and regulations that are completely outside of the cookie-cutter single franchise unit transaction. While there may be available exemptions applicable to many of these transactions, there will always be proposed transactions where an exemption is not available or the information currently available makes it too difficult to form an opinion on the availability of an exemption. In view of the changes to FDD disclosure discussed above, the LOI may be a very useful tool to assist clients in moving “deals” along without violating the Amended Franchise Rule.

Business people use LOIs and term sheets all the time. Sometimes a buyer and seller use it to test the waters before incurring the costs of negotiating a definitive (and binding) agreement. The legal principles for when a LOI is or is not binding are fairly easy to state:

If the parties intend not to be bound to each other prior to the execution of a definitive agreement, the courts will give effect to that intent and the parties will not be bound until the agreement has been executed. This is true even if all issues in the negotiations have been

\(^{10}\) 72 Fed Reg at 15469.

\(^{11}\) The FAQs are available online at [http://www.ftc.gov/bcp/franchise/amended-rate-faqss.shtml](http://www.ftc.gov/bcp/franchise/amended-rate-faqss.shtml).
resolved. On the other hand, if the parties intend to be bound prior to the execution of a definitive agreement, the courts will give effect to that intent and the parties will be bound even though they contemplate replacing their earlier understanding with the agreement at a later date. Courts have consistently stated that the most important factor in determining whether or which provisions in a LOI are binding is the language used by the parties in the document.

Typically, practitioners draft LOIs to be at least partially binding. The LOI is drafted in two parts: provisions not intended to be binding and provisions expressly intended to be binding on the parties. The non-binding provisions consist primarily of the “deal points”, such as a description of the proposed transaction, the purchase price, key ancillary agreements and important deal conditions. The binding provisions focus on the negotiation process, including access to information, confidentiality, a “no-shop” provision in which the seller agrees not to offer or sell the subject of the transaction to another for a specified period of time and non-disclosure (to third parties) obligations.

A form LOI containing binding and non-binding provisions for a franchise development opportunity is attached as Appendix A.

In a franchise transaction, the terms of the proposed transaction (“deal points”) would likely be in the non-binding section of the LOI. Possible binding obligations could include confidentiality provisions (see discussion above) and a “no-shop” lockup, or exclusivity provision, in which the franchisor agrees not to offer or sell the proposed transaction (e.g., a specified area or location or the first franchise units of a new concept) for some specified period of time.

Term sheets are also used by parties to formulate deal points without committing to the actual transaction. In the franchise context, however, because clarity is essential with respect to the non-binding provisions, the LOI is probably a better vehicle. Most transactional lawyers are more comfortable with an LOI, in which the parties can spell out the transaction with some specificity in the non-binding section, but still address certain binding conditions that do not relate to the actual sale of a franchise (e.g. confidentiality and no shop provisions).

2. CHANGING THE ANALYSIS: THE REGISTRATION STATES

The discussion above has been in the context of a proposed transaction in which the Amended Franchise Rule governs. The analysis changes in the Registration States. Most importantly, unlike the Amended Franchise Rule, the Registration States prohibit “offers” of a franchise absent state law compliance. While the Amended Franchise Rule triggering elements relate to binding agreements or payments to the franchisor or an affiliate, state franchise law analysis commences by examining the meaning of the term “offer” in a particular state, and what may or may not be permitted. State laws generally define the offer of a franchise to include “every attempt to offer or dispose of, or solicitation of an offer to buy, a franchise or

---

14 See R.G. Group, supra, 751 F.2d at 74.
interest in a franchise for value”.15 Because most of the states modeled their franchise laws after security laws, the vague and dangerous “offer” concept triggers franchise registration and disclosure obligations long before the now bright line timing obligations set forth in the Amended Franchise Rule.

There are also practical considerations. In most non-Registration States the liability risks associated with failing to deliver the FDD as required by the FTC are relatively low. There is no state agency that is overseeing franchise disclosure laws and disclosure activity and no private right of action is permitted for violations of the Amended Franchise Rule. The analysis changes dramatically if the proposed transaction involves one of the Registration States. Because most of the states modeled their franchise laws after security laws, the vague and dangerous “offer” concept triggers franchise registration and disclosure obligations long before the now bright line timing obligations set forth in the Amended Franchise Rule.

While envelope pushing may make sense in a non-Registration State, the liability risks associated with failing to comply with state disclosure law in Registration States are quite high. There are usually state agencies actively overseeing franchise activities in the state. Typically these agencies have broad enforcement powers and great discretion when it comes to interpreting compliance with the state’s franchise laws, including when disclosures are required. In addition, the Registration States allow private rights of action for franchise law violations and have statutory provisions to impose criminal and civil penalties.

3. IS AN EXEMPTION AVAILABLE?

a. Amended Franchise Rule: Large Franchise Investment Exemption

A detailed discussion of franchise law exemptions is beyond the scope of this paper. The Amended Franchise Rule has, however, given the franchise practitioner some further relief when responding to the questions posed above from the Friday 6 PM client phone call. You can

15 See, e.g., CAL. CORP. CODE §31018(b).

now ask two questions that may still allow you to go home early. Is a large franchise exemption available and does the prospective franchisee qualify for the large franchisee exemption? The Amended Franchise Rule exempts franchise offers and sales where the initial investment is at least $1 million, excluding the cost of unimproved land and any franchisor (or affiliate) financing.¹⁷

A franchisee’s “initial investment” is limited to the type of expenses that would ordinarily appear in an Item 7 disclosure – expenses paid through the opening of the outlet and any additional expenses paid through the three-month initial period thereafter. It does not reach all possible payments to the franchisor made over the life of the franchise agreement. Accordingly, future obligations to pay rent, royalties, or advertising fund contributions to be made over the life of the franchise agreement do not count toward the “initial investment.” The “initial investment” also does not reach costs associated with unimproved land, nor any funds obtained through franchisor (or affiliate) financing.

Conversion franchises and transfers of franchised outlets may qualify for the large investment exemption. In a conversion franchise, a business owner has already invested in his or her existing business and now seeks to associate with a particular franchisor’s mark by entering into a franchise agreement with that franchisor. When considering a conversion franchisee’s “initial investment” in a franchise, the conversion franchisee’s previous investment in the outlet (as opposed to the current value of the outlet) may be considered.

This is true even though the conversion franchisee’s initial investment was not paid to the franchisor making the current offer. In a transfer, a prospective franchisee buys an existing franchise directly from an existing franchisee, but then may enter into a new franchise agreement with the franchisor. The fact that a transferee will assume an existing contract or may renegotiate an existing contract with the franchisor ordinarily has no bearing on his or her level of sophistication as an investor. As long as he or she satisfies the monetary threshold, the large investment exemption is available. As in the case of the conversion franchisee, the prior investment to a party other than the franchisor – here, the transferring franchisee – does not preclude application of the large investment exemption.

Where an investor group seeks to purchase a franchise, at least one individual must invest at the $1 million level for the exemption to apply. The large investment exemption is premised on the assumption that a franchisee’s ability to pay a large sum equates with sophistication. That assumption fails when no one investor standing alone is investing at the requisite threshold level. For purposes of this provision, a husband and wife can be considered a single individual since their assets are typically commingled.

b. **Amended Franchise Rule: Large Franchisee Exemption**

The Amended Franchise Rule exempts franchise offers and sales to large entities – such as airports, hospitals, and universities – that have been in business for at least five years and have a net worth of at least $5 million.¹⁸

---

¹⁷ 16 C.F.R. §436.8(a)(5)(i).
¹⁸ 16 C.F.R. §436.8(a)(5)(ii).
To qualify for the exemption, the large entity must have five years of prior business experience. That experience, however, need not be in franchising, or even in the franchised business in particular. For example, a hospital seeking to purchase a donut franchise could qualify for the exemption, even though the hospital may not have any prior experience with franchising or with the donut or baking industry.

To qualify for the large franchisee exemption, the prospective franchisee-entity must have a net worth of $5 million. The net worth of an entity can readily be determined from the entity’s balance sheet or other financial information, typically submitted as part the application process.

When determining the prior experience and net worth of a franchisee-entity, franchisors may consider the prior experience and net worth of the prospective franchisee’s affiliates and parents. For example, a franchisor – such as a hotel – may wish to establish a separate corporation for a particular transaction. It is possible, however, that the new spin-off corporation will meet neither the net worth nor prior experience prerequisites. The Amended Franchise Rule makes clear that the prior experience and net worth of the parent may be considered in such circumstances. Accordingly, franchisors may aggregate commonly-owned franchisee assets in determining the availability of the large entity exemption.

c. **State Law Exemptions**

The Registration States have their own sets of exemptions from disclosure and/or registration requirements. In some cases, there is an exemption only from registration (while still requiring disclosure), some are self-executing (i.e., by definition the offering is exempt and there is no filing or registration requirement), and some require filing, paying a filing fee, and annual renewal.

Some Registration States have exemptions for “fractional franchises”, “sophisticated investors”, and “high net worth” franchisor exemptions. The most frequently relied on registration exemption is the “large franchisor” exemption. So-called “isolated sale” or “single license” are exempt from registration, but not disclosure, and are available in certain Registration States, the particular requirements of which should be carefully examined.

Franchisors must also be cognizant of the “business opportunity” and “seller-assisted marketing plan” laws that have been enacted in twenty-six states. Some of these laws have their own registration and disclosure requirements, as well as financial assurance requirements; however, some do not have a filing requirement. The definition of a “business opportunity” or “seller-assisted marketing plan” is often broad enough to cover franchises. In most cases, however, a franchisor will be exempt from the business opportunity laws if: (1) it complies with the Amended Franchise Rule; or (2) the marketing plan is in conjunction with a federal or state registered trademark. In many states, the exemption is automatic, and the franchisor need not

---

19 *See, e.g.*, CAL. CORP. CODE §31101

20 *See, e.g.*, N.Y. GEN. BUS. LAW §684(3)(c).
take any action if it qualifies for such an exemption. In others, franchisors must file an affidavit or notice in order to perfect their exemption.  

4. REMEDYING PRE-SALE DISCLOSURE VIOLATIONS

For purposes of this discussion, we have separated pre-sale violations into two categories, those that are discovered before the consummation of the sale of the franchise, and those that are discovered after the fact. Dealing with pre-sale violations that are not discovered until after the sale closes is beyond the scope of this paper. The Annual Forum has had at least three workshops that have focused exclusively on this subject, and the Franchise Law Journal has reported on this subject. Rather, this paper will focus on pre-sale violations that are discovered prior to the closing of the sale, and whether, and how, they can be “corrected.”

There are a variety of pre-sale violations that can be caught prior to closing. The most common are likely to be a FDD that is inaccurate or omits required information, misrepresentations made by sales personnel, and the provision of a financial performance representation (“FPR”) to the prospective franchisee that is not included in the FDD. Should such a violation occur, the safest and most conservative course of action would be to walk away from the sale. In those situations, most prospective franchisees would be hard pressed to prove they incurred any damages as a result of the violation. For one thing, unless the prospective franchisee could show that the franchisor had committed itself to granting the franchise, franchisors are always free to reject a prospect. Further, if the franchise is never granted, then it would be difficult for a prospective franchisee to show that it incurred significant damages in reliance upon the violation. On the other hand, there is case law allowing a prospective franchisee to recover damages incurred based on reliance on statements concerning the franchisor’s commitment to sell the franchise. Once a commitment has been made, if the franchisee can show the franchisor reneged on its commitment, particularly when the only reason was because of the franchisor’s own misconduct, a cause of action could lie in favor of the prospective franchisee.

---

21 See the FTC website at http://www.ftc.gov/bcp/franchise/netbusop.shtm for the addresses and websites of state agencies that regulate business opportunities.


a. **Violations That Are Easy to Remedy**

There are certain violations that should be capable of easy remedy. For example, in a situation where the franchisor delivered an FDD from the wrong state, there is no reason not to provide a substitute FDD. Likewise, when one discovers that an FDD omitted material required disclosures, an updated FDD should be delivered before completion of the sale.

b. **Violations That Are More Difficult to Remedy**

Other pre-sale violations are more difficult to “correct.” For example, once a franchisee has received a glowing FPR, then like the juror who is admonished by a judge to forget the “smoking gun” that was improperly introduced, it is difficult for a franchisee to ignore what he saw. In those circumstances, the franchisor should consider whether there is any way to remedy the violation.

Actually, the example of the improper FPR provides a good framework for the discussion. One might ask whether the FPR, admittedly improper, was accurate. If it was, then the best advice for the franchisor would be to amend the FDD to include the information in the FDD, with all appropriate disclosures, and provide a new FDD. It would seem to be difficult for a franchisee to argue that they suffered any damages if the franchisor provided accurate information, confirmed its mistake to the franchisee, then provided the same information in proper form, and waited 14 days before accepting any money or signed contracts from the prospect. In fact, while two state franchise laws that have been construed to impose strict liability on franchisors for violations, there are some states where even without including the information in the FDD, the courts have ruled that when there is “no harm,” there is “no foul.”

c. **Violations That May Be Impossible to Remedy**

Unfortunately, there may be situations where incomplete or inaccurate information was provided to the prospective franchisee that was so material to the decision that the violation cannot be remedied. In this situation, if the sale closes, there may not be a way to “correct” the error. In *Ciampi v. Red Carpet Corp. of America*, the franchisor failed to disclose significant information that was required to be included in the disclosure document under California law. When the franchisee later sued, the franchisor introduced evidence showing that the franchisee had been appraised of most of these facts before the contracts were signed. The appellate

---


26 *See, e.g.*, Benson v. Sbarro Licensing, Inc., [1983-1985 Transfer Binder] Bus. Franchise Guide (CCH) ¶7967 (D. Minn. 1983), wherein the franchisor not only provided a projection to the prospective franchisee outside of the disclosure document, but had not even completed its franchise registration with the State of Minnesota. In a subsequent action for rescission, the court noted that the franchisee’s results exceeded the projection, and therefore found that there was no harm to the franchisee and no right to rescind. *Id.* at 13,598-600.

court rejected the franchisor’s argument, finding that if those arguments were adopted “a franchisor could submit a misleading prospectus to a prospective franchisee who in reliance thereon might make substantial expenditures to qualify as a franchisee (e.g. closing existing businesses, buying or leasing space for the franchise outlet, borrowing funds, etc.). The franchisor could put off disclosing the more unpleasant truths about the investment until the prospective franchisee had strong economic incentives not to withdraw from the contract.”

The court found that while subsequent disclosures “might affect the amount of damages caused a prospective franchisee, such disclosures cannot be used to avoid liability for a violation of Section 31300.”

Thus, in these situations, the franchisor needs to take a careful look at all the facts and determine the extent to which a prospective franchisee may already have made a decision based on the previously provided information. If the investment has been significant, but there still has been no promise of a grant of a franchise, the only way for the franchisor to really eliminate the likelihood of liability is to walk away from the sale. If management of the franchisor determines this is not a viable option, then we would still recommend disclosing the information in an effort to establish an argument that any damages should be limited to the amounts already expended by the franchisee prior to the disclosure; subsequent costs could not have been reasonably incurred in reliance on the improperly disclosed information.

POST-SALE DISCLOSURE ISSUES

**Transfers**

(1) **When does a transfer of a franchise trigger FDD disclosure?**

Franchisors are often faced with requests from franchisees to transfer their franchises. If franchisor involvement is limited to approval of the transfer, franchisors may respond to these requests without triggering disclosure obligations. The Amended Franchise Rule provides that the sale of a franchise “does not include the transfer of a franchise by an existing franchisee where the franchisor has had no significant involvement with the prospective franchisee.”

The Commission provides additional guidance in the Compliance Guide where it explains that “a person who purchases an existing franchise directly from the franchisee who owns it, without any significant contact with the franchisor – is not a prospective franchisee.” In addition, the Commission notes in the FTC Statement that the Amended Franchise Rule makes clear that a transfer without significant involvement of the franchisor is not the sale of a franchise within the ambit of the Rule.”

---

28 Id. at 15,357-58.
29 Id. at 15,358.
30 16 C.F.R. § 436.1(t).
31 Compliance Guide at 18.
32 FTC Statement, 72 Fed. Reg. at 15466. Further, the FTC Statement makes clear that the simple approval or disapproval of a potential purchaser by the franchisor is not considered to be significant involvement of the franchisor in the sale of the franchise.
a franchisee is not a prospective franchisee and the transaction itself is not a sale of a franchise, then the franchisor will not have a disclosure obligation. Hence, the determining factor in the analysis is the franchisor’s level of involvement.

To understand what levels of involvement do not trigger franchisor’s disclosure obligation, we can look to the Amended Franchise Rule and the Compliance Guide. Under the Amended Franchise Rule, “a franchisor’s approval or disapproval of a transfer alone is not deemed to be significant involvement.” So, what is? According to the Compliance Guide, providing financial performance information constitutes significant involvement. Other examples of franchisor actions that may constitute significant involvement are discussed below.

(2) **How does the analysis differ when the franchise is in a Registration State?**

The Registrations States each provide an exemption for the transfer of a franchise from franchisor’s disclosure and registration obligations where the sale is not effected by or through the franchisor. The key here is that transaction must “not [be] effected by or through the franchisor” which is very similar to the “no significant involvement” threshold under the Amended Franchise Rule. The majority of Registration States also provide that approval alone does not trigger franchise disclosure or registration obligations for the franchisor. Several Registrations States go further and explicitly provide that the imposition of a reasonable transfer fee is also not a trigger. As such, the analysis in most Registration States is largely the same as in FTC Disclosure States.

An example of the analysis can be found in Drake v. Maid-Rite Co, where the appellant-plaintiff, who previously purchased a Maid-Rite franchise from Sam Sweeden (an existing Maid-Rite franchisee), appealed the lower court’s finding that the sale of the franchise was not effected by or through the franchisor. The appellant argued that Sweeden was an agent because he was acting in furtherance of Maid-Rite’s interest by helping Maid-Rite expand into Indiana by purchasing a franchise and reselling it. The Indiana Court of Appeals reasoned that if it accepted appellant’s argument, “franchisees who acquire a franchise and subsequently sell it are acting in the interest of and are therefore agents of the franchisor.” The Court refused to accept this argument and noted that the appellant offered “no evidence of communication or contact, direct or indirect, between herself and Maid-Rite prior to purchasing the restaurant from Sweeden.” Based on this and the lack of other evidence in

---

33 16 C.F.R. § 436.1(t).

34 See Appendix B.

35 These states include California, Illinois, Indiana, Maryland, Minnesota, New York, North Dakota, Oregon, Rhode Island, Virginia, Washington, and Wisconsin.

36 These states include Illinois, Rhode Island, Virginia, Washington, and Wisconsin.

37 681 N.Ed.2d 734 (Ind. Ct. App. 1997).

38 Id.

39 Id.
support of the sale being effected by or through the franchisor, the Court, determining that there
was no genuine issue of fact, held that the trial court did not err in its finding.\textsuperscript{40}

In a few of the Registration States, the analysis is complicated by additional conditions
impacting the applicability of the transfer exemption. One such condition is that the sale must
be an isolated sale for the exemption to apply.\textsuperscript{41} Under Minnesota’s law, only one sale during
any 12 month period is exempt.\textsuperscript{42} Franchisors approving transfers in Minnesota must be mindful
if a franchisee is planning to transfer more than one franchise during any 12 month period.
Other potentially troublesome states are New York, Michigan, and North Dakota. Under the
New York Franchise Act, the franchisee must give the prospective purchaser a copy of the
disclosure document that is currently registered at least one week before the earlier of the
signing of any binding agreement or the receipt of any consideration.\textsuperscript{43} So, although there is an
exemption for transfers where franchisor’s involvement is limited, franchisor’s registration must
be effective in New York to comply. In Michigan, a franchisee selling its franchise must provide
the prospective purchaser “full access to the books and records related to the franchise.”\textsuperscript{44} In
North Dakota, subfranchisors selling a franchise must obtain the commissioner’s written
approval. And, it is within the commissioner’s discretion to require the subfranchisor and the
franchisor to provide information and disclosures to the prospective purchaser and to the
commissioner.\textsuperscript{45} Because these conditions on exemption rely on actions by the franchisee or
subfranchisor, franchisors would be wise to require proof of compliance before approving
transfers in these states.

What elements of a franchisor’s approval process are unlikely to trigger franchise
disclosure and registration obligations?

As outlined above, franchisors may approve transfers and require a transferring
franchisee to pay a transfer fee without triggering franchise disclosure and registration
obligations. Although there is not much guidance on what other franchisor activities would be
below the threshold, the authors of this paper believe it is fair to surmise that in most cases a
franchisor approval process including the following would not trigger franchisor disclosure and
registration obligations: franchisor evaluation of the prospective purchaser’s financial
wherewithal, business acumen, and compatibility with the franchise system; a requirement that
the franchisee-transferor obtain a signed confidentiality agreement in favor of franchisor from
the prospective purchaser; franchisor review and approval of the purchase agreement; a
requirement that the prospective purchaser sign the same form of guarantee as was signed with

\textsuperscript{40} See also Godfrey v. Schroeckenthaler, 177 Wis.2d 1, 501 N.W.2d 812 (Wis. Ct. App. 1993)
(holding that the franchisee’s sale of its franchise was for its own account and thereby
exempt from the Wisconsin franchise investment law registration requirements).

\textsuperscript{41} These states include Hawaii, Michigan, Minnesota, and New York.

\textsuperscript{42} Minn. Stat. § 80C.03

\textsuperscript{43} N.Y. Laws § 684.

\textsuperscript{44} Mich. Comp. Laws § 445.1506.

\textsuperscript{45} N.D. Cent. Code § 51-19-04
the franchise agreement being transferred; and evidence from the franchisee-transferor of compliance with franchise investment law obligations.

What elements of a franchisor’s approval process are likely to trigger franchise disclosure and registration obligations?

Activities that would likely trigger disclosure and registration obligations include requiring a prospective purchaser to sign a new franchise agreement or to pay a fee directly to franchisor. These requirements would make the prospective purchaser a prospective franchisee and would require disclosure and registration, as applicable. Providing financial performance information to the prospective purchaser or financing the purchase of the franchise would also trigger disclosure and registration obligations. And, the clearest indication of significant franchise involvement or that a sale that is effected by or through a franchise is that the transaction was brokered by the franchisor. In Interstate Automatic Transmission Company, Inc. v. Harvey, the Michigan Court of Appeals held that the franchisor was liable under the franchise investment law where franchisor “undertook to act as broker for [franchisee-transferor] in the selling of the franchise and preparation of all legal documents in connection therewith.” If franchisors wish to avoid disclosure and registration requirements, they should steer clear of these activities.

Renewals

(3) When does renewal of a franchise agreement trigger FDD disclosure?

Sometimes it happens. Franchisor and franchisee are surprised to discover that the parties’ franchise agreement is about to expire. Both agree that the franchise agreement should be renewed and the franchise agreement provides for renewal on the franchisor’s then-current form. But, the then-current form contains terms that are materially different from those in franchisee’s existing agreement, and there is no time to make a proper disclosure prior to the franchise agreement’s expiration.

The Amended Franchise Rule provides that the sale of a franchise “does not include extending or renewing an existing franchise agreement where there has been no interruption in the franchisee’s operation of business, unless the new agreement contains terms that differ materially from the original agreement.” Accordingly, the disclosure requirement is not triggered by the mere renewal of a franchise agreement but is triggered when the franchisee is required to sign a then-current form that contains terms that differ materially from those contained in the franchisee’s original agreement.

It is important to note that the Commission in Informal Staff Advisory Opinion 97-8 advised that “terms that differ materially from the original agreement” includes material changes

---


47 16 CFR 436.2(k).

48 See also the Compliance Guide at 18.
“in the franchisor’s business, such as new litigation or a bankruptcy filing.”\textsuperscript{49} It then follows that even when renewing or extending an existing agreement without changing anything other than the term of the agreement, disclosure is required if there has been a material change in the franchisor’s business.

(4) \textbf{When disclosure is not possible, are there any other options?}

(a) \textbf{Extending the term of the franchise agreement.} The Amended Franchise Rule treats extensions the same as renewals.\textsuperscript{50} As long as the extension is limited to extending the term of the franchise agreement and does not include any change in material terms, disclosure is not required.\textsuperscript{51} Although there is very little case law interpreting the disclosure requirements upon extension of a franchise agreement, what does exist has held that disclosure obligation is not triggered by the renewal or extension of a franchise agreement alone. In Rich Food Services, Incorporated v. Rich Plan Corporation,\textsuperscript{52} a franchisee sued its franchisor alleging, inter alia, that its franchisor failed to make the disclosures required under federal and New York law. The court held that the franchisor was not required to make the federal or New York franchise disclosures because the latter “agreement was a renewal or extension under the franchise disclosure laws because it functioned only to lengthen an existing franchise relationship.”\textsuperscript{53} When a franchise agreement will expire prior to the end of the 14 day cooling off period needed to comply with the disclosure obligation, extending a franchise agreement at least until the end of the cooling off period may be a more viable option than renewing it on its existing terms.

(b) \textbf{Amending the franchise agreement.} Amending a franchise agreement when renewing or extending is a little trickier. The Amended Franchise Rule provides that, on renewal or extension of a franchise agreement, the element that triggers the disclosure obligation is the existence of terms that differ materially from the franchisee’s original agreement. Therefore, any amendment or modification of a term of the franchise agreement on renewal or extension would trigger disclosure. However, if the amendment is not executed while renewing or extending, the implication is that amendment of material terms (other than the term of the agreement) does not require disclosure. In Informal Staff Advisory Opinion 02-3, the Commission advised that “a franchisee-initiated modification of an existing franchise agreement alone does not constitute the ‘sale of a franchise.’”\textsuperscript{54} The Commission limited its review to

\begin{itemize}
\item \textsuperscript{50} 16 C.F.R. § 436.1(t).
\item \textsuperscript{51} See Perry v. Meredith Corp., 77 Fed.Appx. 128 (4\textsuperscript{th} Cir. 2003) (holding that franchise disclosure was not required where an amendment’s only material change was to extend the term).
\item \textsuperscript{52} 98 Fed.Appx.206, 2004 WL 937260 (C.A.4 (N.C.)).
\item \textsuperscript{53} Id. at 210.
\end{itemize}
franchisee initiated modifications. As such, although a franchisee-initiated amendment is permissible without disclosure and an amendment of a material term that does not impact the term of an agreement is likely permissible without disclosure, it appears that amending a material term of an existing agreement when renewing or extending an existing franchise agreement would not be permissible without disclosure.

(c) **Signing a non-binding LOI.** A non-binding letter of intent (which is discussed earlier in this paper) paired with a short term extension may be a franchisor’s most attractive option. With this option, the franchisor can comfortably extend the franchise agreement to allow time for proper disclosure and at the same time outline (in the non-binding section of the LOI) the terms of the franchisor’s then-current franchise agreement that may differ from franchisee’s existing agreement. Presenting the LOI to the franchisee before agreeing to extend the agreement would allow the franchisee and the franchisor the opportunity to discuss the terms of the franchisor’s then-current form and explore each other’s interest in signing a new franchise agreement.

(5) **How does the analysis differ when the franchise is in a Registration State?**

All but one of the Registrations States have excluded renewals without terms that are materially different either by excluding such renewals from the definition of “offer” or “offer to sell” or by providing an exemption. Indiana, New York, North Dakota, South Dakota, and Wisconsin, exclude renewals from the definition of “offer” or “offer to sell” while California, Hawaii, Illinois, Maryland, Michigan, Oregon, Rhode Island, Virginia, and Washington provide a specific exemption for renewals. Minnesota, on the other hand, specifically includes “renewal or extension of an existing franchise” in its definitions of sale, sell, offer, and offer to sell. So, as long as the franchise is not in Minnesota and the renewal franchise agreement does not contain terms that are materially different from the original franchise agreement, the disclosure requirement is not triggered.

Most franchise agreements drafted today provide for renewal on the franchisor’s then-current form. Given that disclosure is required if that form contains terms that are materially different than those in the franchisee’s existing agreement, the analysis in the Registration States is the same as in a state subject only to the Amended Franchise Rule. There is one twist: In California and North Dakota, the disclosure requirement for material modifications of an existing franchise agreement is that the franchisor must disclose with specificity the modifications to each section of the existing franchise agreement. Accordingly, in California and North Dakota a franchisor must provide an existing franchisee written notification of the specific

---

55 See Appendix B.

56 The renewal exemption in Washington is not as straight forward as the exemption in the other states. The Washington exemption refers to the offer or sale of an additional franchise to an existing franchisee but does not specifically provide an exemption for renewals. As long as the franchisee’s franchise agreement has not yet expired, the renewal of the franchise agreement would technically be the sale of an additional franchise to an existing franchisee, and should therefore be exempt from the disclosure requirement.

57 See Appendix B.
Practically speaking, to comply with both federal and state requirements, a franchisor renewing or extending a franchise agreement with material modifications in California and North Dakota would have the added state law requirement of having to provide a disclosure outlining the specific material modifications.

(6) **What best practices should franchisors implement?**

Franchisors should diligently monitor franchise agreement expiration dates and plan ahead for dark periods. A lack of planning may result in inadvertent violations of franchise disclosure and registration requirements while updating its FDD or renewing its state registrations and exemptions. It may make sense for a franchise to provide its FDD prior to the expiration of a franchise agreement. A franchisor may also decide to not only provide the FDD early but to permit the franchisee to renew early.

**UNIQUE DISCLOSURE ISSUES**

**Disclosing Multiple Concepts In One Franchise Disclosure Document**

The merger and acquisition craze of the first decade of this century resulted in many companies owning multiple franchise systems, either directly, or through affiliated entities. Some companies found it more expedient to use one disclosure document to describe offerings of multiple brands. When is this permitted, and when is it advisable?

(7) **When Is It Permissible To Use a Single FDD?**

In order for multiple brands to be disclosed in a single FDD, the various brands must be owned by a single entity; not by affiliates, but by a single entity. Although the Amended Franchise Rule does not contain such a requirement, the state registration laws require that the person who grants the franchise register the offering, and provide a disclosure document. Thus, by practice, the states require that each franchisor register with them (and each pay an initial filing fee), and that each franchisor provide a disclosure document describing their offering. Two affiliated companies would therefore have to each register their franchise for sale, and each provide their own disclosure document to prospective franchisees.

The foregoing is not true, however, when one franchisor offers multiple brands. In this case, the “person” who is granting the franchise, and thus, the person who is required to register, is the same for each brand. Thus, the states will generally accept a single registration by one franchisor who is offering multiple concepts pursuant to a single disclosure document.

---

58 See In re: Conoco Phillips Co., 2010 WL 2231875 (N.D.Cal.) (The court dismissed the plaintiff franchisee’s claim for relief alleging that its franchisor violated the California Franchise Investment Law by not providing the required disclosures. The court found that the disclosure obligation applies to new franchise agreements and not renewals and that a material modification of an existing franchise agreement required the franchisor to provide notice of the material modifications but did not trigger the same disclosure obligations that exist for new franchise agreements.).
There is, however, a way to turn two franchisors into one! It is best exemplified by a registration maintained by American Dairy Queen Corporation ("ADQ"). ADQ is the franchisor of the Dairy Queen brand. However, ADQ is also a subfranchisor of Orange Julius of America, one of its affiliates, and has the right to sublicense the Orange Julius name and mark for combination Dairy Queen/Orange Julius units. Through this subfranchise arrangement, ADQ becomes the franchisor for both brands and is able to maintain just one registration, and one disclosure document by which it offers these combination units. (ADQ does not use this FDD to offer units that exclusively offer the Dairy Queen products, but there is no reason they could not do so.)

(8) When Is It Practical To Have Multiple FDDS?

The more difficult question is not whether it is possible to offer multiple franchises through one disclosure document, but whether a franchisor should want to include multiple offerings in one disclosure document. Along the same lines, when would a state be justified in rejecting such an application? The Amended Franchise Rule requires that all disclosures be prepared “clearly, legibly, and concisely in a single document. . . .” If a single entity owned, for example, a service franchise, and a restaurant franchise, with different officers, different fees, and different agreements, it would be hard to imagine that both concepts could be combined into a single document that is written “clearly,” and “concisely.” If it could not, the disclosure document would not meet the requirements of the Amended Franchise Rule, and state regulators would certainly be acting within the scope of their authority to refuse to accept the document for registration.

Even if one could argue that an offering of the foregoing nature would comply with applicable legal requirements, the authors of this paper generally recommend against preparing such a disclosure document. Any possible administrative or cost savings that might exist in having only one disclosure document and one registration for these offerings will be more than offset by the potential loss of one franchise sale from a confused franchisee. Moreover, these savings will pale in comparison to the cost and burden of defending one subsequent lawsuit that alleges the disclosures were too complicated for the plaintiff (and likely, a jury) to understand.

In practice, many franchisors reach this same conclusion even when offering franchises for similar types of businesses. For example, in the hotel industry, historically, Hilton Hotels Corporation (now Hilton Worldwide, Inc.) operated several brands, including Hilton and Hilton Garden Inn, while a sister company, Promus Hotels, Inc., also owned multiple brands, including Embassy Suites and Homewood Suites by Hilton. The franchise agreements for all these brands were identical. However, the personnel involved in the systems was not the same, the litigation history was not the same, the initial fees were not the same, the initial investment was not the same, and so forth, and these companies therefore made the decision to have separate disclosure documents for each brand.


60 16 C.F.R. § 436.6(b) (2009).
That is not to say there will not be situations where it would be more efficient for the franchisors, and easier for a franchisee to understand its options, when multiple brands are included in one disclosure document. This is particularly true for brands that offer combination units. The previously mentioned ADQ registration is such an example. However, the combination units that are offered could be even more extensive. At one time, Allied Domecq owned the Dunkin Donuts, Baskin Robbins, and Togo brands. They offered individual franchises for each of these brands, but they also offered combination units that might include all three of the brands, or any two of the three brands. They used one Offering Circular to describe all the offerings. The document was over 1,000 pages in length (the list of franchisees of all the brands consumed hundreds of pages). However, preparing a different disclosure document for each combination, and knowing ahead of time which document to give a prospective franchisee (especially when delivery of the document was required no later than the first personal meeting with the prospective franchisee) would have been difficult. Thus, all the offerings were combined into a single document.

From a practical standpoint, in advising clients, the decision whether to have one disclosure document or multiple disclosure documents should never turn on the cost of producing or registering the document. Rather, the authors suggest that the decision should turn on the best way to "clearly, legibly, and concisely" describe the offering or offerings that are available to prospective franchisees.

Financial Performance Representations – How Can A Franchisor Properly Provide Information That Is Not In The FDD?

The requirements of Item 19 of the Amended Franchise Rule are clear: “If the franchisor makes any financial performance representations to prospective franchisees, the franchisor must have a reasonable basis and written substantiation for the representation at the time the representation is made and must state the representation in the Item 19 disclosure (emphasis added).” However, there are exceptions to the Amended Franchise Rule, and even if there were no exceptions, not all financial performance numbers constitute financial performance representations.

(9) Financial Representations that Fall within Specific Exceptions to the Amended Franchise Rule.

(a) Expenses. Cost information is no longer included within the definition of an FPR under the Amended Franchise Rule. However, there are still two caveats with respect to the provision of cost information. First, the FTC has verbally taken the position that cost information, expressed as a percentage of sales, is subsumed within the definition of “sales,” and thus is prohibited, even if no level of sales is shown or suggested. In addition, as of the date of this writing, there are still three states that specifically include costs in the information that cannot be provided to franchisees outside of Item 19.  

61. 16 C.F.R. § 436.5(s).

62. These states are Illinois, Maryland and New York. See Ill. Admin. Code tit. 14A, Appendix A, Illustration L; Md. Regs. Code tit. 2, §02.02.08.16; and New York N.Y. Comp. Codes R. & Regs. tit. 13, §200.2(c). In addition, while not specifying costs, Minnesota requires
(b) **Actual Operating Results of An Outlet Offered For Sale.** The first exception to this rule is that a franchisor is permitted to disclose the actual operating results for a specific outlet being offered for sale. In that case, the disclosure need not comply with any of Item 19, but it can be given only to potential purchasers of that outlet. In addition, pursuant to the requirements for Item 20, if the outlet is then under the control of the franchisor, there must also be disclosure of additional information concerning the outlet for the last five fiscal years. Best practices would suggest that any franchisor using this exception document the circumstances, and obtain an acknowledgment from the perspective franchisee that they received the additional information concerning the outlet.

(c) **Supplemental Financial Performance Representations.** The second exception is a broader one, but it applies only if the franchisor includes a financial performance representation in its disclosure document. In that case, the franchisor may deliver to a prospective franchisee a supplemental FPR about a particular location or variation, apart from the disclosure document, so long as the supplemental representation is in writing, explains the departure from the FPR contained in Item 19, and otherwise complies with the requirements for inclusion of an FPR in Item 19. This second exception gives a franchisor a great deal of leeway, but again, it applies only if the franchisor has a financial performance representation in its FDD.

There is no limitation on the type of “supplemental” FPR that can be provided. It could be a projection aimed specifically at a particular site the franchisee already owns, perhaps showing how operations might be improved by renewing the franchise and remodeling the unit. It might be a projection specific to a particular site the franchisee is considering acquiring for the franchised business.

A supplemental FPR could also be a representation not geared to a specific location, but to a unique set of facts. For example, it might be an FPR prepared for a business proposed to be open 24 hours a day when typical units are not always open. Another example is a smaller (or larger) than typical site, or one offering products or services that are not typically offered in franchise units and are expected to generate increased sales from the model shown in Item 19. In all these cases, the franchisor must still have a reasonable basis for the projection, and could not simply provide a projection based on a set of circumstances that has never occurred in the

---

63 16 C.F.R. § 436.5(s)(4).

64 16 C.F.R. § 436.5(t)(6). The additional information required by Item 20 may be attached as an addendum to the disclosure document, or in a supplement to a previously furnished disclosure document. The information includes the name, city and state, current business telephone (or if unknown, the last known home telephone number) of each previous owner of the outlet, the time period when each previous owner controlled the outlet, the reason for each previous change in ownership, and the time periods when the franchisor retained control of the outlet.

65 16 C.F.R. § 436.5(s)(5).
past. However, the supplemental disclosure provisions do provide great leeway to the franchisor to generate a separate FPR, specific to a particular site or set of facts.

A supplemental information disclosure may also be appropriate as the information in Item 19 becomes more dated. The supplemental disclosure provisions would allow the franchisor to provide updated results of its franchised and company-owned units based on operating improvements that have occurred since the publication of the FDD. (To the extent the operating results have materially deteriorated, the franchisor already has an obligation to provide, not a supplemental disclosure, but either an amended FDD or, pursuant to the Amended Franchise Rule, a specific notification of any material changes relating to the FPR that is known at the time the FDD is furnished.66 The Compliance Guide makes clear that the seller may inform the prospective franchisee of a material change “in any reasonable manner, such as by letter, telephone call, or email.”67 However, as the Compliance Guide further states, “the franchise seller has the burden of proving that such notification was made.” Thus, best practices would suggest the disclosure be made in writing.)

A supplemental disclosure may even be made by providing numbers that are not reflective of this franchisor’s operations. For example, it could be detail of the revenues of nearby units owned or franchised by competitors, information that is readily available in the hospitality industry. This disclosure would be a more complicated one, because it would still need to disclose the source of the information (which must be a reliable source in order to meet the requirement that the franchisor have a “reasonable basis” for making the representation), it would need to include the other information required by Item 19, and it would need to show how this information varies from the representation already included in Item 19.68 Further, to the extent the financial results of competitive units are very different from the financial results of this franchisor’s units, to avoid any claims of misrepresentation by omission, the disclosure should make very clear that these results are provided not as a suggestion of the likely results of a franchised unit, but rather, to show the market opportunities. However, in the hospitality industry, where many systems are primarily comprised of multi-unit franchisees, those franchisees may not only be sophisticated, but also familiar with the operations of competitors, and in those cases, the provision of competitor information in the market can be very helpful to a prospective franchisee.

The danger in providing a supplemental disclosure, and the reason many attorneys fail to discuss the option with their clients, is that the nature of the requirements make it very difficult for a sales person to simply prepare a supplemental disclosure without the assistance of counsel. And, of course, when sales people know they have the ability to provide additional financial information, there is always a tendency to want to “talk numbers.” Business people must therefore be reminded that the disclosure cannot be made orally, and it is not something that can be prepared on the back of a napkin. Rather, it actually requires more disclosure than an FPR contained in Item 19, because it must not only include everything required of a disclosure in Item 19, but it also must show the variances from the published disclosure.

66 16 C.F.R. § 436.7(d).
67 Compliance Guide at 129.
68 16 C.F.R. § 436.5(s)(v)(5).
While the Compliance Guide does not contemplate any other FPR being provided outside the FDD, this does not mean that no operating results can ever be provided to prospective franchisees outside of Item 19. While someone may term some of the ideas that follow as “pushing the envelope,” the fact is that there are a number of lawful ways of transmitting information on operating results to prospective franchisees.

(a) **Audited Financial Statements.** Item 21 already includes a requirement that annual financial statements, in most cases audited, be provided to prospective franchisees. Those financial statements include a statement of operations. Particularly in the case of smaller franchisors, those operating statements may identify revenues from company-owned units if those units are operated by the same entity that offers franchises. If the franchisor opened and/or closed a number of units during the year, it would be impossible for a prospective franchisee to look at this information and obtain an accurate average of the revenues from each company-owned unit. However, if the number of units operated during the year was constant, then prospective franchisees could identify average revenue numbers, and possibly profit and loss information, from the statement of operations that are a part of the audited financial statements. (While many franchise attorneys counsel start-up clients to establish a separate franchise company, distinct from the entity that operates company-owned units, to offer franchises, and there are certainly a number of reasons for doing so, this is one reason that some companies may prefer to use their existing entity.)

(b) **Financial Information Provided Outside the Context of The Sale of a Franchise.** The prohibition on disclosure of financial information applies in connection with the sale of a franchise. The law does not apply to the disclosure of financial information in other contexts. There are numerous other situations in which financial information is published and, in many cases, available to prospective franchisees.

(i) **Press Releases and News Stories.** There is nothing in the Amended Franchise Rule that prohibits companies from issuing press releases, or talking to reporters about their results. The Compliance Guide specifically provides that FPRs include representations in general media advertising, but do not include speeches, press releases, and the like that are not “specifically directed at members of the public interested in purchasing a franchise.” To be clear, we are not suggesting franchisors can direct franchisees to this information, or provide copies of press releases, or even printed articles, to prospective franchisees. Indeed, such action is prohibited by the Compliance Guide. However, if the information is quoted extensively in articles of general publication, prospective franchisees will find it on their own.

(ii) **S.E.C. Disclosures.** Public companies are required to disclose significant operating information to the public in general, and to the investment community in particular. Such information will frequently include average per store sales and

---


70 Compliance Guide at 131.

71 *Id.* at 132.
profits, comparative sales and profits, costs of goods sold as a percentage of sales, and other information relevant to shareholders. In the FTC Statement issued with the Amended Franchise Rule, the FTC made clear that such information “is for the benefit of more than prospective franchisees, including investors, potential suppliers, and members of the general public,” and thus the Amended Franchise Rule is not intended to apply to such information. Of course, it would still not be appropriate to direct prospective franchisees to these reports. On the other hand, it is public information that any prospective franchisee can find if they have a computer with Internet access.

(iii) Operating Information Needed by Existing Franchisees. In many systems, existing franchisees are the best prospects for future development. There is no exemption in the Amended Franchise Rule, or in any of the state laws, permitting franchisors to provide financial information to existing franchisees to induce them to purchase a franchise. However, outside the sales process, many franchise systems provide extensive financial information to their franchisees to assist them in the operation of their business. As an example, many restaurant systems provide their existing franchisees with information as to average revenues, gross profit margins, operating cost percentages, and average check of both company-owned and franchised units throughout the system, as well as those in the same market, so that existing franchisees will have benchmarks that inform them how they are performing vis-à-vis other franchisees. Such information is very valuable in helping existing franchisees improve their operations, and franchisors that provide this information are providing a very valuable service to their franchisees. The fact that some of these existing franchisees may be prospects for a new franchise does not change either the legality of providing this information to franchisees to assist them in their operations, or the necessity for doing so.

This is not to say that franchisors have a “loop hole” for providing financial information to prospective franchisees. It would certainly be improper for a franchisor to encourage its existing franchisees to share this information with prospective franchisees. Moreover, in providing this information to existing franchisees, the franchisor still must ask itself what the purpose is for providing the information. If the information has never been previously provided, and all of a sudden the franchisor embarks on an aggressive expansion program that targets existing franchisees for new outlets, then one would have to question whether the purpose of providing that information was to assist franchisees in operating their existing businesses, which is both permissible and extremely valuable, or to encourage them to acquire additional units, which would be a prohibited FPR. However, sophisticated franchisors are in many cases already providing this information to their franchisees, and there is no law that requires franchisors cease doing so simply because those franchisees may be interested in purchasing additional units, or may be targeted for additional franchise opportunities.

In providing this information to existing franchisees, franchisors also need to be careful as to the context in which the information is provided. For example, most franchise systems have annual conventions, and for larger systems, one of the agenda items for the convention may be to introduce franchisees to expansion opportunities. At that same convention, the franchisor's President (or others) may be giving extensive information as to the system’s operating results in his or her “state of the system” address. In fact, in that same speech, the President may want to talk about expansion opportunities. The authors believe both topics are permissible subjects in that context, but caution that the context in which the financial information is imparted is critical. Presenting positive operating results as a rallying point for the

convention is permissible, as is discussing expansion opportunities, but providing operating information in the context of a discussion of expansion opportunities is clearly an FPR that would be prohibited if not included in the franchisor's FDD. It is a fine line that franchisors need to be careful not to cross.

(11) Exempt Transactions

As discussed elsewhere in this paper, there are now numerous situations, particularly under federal law, where a sale is exempt from the disclosure requirements. For example, if a prospective franchisee has been in business for at least five years and has a net worth of $5 million, which is frequently the case in the hospitality industry, the offer and sale of a franchise is exempt from the disclosure requirements of the Amended Franchise Rule.73 In those situations, the prohibitions contained in the Amended Franchise Rule simply do not apply. Thus, not only is there no requirement for delivery of a disclosure document, but there is no restriction on the information that can be provided to prospective franchisees, including the provision of an FPR that would not otherwise be included in the franchisor’s FDD or meet the requirements of Item 19. The same would be true for a franchise involving an investment of at least $1 million that is not funded in any part by the franchisor.74

While many of the registration states also have exemptions, you need to be careful in three respects. First, in most cases, the state exemptions do not mirror the federal exemptions. Second, you must confirm that the exemption is not only an exemption from registration, but also from disclosure. Third, you must be certain there is not a separate requirement related to the provision of financial information.

Some of the differences between the state and federal exemptions were discussed earlier in this paper will not be repeated in this section. With regard to the requirement for delivery of a disclosure document, the exemption in Illinois, Rhode Island and Washington is an exemption from registration, but franchisors are still required to provide a disclosure document complying with the FTC requirements.75 Thus, in those states, the exemption will not apply to the provision of an FPR.

In South Dakota, there is a sophisticated franchisee exemption available that applies to both registration and delivery of a disclosure document. However, there is a separate statutory provision stating that franchisors may not disseminate any FPR to prospective franchisees unless they have a reasonable basis and “written substantiation” for the representation at the time it is made, and the representation is included in the franchisor’s disclosure document.76 Thus, if an FPR is made in South Dakota, it would still have to be included in the FDD, and in that case, the FDD would presumably have to be provided to a sophisticated investor. The same would obviously be true of any state that did not have an available exemption for the transaction.

73 16 C.F.R. § 436.8(5)(ii).
74 16 C.F.R. § 436.8(5)(i).
76 S.D. Codified Laws § 37-5B-13(2).
We would offer one other caution to franchisors in connection with the delivery of financial information to prospective franchisees. When the information is provided in the FDD, it has likely been reviewed and sanitized by legal counsel. It is accompanied by extensive disclosure of assumptions, disclaimers, footnotes, and so forth, to assure that the information is not misleading and does not omit to state material facts necessary to keep the information from being misleading. Financial information provided to prospective franchisees, and to existing franchisees in connection with the solicitation of additional franchise sales, should always be given this scrutiny, even when lawfully provided outside the FDD, because even if the franchise disclosure laws do not apply, there are no exemptions from common law claims for fraud or misrepresentation.

**Phase-In Of Audited Financial Statements**

Section 436.5(u)(2) of the Amended Franchise Rule retained the original Rule provision permitting start-up franchise systems to phase-in audited financial statements within three years but clarified several issues on how the phase-in was to work.

The phase-in works as follows:

(1) When a new franchisor initially prepares an FDD for the sale of franchises, it need only provide an unaudited opening balance sheet prepared in accordance with GAAP. Even when a franchisor takes advantage of the phase-in, the data underlying the financial statement must be prepared according to GAAP (or SEC standards).

(2) In its second fiscal year, the franchisor must include an audited balance sheet opinion on its financial condition based on its opening balance sheet and a balance sheet prepared at the end of its first fiscal year.

During the third fiscal year, and continuing thereafter, the franchisor must include all required financial statements.

There are no comparable provisions in the Registration States, and a franchise practitioner needs to examine each individual state’s law, applicable regulations and administrative procedures. California and Illinois permit a phase-in of audited financial statements under limited conditions.

For example, California provides for the use of unaudited statements in extraordinary cases such as where (1) the franchisor has not had prior audited statements, (2) the close of the most recent or current fiscal year is so near the time of filing of the application that it would be “unreasonably” costly or impractical to provide audited statements with the application, and (3) that audited statements will be furnished within a reasonable time after the end of the most recent or current fiscal year. Use of un-audited statements does not relieve the franchisor from liability for false and misleading statements in the financial documents.\(^7\)

---

\(^7\) CAL. CODE REGS. tit. 10 §310.111.2 (2010).
What is a start-up? The Commission has stated that the term “start-up” was to be read narrowly, meaning “entities that are new to franchising and that ordinarily have not prepared audited financials to date”\(^{78}\)

The non-franchise company that has prepared audited financials in the ordinary course of business must include such audited financials in an FDD upon commencement of an offering to sell franchises.

The phase-in is also not intended for spin-offs, affiliates, or subsidiaries of a franchisor, where the franchisor “has been engaged in franchising” or “has prepared audited financial statements for any purpose.

5. CONCLUSION

The Amended Franchise Rule makes the late Friday afternoon call described in the Introduction easier to address, especially if a Registration State is not involved in the proposed transaction. FDD delivery requirements have more clarity. You can focus your attention on the payment of money to the franchisor or an affiliate (not permitted) and the nature of the binding (not permitted if it relates to a franchise sale) and non-binding commitments (permitted) being negotiated. Have a form LOI with clear non-binding language handy.

You should also factor into the analysis expanded exemptions under the Amended Franchise Rule, which may make the Friday 6:00 p.m. call an easy one to answer. Registration State exemptions, if applicable, should be checked.

In addition, if a Registration State is involved in the analysis, determine if the state has adopted the Amended Franchise Rule’s FDD delivery requirements. If not, your advice will likely be more conservative.

As stated above, best practices in most situations are to advise your client as follows: (1) do not sign a binding agreement that commits a prospective franchisee to buy a franchise; (2) do not take any money from the prospective franchisee; (3) give accurate information on the status of your FDD; (4) give the FDD when completed; and (5) following the appropriate “cooling off period”, proceed.

\(^{78}\) FTC Statement, 72 Fed. Reg. 15512.
APPENDIX A – FORM LETTER OF INTENT

FORM OF LETTER OF INTENT

Re: Proposal for Possible Purchase of Franchise Development Opportunity

The purpose of this letter (the "Letter") is to set forth certain nonbinding understandings and certain binding agreements between Prospective Buyer, LLC and its members (collectively “Prospective Buyer”) and ABC Co., Inc. (“Franchisor”).

This Letter will confirm that Prospective Buyer is interested in franchise development opportunities as described in paragraph 2 of this Letter, on terms that would be mutually agreeable. In this Letter, (a) Prospective Buyer and the Franchisor are sometimes called singularly a “Party” and collectively the “Parties”; and (b) Prospective Buyer’s possible purchase of a franchise development opportunity is sometimes called the “Possible Purchase”.

NONBINDING PROVISIONS

The Parties wish to commence negotiating definitive and fully integrated written agreement (the “Definitive Agreement”) providing for the Possible Purchase. The following numbered sections of this Letter (collectively, the “Nonbinding Provisions”) reflect the Parties’ mutual understanding of the matters described in them, but each party acknowledges that the Nonbinding Provisions are not intended to create or constitute any legally binding obligation between Prospective Buyer and Franchisor. Prospective Buyer and Franchisor will not have any liability to the other with respect to the Nonbinding Provisions until (i) Franchisor has complied with all applicable franchise laws and (ii) the Definitive Agreement, and other related documents, are prepared, authorized, executed and delivered by and between all Parties.

If the Definitive Agreement is not authorized, executed or delivered for any reason, no Party to this Letter will have any liability to any other Party to this Letter based upon, arising from, or relating to the Nonbinding Provisions.

Based upon the information currently known to Prospective Buyer, it is proposed that the Definitive Agreement include the following terms:

1. Franchisor is the owner of the ABC proprietary trademarks, service marks and trade names (the “Marks”).

2. Among other activities, Franchisor has been engaged in the development of franchise concepts for the establishment and operation of retail outlets identified with one or more Marks that are in the business of selling food products, including roast beef sandwiches (the “ABC Outlets”).

3. Franchisor will enter into an area development agreement with Prospective Buyer and grant Prospective Buyer the right to own and operate five ABC Outlets in [fill in] (the “Development Area”) for a term of ten (10) years. So long as Prospective Buyer has substantially complied with the area development agreement during the initial term, additional terms (with no renewal fee) will be granted.
4. Franchisor will provide Prospective Buyer with:

(i) a license to use the Marks and other proprietary information in the Development Area;
(ii) specifications on proprietary food products to be sold at each ABC Outlet;
(iii) specifications on food and non-food supplies, paper goods and related products;
(iv) specifications on the proprietary kitchen layout for the cooking of the specified food products to be sold at the ABC Outlets;
(v) specifications on proprietary food preparation for the food products to be sold at the ABC Outlets;
(vi) menu development;
(vii) approved suppliers for the sale of food and non-food products;
(viii) two weeks of initial training; one week at Franchisor's training site and one week on-site at the initial ABC Outlet;
(ix) a proprietary Operations Manual;
(x) marketing materials;
(xi) ongoing advice and support.

All proprietary information (the “Proprietary Information”) as described above belongs solely to Franchisor.

5. Prospective Buyer will develop the five ABC Outlets in the Development Area (the “Development Schedule”) as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Number Open and Operating</th>
</tr>
</thead>
<tbody>
<tr>
<td>Year 1</td>
<td>1 ABC Outlet</td>
</tr>
<tr>
<td>Year 2</td>
<td>2 additional ABC Outlet</td>
</tr>
<tr>
<td>Year 3</td>
<td>3 additional ABC Outlet</td>
</tr>
<tr>
<td>Year 4</td>
<td>4 additional ABC Outlet</td>
</tr>
<tr>
<td>Year 5</td>
<td>5 additional ABC Outlet</td>
</tr>
</tbody>
</table>

So long as Prospective Buyer complies with this Development Schedule, Prospective Buyer's right to open and operate ABC Outlets in the Development Area shall be exclusive.

6. Prospective Buyer will pay:

(i) An Area Development Fee of $100,000 (One Hundred Thousand Dollars) as follows: $50,000 upon signing an Area Development Agreement with Franchisor and $50,000 to be paid six months thereafter;
(ii) a continuing royalty of five percent (5%) of the Gross Sales of the ABC Outlets operating in the Development Area; and
(iii) a continuing marketing fee of two percent (2%) of the Gross Sales of the ABC Outlets operating in the Development Area.

7. Prospective Buyer acknowledges that it has and will continue to receive Proprietary Information and agrees:

(i) not to disclose such information to third parties; and
(ii) that all such Proprietary Information belongs solely to Franchisor.

8. Prospective Buyer agrees that the proprietary food products and all other food and non-food products designated by Franchisor to be used in the ABC Outlets must be purchased from designed approved suppliers. All other items for use or sale at the ABC Outlets must be approved by Franchisor.

9. ALTHOUGH THIS LETTER CONTAINS PROPOSALS WHICH MAY BE LATER INCLUDED IN A BINDING AGREEMENT BETWEEN THE PARTIES, THESE PROPOSALS SHALL NOT BE A BINDING COMMITMENT BETWEEN FRANCHISOR OR PROSPECTIVE BUYER, BUT RATHER AN INDICATION OF THE DESIRE TO CONSUMMATE A TRANSACTION BETWEEN THE PARTIES. THE PARTIES' SIGNATURES BELOW ACKNOWLEDGE ONLY THAT THIS LETTER FAIRLY REPRESENTS THE PROPOSED RELATIONSHIP UNDER WHICH THE PARTIES EACH DESIRE TO MOVE FORWARD. THE PARTIES UNDERSTAND THE RIGHTS, DUTIES AND OBLIGATIONS DESCRIBED IN THIS LETTER ARE NOT AT THE CURRENT TIME INTENDED TO CREATE A FRANCHISE RELATIONSHIP IN ANY MANNER WHATSOEVER AND THAT THE TERMS HEREOF ARE IN ALL RESPECTS NONBINDING UNTIL A DEFINITIVE AGREEMENT CAN BE NEGOTIATED AND APPROVED BY ALL PARTIES.

BINDING PROVISIONS

Upon execution by the Franchisor and Prospective Buyer of this Letter or counterparts thereof, the following sections of this Letter (collectively the “Binding Provisions”) will constitute the legally binding and enforceable agreement of Franchisor and Prospective Buyer in recognition of the significant costs to be borne by Prospective Buyer and Franchisor in pursuing this Possible Purchase and further in consideration of their mutual undertakings as to the matters described herein.

10. Access to Information. Prior to delivery of a Franchise Disclosure Document, Franchisor shall provide to Prospective Buyer reasonable information concerning the ABC Outlets.

11. Exclusive Dealing. Upon execution of this Letter, Franchisor shall terminate existing discussions with others concerning franchise development opportunities in the Development Area (the “Opportunities”). For the period commencing on the date of this Letter is executed and ending on the earlier of November 30, 2010 or the date on which the Binding Provisions are terminated as provided in Section 14 below, Franchisor shall not, directly or indirectly, through any representative or otherwise, solicit or entertain offers from, negotiate with or in any manner encourage, discuss, accept or consider any proposal of any other person or entity relating to the Opportunities. Franchisor shall promptly notify Prospective Buyer of any offer, contact or discussion, unsolicited or otherwise, with respect to the Opportunities.

12. Disclosure. Except as and to the extent required by law, without the prior written consent of the other party, neither Prospective Buyer nor Franchisor shall directly or indirectly, make any public comment, statement or communication with respect to, or otherwise disclose or permit the disclosure of the existence of discussions regarding, a possible transaction between the Parties or any of the terms, conditions or other aspects of the possible acquisition proposed in this Letter. If a Party is required by law to make such disclosure, it must first provide to the other Party the content of the proposed disclosure, the reason that such disclosure is required by law, and the time and place that the disclosure will be made.
13. **Confidentiality.** Except as and to the extent required by law, Prospective Buyer will not disclose or use, and will direct its representatives not to disclose or use to the detriment of the Franchisor, any Confidential Information (as defined below) with respect to the Franchisor furnished, or to be furnished, by Franchisor to Prospective Buyer at any time or in any manner other than in connection with its evaluation of the Possible Purchase. For purposes of this Section, “Confidential Information” means any information about the Franchisor stamped “confidential” or identified in writing as such to Prospective Buyer by the Franchisor promptly following its disclosure, unless (a) such information is already known to the Prospective Buyer or to others not bound by a duty of confidentiality at the time of its disclosure or such information becomes publicly available through no fault of Prospective Buyer; (b) the use of such information is necessary or appropriate in making any filing or obtaining any consent or approval required for the consummation of the Possible Purchase; or (c) the furnishing or use of such information is required by or necessary or appropriate in connection with legal proceedings. Upon the written request of the Franchisor, Prospective Buyer will promptly return to the Franchisor or destroy any Confidential Information in its possession and certify in writing to the Franchisor that it has done so.

14. **Costs.** Prospective Buyer and Franchisor shall be responsible for and bear all of their respective own costs and expenses (including any broker's or finder's fees) incurred in connection with the proposed transaction, including expenses of its representatives, incurred at any time in connection with pursuing or consummating the proposed transaction.

15. **Termination.** The Binding Provisions may be terminated:

   a. By mutual written consent of Prospective Buyer and the Franchisor; or

   b. Upon written notice by any party to the other party if the Definitive Agreement has not been executed by November 30, 2010; provided, however, that the termination of the Binding Provisions shall not affect the liability of a party for breach of any of the Binding Provisions prior to the termination.

16. **Entire Agreement.** The Binding Provisions constitute the entire agreement between the Parties and supersede all prior oral or written agreements, understandings, representations and warranties and courses of conduct and dealing between the Parties on the subject matter hereof. Except as otherwise provided herein, the Binding Provisions may be amended or modified only by a writing executed by all of the Parties.

17. **Counterparts.** This Letter may be executed in one or more counterparts, each of which will be deemed to be an original of this Letter and all of which, when taken together, will be deemed to constitute one and the same letter.

Please sign and date this Letter in the space provided below to confirm the mutual agreements set forth in the Binding Provisions and return a signed copy to the undersigned.

Very truly yours,

_________________________________
Acknowledged and agreed as to the Binding Provisions:

ABC CO., INC.

By: _____________________________
Name: _____________________________
Title: _____________________________

_____________________, LLC

By: _____________________________
Name: _____________________________
Title:  Managing Member
APPENDIX B

REGISTRATION STATES TRANSFER AND RENEWAL EXCLUSIONS AND EXEMPTIONS

California:

TRANSFER EXEMPTION

Cal. Corp. Code § 31102

The offer or sale of a franchise by a franchisee for his own account or the offer or sale of the entire area franchise owned by a subfranchisor for his own account, is exempted from the provisions of Section 31110 if the sale is not effected by or through a franchisor. A sale is not effected by or through a franchisor merely because a franchisor has a right to approve or disapprove a different franchisee.

RENEWAL EXEMPTION

Cal. Corp. Code § 31018

(a) "Sale" or "sell" includes every contract or agreement of sale of, a contract to sell, or disposition of, a franchise or interest in a franchise for value.
(b) "Offer" or "offer to sell" includes every attempt to dispose of, or solicitation of an offer to buy, a franchise or interest in a franchise for value.
(c) The terms defined in this section do not include the renewal or extension of an existing franchise where there is no interruption in the operation of the franchised business by the franchisee; provided, that a material modification of an existing franchise, whether upon renewal or otherwise, is a "sale" within the meaning of this section.

Cal. Corp. Code § 31106

There shall be exempted from the provisions of Chapter 2 (commencing with Section 31110) of this part, any offer, sale, or other transfer of a franchise or any interest in a franchise, provided that the offer, sale or transfer meets the requirements in subdivisions (a) and (b):

(a) Any of the following conditions apply:
   (3) The offer, sale, or other transfer is of an additional franchise to an existing franchisee of the franchisor, or to an entity, one or more of the officers, directors, managing agents or owners of at least a 25 percent interest of which is an existing franchisee of the franchisor; provided that, in either case, for 24 months or more the franchisee, or the qualifying person, has been engaged in a business offering products or services substantially similar to those to be offered by the franchise being sold, or otherwise transferred.

(b) The franchisor files with the commissioner a notice of exemption and pays the fee prescribed in subdivision (f) of Section 31500 no later than 15 calendar days after the sale of a franchise in this state pursuant to this section.

MATERIAL MODIFICATION DISCLOSURE REQUIREMENT
Cal. Corp Code § 31101

There shall be exempted from the provisions of Chapter 2 (commencing with Section 31110) of this part the offer and sale of a franchise if the franchisor complies with each of the following minimum net worth, experience, disclosure, and notice filing requirements:

(a) Net worth. The franchisor and, when necessary, a corporation owning at least 80 percent of the franchisor (parent) meet one of the following net worth requirements, according to financial statements for the fiscal year just ended. The franchisor and the parent, when necessary, may rely upon the immediately preceding fiscal year's audited financial statement for 15 months from that fiscal year end date.

1. The franchisor has a net worth on a consolidated basis of not less than five million dollars ($5,000,000), according to its audited financial statement.
2. The franchisor has a net worth of not less than one million dollars ($1,000,000) and its parent has a net worth of five million dollars ($5,000,000), according to the audited financial statements of the franchisor and its parent, respectively.
3. The franchisor has a net worth of one million dollars ($1,000,000), according to its unaudited financial statement, and the parent has a net worth on a consolidated basis of not less than five million dollars ($5,000,000), according to its audited financial statement, and the parent absolutely and unconditionally guarantees to assume the duties and obligations of the franchisor under the franchise agreement should the franchisor become unable to perform its duties and obligations.

(b) Experience. The franchisor or a corporation owning at least 80 percent of the franchisor (parent) complies with one or more of the following conditions throughout the five-year period immediately preceding the offer and sale of the franchise, or complies with one of the following conditions during part of the period and one or more of the following conditions during the balance of the period:

1. The franchisor has had at least 25 franchisees conducting business which is the subject of the franchise.
2. The franchisor has conducted business which is the subject of the franchise.
3. The parent has had at least 25 franchisees conducting business which is the subject of the franchise.
4. The parent has conducted business which is the subject of the franchise.

(c) Disclosure.

1. Except as provided in subparagraph (2), the franchisor discloses in writing to each prospective franchisee, at least 10 business days prior to the execution by the prospective franchisee of any binding franchise or other agreement, or at least 10 business days prior to the receipt of any consideration, the following information:
(A) The name of the franchisor, the name under which the
franchisor is doing or intends to do business, and the name of any
parent or affiliated company that will engage in business
transactions with franchisees.
(B) The franchisor's principal business address and the name and
address of its agent in the State of California authorized to receive
service of process.
(C) The business form of the franchisor, whether corporate,
partnership, or otherwise.
(D) The business experience of the franchisor, including the length
of time the franchisor (i) has conducted a business of the type to
be operated by the franchisees, (ii) has granted franchises for
such business, and (iii) has granted franchises in other lines of
business.
(E) A copy of the typical franchise contract or agreement proposed
for use or in use in this state.
(F) A statement of the franchise fee charged, the proposed
application of the proceeds of such fee by the franchisor, and the
formula by which the amount of the fee is determined if the fee is
not the same in all cases.
(G) A statement describing any payments or fees other than
franchise fees that the franchisee or subfranchisor is required to
pay to the franchisor, including royalties and payments or fees
which the franchisor collects in whole or in part on behalf of a third
party or parties.
(H) A statement of the conditions under which the franchise
agreement may be terminated or renewal refused, or repurchased
at the option of the franchisor.
(I) A statement as to whether, by the terms of the franchise
agreement or by other device or practice, the franchisee or
subfranchisor is required to purchase from the franchisor or his or
her designee services, supplies, products, fixtures, or other goods
relating to the establishment or operation of the franchise
business, together with a description thereof.
(J) A statement as to whether, by the terms of the franchise
agreement or other device or practice, the franchisee is limited in
the goods or services offered by him or her to his or her
customers.
(K) A statement of the terms and conditions of any financing
arrangements when offered directly or indirectly by the franchisor
or his or her agent or affiliate.
(L) A statement of any past or present practice or of any intent of
the franchisor to sell, assign, or discount to a third party any note,
contract, or other obligation of the franchisee or subfranchisor in
whole or in part.
(M) If any statement of estimated or projected franchisee earnings
is used, a statement of such estimation or projection and the data
upon which it is based.
(N) A statement as to whether franchisees or subfranchisors
receive an exclusive area or territory.
(O) A copy of the financial statement or statements required by subdivision (a).

(P) A copy of the unconditional guaranty, if applicable, required by paragraph (3) of subdivision (a).

(2) In the case of a material modification of an existing franchise, the franchisor discloses in writing to each franchisee information concerning the specific sections of the franchise agreement proposed to be modified and such additional information as may be required by rule or order of the commissioner. Any agreement by such franchisee to such material modifications shall not be binding upon the franchisee if the franchisee, within 10 business days after the receipt of such writing identifying the material modification, notifies the franchisor in writing that the agreement to such modification is rescinded. A writing identifying the material modification is received when delivered to the franchisee. A written notice by the franchisee rescinding an agreement to a material modification is effective when delivered to the franchisor or when deposited in the mail, postage prepaid, and addressed to the franchisor in accordance with any notice provisions in the franchise agreement, or when delivered or mailed to the person designated in the franchise agreement for the receipt of notices on behalf of the franchisor.

(d) Notice Filing. The franchisor has filed with the commissioner a notice of exemption and paid the fee required by subdivision (f) of Section 31500 prior to an offer or sale of a franchise in this state during any calendar year in which one or more franchises are sold, excluding any material modification.

Hawaii:

TRANSFER EXEMPTION

Haw. Rev. Stat. § 482E-4

(a) Sections 482E-3, 482E-5(a) and 482E-5(c) shall not apply to:

(7) The offer or sale of a franchise by a franchisee for the franchisee's own account, or the issuance of a new franchise agreement pursuant to a sale by a franchisee for the franchisee's own account, if the sale is an isolated sale and not part of a plan of distribution of franchises.

RENEWAL EXEMPTION

Haw. Rev. Stat. § 482E-4

(a) Sections 482E-3, 482E-5(a) and 482E-5(c) shall not apply to:

(5) The extension or renewal of an existing franchise or the exchange or substitution of a modified or amended franchise agreement or the transfer of the location of a franchise where there is no interruption in the operation of the franchise business of the franchisee, and no material change in the franchise relationship.

(6) The offer or sale of an additional franchise to an existing franchisee of the same franchisor.
**Illinois:**

TRANSFER EXEMPTION

815 Ill. Comp. Stat. 705/7

Sec. 7. Sale by franchisee and extension or renewal of existing franchise. There shall be exempted from the provisions of Sections 5, 10, 11, 13 and 15 of this Act the offer or sale of a franchise by a franchisee for its own account if the sale is not effected by or through a franchisor. A sale is not effected by or through a franchisor merely because a franchisor has a right to approve or disapprove a different franchisee or requires payment of a reasonable transfer fee or requires the new franchisee to execute a franchise agreement on terms not materially different from the existing franchise agreement.

RENEWAL EXEMPTION

815 Ill. Comp. Stat. 705/7

Sec. 7. There shall be exempted from the provisions of Sections 5, 10, 11, 13 and 15 of this Act the extension or renewal of an existing franchise or the exchange or substitution of a modified or amended franchise agreement where there is no interruption in the operation of the franchise business by the franchisee.

**Indiana:**

TRANSFER EXEMPTION

Ind. Code § 23-2-2.5-4

*Exempt franchisees* Sec. 4. The offer of sale of a franchise by a franchisee who is not an affiliate of the franchisor for his own account is exempt from section 9 if the offer or sale is not effected by or through a franchisor. A sale is not effected by or through a franchisor if a franchisor is entitled to approve or disapprove a different franchisee.

RENEWAL EXEMPTION

Ind. Code § 23-2-2.5-1

*Definitions* (g) "Offer" or "offer to sell" does not include the renewal or extension of an existing franchise where there is no interruption in the operation of the franchised business by the franchisee.
Maryland:

TRANSFER EXEMPTION


(c) Sale for franchisee’s or subfranchisor’s own account. –

(1) The registration requirement of this section does not apply to the offer to sell or sale of a franchise by a franchisee for the franchisee’s own account, or the offer to sell or sale of the entire area franchise owned by a subfranchisor for the subfranchisor’s own account.

(2) A sale is not effected by or through a franchisor merely because a franchisor has a right to approve or disapprove a different franchisee.

RENEWAL EXEMPTION


(c) Existing franchise. This subtitle does not apply to the renewal or extension of an existing franchise if there is no interruption in the operation of the franchised business.


(b) Exemptions. The registration requirement of this section does not apply to:

(2) an offer to sell or sale of a franchise that is substantially similar to a franchise already owned by the offeree or buyer.

Michigan:

TRANSFER EXEMPTION

Mich. Comp. Laws § 445.1506

Sec. 6.

(1) Except as provided in subsection (2), the offer and sale of a franchise is exempt from sections 7a and 8 if any of the following circumstances apply:

(f) The offer or sale of a franchise by a franchisee for the franchisee's own account, if all of the following conditions are met:

   (i) The sale is an isolated sale, and not part of a plan of distribution of franchises.
   (ii) The franchisee provides to the prospective purchaser full access to the books and records related to the franchise in actual or constructive possession of the franchisee.

RENEWAL EXEMPTION

Sec. 3.

(3) “Offer” or “offer to sell” includes an attempt to offer to dispose of or solicitation of an offer to buy, a franchise or interest in a franchise for value. The terms defined in this act do not include the renewal or extension of an existing franchise where there is no interruption in the operation of the franchised business by the franchisee.

Mich. Comp. Laws § 445.1506

Sec. 6.

(1) Except as provided in subsection (2), the offer and sale of a franchise is exempt from sections 7a and 8 if any of the following circumstances apply:

(e) There is an extension or renewal of an existing franchise or the exchange or substitution of a modified or amended franchise agreement where there is no interruption in the operation of the franchise business of the franchisee, and no material change in the franchise relationship.

Minnesota:

TRANSFER EXEMPTION

Minn. Stat. § 80C.03

The registration requirement imposed by section 80C.02 shall not apply to the following provided that the method of offer or sale is not used for the purpose of evading sections 80C.01 to 80C.22:

(a) the offer or sale of a franchise owned by that franchisee, or the offer or sale of the entire area franchise owned by the subfranchisor making the offer or sale if the sale is not effected by or through a franchisor; provided, however, that no person shall make more than one sale during any period of 12 consecutive months of a franchise or area franchise granted by a single franchisor. A sale is not effected by or through a franchisor merely because a franchisor has a right to approve or disapprove a different franchisee.

[RENEWAL NOT EXEMPTED]

Minn. R. 2860.0100

Subp. 9. Sale; sell; offer; offer to sell. "Sale," "sell," "offer," and "offer to sell" shall include the renewal or extension of an existing franchise for value for the purposes of Minnesota Statutes 1973 Supplement, sections 80C.10 to 80C.22, and parts 2860.4300 to 2860.8300.

New York:
TRANSFER EXEMPTION

N.Y. Laws § 684

There shall be exempted from the registration provisions of section six hundred eighty-three of this article the offer and sale of a franchise if:

5. The offer or sale of a franchise by a franchisee for his own account or the offer and sale of an entire area franchise owned by a subfranchisor for his own account is exempted from the registration provisions of section six hundred eighty-three of this article if:
   (a) The sale is an isolated sale and not part of a plan of distribution of franchises; and
   (b) The sale is not effected by or through a franchisor; and
   (c) The franchisee furnishes to the prospective purchaser, at least one week prior to the execution of any binding contract or purchase agreement, or at least one week prior to the receipt of any consideration, whichever occurs first, a copy of the offering prospectus of the franchisor (including amendments, if any) currently registered with the department of law.

A sale is not effected by or through a franchisor merely because a franchisor has a right to approve or disapprove a different franchisee.

RENEWAL EXEMPTION

N.Y. Laws § 681

"Offer" or "offer to sell" includes any attempt to offer to dispose of, or solicitation of an offer to buy, a franchise or interest in a franchise for value. The terms "offer" and "offer to sell" do not include the renewal or extension of an existing franchise where there is no interruption in the operation of the franchised business by the franchisee.

North Dakota:

TRANSFER EXEMPTION

N.D. Cent. Code § 51-19-04

2. The offer or sale of a franchise by a franchisee for the franchisee's own account or the offer or sale of the entire area franchise owned by a subfranchisor for the subfranchisor's own account is exempted from the provisions of section 51-19-03 if the sale is not effected by or through a franchisor; provided, however, that no subfranchisor may offer or sell a franchise under this subsection without first obtaining the written approval of the commissioner. The commissioner may require that the subfranchisor and the franchisor provide the prospective purchaser and the commissioner with such information and disclosures as the commissioner deems necessary or appropriate to carry out the purposes of this chapter. A sale is not effected by or through a franchisor merely because a franchisor has a right to approve or disapprove a different franchisee.

RENEWAL EXEMPTION
N.D. Cent. Code § 51-19-02

14. a.

(1) "Sale" or "sell" includes every contract or agreement of sale of, contract to sell, or disposition of a franchise or interest in a franchise for value.

(2) "Offer" or "offer to sell" includes every attempt to offer to dispose of or solicitation of an offer to buy a franchise or interest in a franchise for value. The terms defined in this subsection do not include the renewal or extension of an existing franchise where there is no interruption of the operation of the franchised business by the franchisee.

MATERIAL MODIFICATION DISCLOSURE REQUIREMENT

N.D. Cent. Code § 51-19-04

1. There must be exempted from the provisions of section 51-19-03 the offer to sell, the offer to purchase, the sale, and the purchase of a franchise if the franchisor:

a. Has a net worth on a consolidated basis according to its most recent audited financial statement of not less than ten million dollars; or the franchisor has a net worth according to its most recent financial statement of not less than one million dollars and is at least eighty percent owned by a corporation which has a net worth on a consolidated basis according to its most recent audited financial statement of not less than ten million dollars;

b. Has had at least twenty-five franchisees conducting business at all times during the five-year period immediately preceding the offer or sale; or has conducted business which is the subject of the franchise continuously for not less than five years preceding the offer or sale; or if any corporation which owns at least eighty percent of the franchisor has had at least twenty-five franchisees conducting business at all times during the five-year period immediately preceding the offer or sale; or such corporation has conducted business which is the subject of the franchise continuously for not less than five years preceding the offer or sale;

c. Except as provided in subdivision d, discloses in writing to each prospective franchisee, at least seven days prior to the execution by the prospective franchisee of any binding franchise or other agreement, or at least seven days prior to the receipt of any consideration, whichever occurs first, the following information:

(1) The name of the franchisor, the name under which the franchisor is doing or intends to do business, and the name of any parent or affiliated company that will engage in business transactions with franchisees.

(2) The franchisor's principal business address and the name and address of its agent in this state authorized to receive service of process.

(3) The business form of the franchisor, whether corporate, limited liability company, partnership, or otherwise.

(4) The business experience of the franchisor, including the length of time the franchisor has conducted a business of the type to be operated by the
franchisee, has granted franchises for such business, and has granted franchises in other lines of business.

(5) A copy of the typical franchise contract or agreement proposed for use or in use in this state.

(6) A statement of the franchise fee charged, the proposed application of the proceeds of such fee by the franchisor, and the formula by which the amount of the fee is determined if the fee is not the same in all cases.

(7) A statement describing any payments or fees other than franchise fees that the franchisee or subfranchisor is required to pay to the franchisor, including royalties and payments or fees that the franchisor collects in whole or in part on behalf of a third party or parties.

(8) A statement of the conditions under which the franchise agreement may be terminated or renewal refused, or repurchased at the option of the franchisor.

(9) A statement as to whether, by the terms of the franchise agreement or by other device or practice, the franchisee or subfranchisor is required to purchase from the franchisor or the franchisor's designee services, supplies, products, fixtures, or other goods relating to the establishment or operation of the franchise business, together with a description thereof.

(10) A statement as to whether, by the terms of the franchise agreement or other device or practice, the franchisee is limited in the goods or services offered by the franchisee to customers.

(11) A statement of the terms and conditions of any financing arrangements when offered directly or indirectly by the franchisor or the franchisor's agent or affiliate.

(12) A statement of any past or present practice of any intent of the franchisor to sell, assign, or discount to a third party any note, contract, or other obligation of the franchisee or subfranchisor in whole or in part.

(13) If any statement of estimated or projected franchisee earnings is used, a statement of such estimation or projection and the data upon which it is based.

(14) A statement as to whether franchisees or subfranchisors receive an exclusive area or territory;

d. In the case of a material modification of an existing franchise, discloses in writing to each franchisee information concerning the specific sections of the franchise agreement proposed to be modified and such additional information as may be required by rule or order of the commissioner. Any agreement by such franchisee to such material modifications is not binding upon the franchisee if the franchisee, within ten business days after the receipt of such writing identifying the material modification, notifies the franchisor in writing that the agreement to such modification is rescinded. A writing identifying the material modification is received when delivered to the franchisee. A written notice by the franchisee rescinding an agreement to a material modification is effective when delivered to the franchisor or when deposited in the mail, postage prepaid, and addressed to the franchisor in accordance with any notice provisions in the franchise agreement, or when delivered or mailed to the person designated in the franchise agreement for the receipt of notices on behalf of the franchisor; and

e. Has filed with the commissioner a notice of exemption and paid the fee required by section 51-19-17 prior to the offer or sale of a franchise in this state.
Any notice of exemption and the renewal must contain the following:

(1) The name of the franchisor, the name under which the franchisor is doing or intends to do business, and the name of any parent or affiliated company that will engage in business transactions with franchisees.
(2) The franchisor's principal business address and the name and address of its agent in this state authorized to receive service of process.
(3) The business form of the franchisor, whether corporate, limited liability company, partnership, or otherwise.
(4) A copy of the typical franchise contract or agreement proposed for use or in use in this state.
(5) Information sufficient to establish that the franchisor satisfies the exemption conditions contained in subdivisions a and b.

Any notice of exemption remains in effect for a period of one year from the date the notice is received by the commissioner.

Oregon:

TRANSFER EXEMPTION

Or. Admin. R. 441-325-0040

The offer or sale of a franchise by a franchisee for his own account or the offer or sale of the entire area franchise owned by a subfranchisor for his own account, is exempted from the provisions of ORS chapter 650 if sale is not effected by or through a franchisor, and the franchisor does not participate or aid in the sale thereof. A sale is not effected by or through a franchisor merely because a franchisor has a right to approve or disapprove a different franchisee.

RENEWAL EXEMPTION

Or. Rev. Stat. § 650.005

8. "Sale" or "sell" includes every contract or agreement of sale of, contract to sell, or disposition of a franchise or interest in a franchise for value, but does not include the renewal or extension of an existing franchise without any material change in the terms thereof if there is no interruption in the operation of the franchised business by the franchisee.

Or. Admin. R. 441-325-0030

The sale of or offer to sell a franchise is exempt from OAR 441-325-0020 if any of the following circumstances apply:

(2) The sale or offer to sell is a renewal, extension, amendment or modification of an existing franchise agreement if there is:
   (a) No interruption in the operation of the franchise relationship;
   (b) No material change adverse to the franchisee in the franchise relationship; and
   (c) No material change adverse to the franchisee in the disclosure information previously furnished to the franchisee.
Rhode Island:

TRANSFER EXEMPTION


Exemption from registration. – The following transactions are exempt from the provisions of § 19-28.1-5:

(2) The offer or sale of a franchise by a franchisee who is not an affiliate of the franchisor for the franchisee's own account if the franchisee's entire franchise is sold and the sale is not effected by or through the franchisor. A sale is not effected by or through a franchisor merely because a franchisee signs agreements with terms which do not materially differ from the agreements with the existing franchisee or because a franchisor has a right to approve or disapprove the sale or requires payment of a reasonable transfer fee. This exemption applies to the offer or sale of a master franchise if the entire master franchise is sold.

RENEWAL EXEMPTION


Exemption from registration. – The following transactions are exempt from the provisions of § 19-28.1-5:

(6) The offer or sale of a franchise involving a renewal, extension, modification or amendment of an existing franchise agreement if there is no interruption in the operation of the franchised business and there is no material change in the franchise relationship. For purposes of this subdivision, an interruption in the operation of the franchised business solely for the purpose of renovating or relocating that business is not a material change in the franchise relationship or an interruption in the operation of the franchise business.

South Dakota:

TRANSFER EXEMPTION

S.D. Codified Laws § 37-5B-1

(16) "Offer," any attempt to dispose of, and any solicitation of an offer to buy, a franchise or interest in a franchise for value by purchase, license, or otherwise. The term does not include an offer to extend or renew an existing franchise if there is no interruption in the franchisee's operation of the business, unless the terms and conditions of the extension or renewal differ materially from the original agreement. The term also does not include an offer of a franchise by an existing franchisee if the franchisor has had no significant involvement with the prospective franchisee. A franchisor's prior dealing with a prospective franchisee alone is not deemed to be significant involvement.

RENEWAL EXEMPTION
S.D. Codified Laws § 37-5B-1

(28) "Sale of a franchise," any agreement whereby a person obtains a franchise from a franchise seller for value by purchase, license, or otherwise. The term does not include extending or renewing an existing franchise agreement if there has been no interruption in the franchisee's operation of the business, unless the new agreement contains terms and conditions that differ materially from the original agreement. The term also does not include the transfer of a franchise by an existing franchisee if the franchisor has had no significant involvement with the prospective transferee. A franchisor's approval or disapproval of a transfer alone is not deemed to be significant involvement.

Virginia:

TRANSFER EXEMPTION

21 Va. Admin. Code § 5-110-75

Any offer or sale of a franchise in a transaction that meets the requirements of this section is exempt from the registration requirement of § 13.1-560 of the Act.

1. Sale or transfer by existing franchisee. The sale or transfer of a franchise by a franchisee who is not an affiliate of the franchisor for the franchisee's own account is exempt if:

   a. The franchisee’s entire franchise is sold or transferred and the sale or transfer is not effected by or through the franchisor.
   b. The sale or transfer is not effected by or through a franchisor merely because a franchisor has a right to approve or disapprove the sale or transfer or requires payment of a reasonable transfer fee.

RENEWAL EXEMPTION

21 Va. Admin. Code § 5-110-75

Any offer or sale of a franchise in a transaction that meets the requirements of this section is exempt from the registration requirement of § 13.1-560 of the Act.

2. Renewal or extension of existing franchise. The offer or sale of a franchise involving a renewal or extension of an existing franchise where there is no interruption in the operation of the franchised business, and there is no material change in the franchise relationship, is exempt. For purposes of this subdivision, an interruption in the franchised business solely for the purpose of renovating or relocating that business is not a material change in the franchise relationship or an interruption in the operation of the franchised business.

Washington:

TRANSFER EXEMPTION

Wash. Rev. Code § 19.100.030
The registration requirements of this chapter shall not apply to:

(1) The offer or sale or transfer of a franchise by a franchisee who is not an affiliate of the franchisor for the franchisee's own account if the franchisee's entire franchise is sold and the sale is not effected by or through the franchisor. A sale is not effected by or through a franchisor merely because a franchisor has a right to approve or disapprove the sale or requires payment of a reasonable transfer fee. Such right to approve or disapprove the sale shall be exercised in a reasonable manner.

RENEWAL EXEMPTION

Wash. Rev. Code § 19.100.030

The registration requirements of this chapter shall not apply to:

(6) The offer or sale of an additional franchise to an existing franchisee of the franchisor for the franchisee's own account that is substantially the same as the franchise that the franchisee has operated for at least two years at the time of the offer or sale, provided the prior sale to the franchisee was pursuant to a franchise offering that was registered in the state of Washington.

Wisconsin:

TRANSFER EXEMPTION

Wis. Stat. § 553.23

Private franchisee and subfranchisor sales exempted. The sale of a franchise by a franchisee for the franchisee's own account and the sale of the entire area franchise owned by a subfranchisor for the subfranchisor's own account are exempted from s. 553.21 if the sale is not effected by or through a franchisor. A sale is not effected by or through a franchisor merely because a franchisor has a right to approve or disapprove a different franchisee or because a franchisor imposes or has the right to impose a fee or charge to reimburse the franchisor for reasonable and actual expenses incurred in connection with the sale.

RENEWAL EXEMPTION

Wis. Stat. § 553.03

(11) "Sale" or "sell" includes every contract or agreement of sale of, contract to sell, or disposition of, a franchise or interest in a franchise for value. This term does not include the renewal or extension of an existing franchise where there is no interruption in the operation of the franchised business by the franchisee.
Jamila Braswell Granger

Jamila Granger is Senior Counsel for Krispy Kreme Doughnuts, Inc. Ms. Granger focuses on all aspects of domestic and international franchise transactions, intellectual property, international trade and supply chain issues. She is a member of the ABA Forum on Franchising (and currently a member of the Publications Committee), the State Bar of Virginia and the District of Columbia Bar. Ms. Granger is a 1998 graduate of the University of Virginia School of Law where she served as an Editorial Board Member of the Virginia Journal of Social Policy & the Law and the Virginia Journal of Law & Technology, and a 1995 graduate of Harvard University in Cambridge, Massachusetts.
Benjamin A. Levin

Benjamin A. Levin is managing partner of the firm, Hyland Levin LLP located in Marlton, New Jersey. His practice focuses on both business and franchise law. He serves as outside general counsel to some of the Mid-Atlantic region’s most vibrant companies, including food and product manufacturers, suppliers of technology and other services and licensors of intellectual property. Ben’s business practice includes counseling and transactional work with all forms of business entities, protection of intellectual property and licensing and distribution matters.

Ben has concentrated his practice in franchise and distribution law matters for over 30 years. His work includes structuring franchise and other distribution relationships, compliance with franchise laws and regulations, preparation of FDDs, the buying and selling of franchise systems and franchisor/franchisee problem solving.

He is included in the International Who’s Who of Franchise Lawyers for 2004 through 2010 and is listed in the Best Lawyers in America. He has been selected by Franchise Times as one of the top franchise lawyers in the United States each year for the past several years and has been named a Super Lawyer in New Jersey Monthly for 2005 through 2010.

Ben was co-chair of the American Bar Association’s 26th Annual Forum on Franchising in October 2003 and served a three-year term on the Governing Committee of the ABA’s Forum on Franchising. He is the founding chairperson of the Franchise Law Committee of the New Jersey State Bar Association.
Charles S. Modell

Mr. Modell is the founder and chairman of the franchise practice group of Larkin Hoffman Daly & Lindgren Ltd., Minneapolis, Minnesota. He has been an active and highly respected member of the franchise legal community for three decades. Mr. Modell’s practice consists primarily of representing franchisors concerning the business aspects of franchising, including the structuring of the franchise relationship; drafting franchise agreements and disclosure documents; compliance with state and federal franchise laws and regulations; negotiations with franchisees; terminations and non-renewals; and the purchase and sale of franchise companies.

Mr. Modell is a former member of the Governing Committee of the American Bar Association’s Forum on Franchising, and served as the Forum’s Franchise Officer for over six years. He has also been active in the IFA for three decades, having served on the Legal/Legislative Committee, the Franchise Relations Committee, and the Board of the Council of Franchise Suppliers. Mr. Modell is a certified commercial arbitrator for the American Arbitration Association, and has testified as an expert witness on franchise matters in state and federal court and in arbitration. He is listed in Best Lawyers in America, Super Lawyers, the International Who’s Who of Franchise Lawyers, and Chambers USA.

Mr. Modell’s clients rely on him as much for his business and financial acumen as for his knowledge of the law, and look to him for business advice as they make decisions in their own businesses. He was the second practicing attorney to receive the designation of Certified Franchise Executive from the International Franchise Association. He served on the Larkin Hoffman Board of Directors for more than ten years, and was previously the firm’s Chief Financial Officer. He received a Bachelor of Science degree from the University of Florida in 1974 and graduated with high honors from the University of Florida College of Law in 1977, after serving as Managing Editor of the Florida Law Review.