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IS THAT A FAIR DEAL? BEST PRACTICES FOR NEGOTIATION OF THE FRANCHISE AGREEMENT

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IS THAT A FAIR DEAL? BEST PRACTICES
FOR NEGOTIATION OF THE FRANCHISE AGREEMENT

I. INTRODUCTION

The question, "Is that a fair deal?," is best answered with an open-ended response, "It depends." Who determines what is fair: is it the franchisor, the franchisee, the judge, the jury, the arbitrators or someone else? One person's fair may not be another's. The authors do not intend to define "fair," nor present what could be considered a "fair" agreement. Rather, the authors aim to provide best practices to use in the negotiation of a franchise agreement, by way of summarizing the different factors that can lead a party to negotiate, presenting an analysis of various provisions in the franchise agreement commonly subject to negotiation, detailing common rationales and reasons behind the franchisor and franchisee positions, and outlining practical tips for representing clients' interests in the process. An understanding and appreciation of all of these aspects best enables the attorney to meet the client's desire to reach what he or she considers a fair deal.

With some exceptions, gone are the days when a franchisor can approach qualified prospects with a "take it or leave it" attitude. Negotiation is common and can result in a franchise agreement that is better suited to the individual franchise relationship than the form franchise contract contained in the Franchise Disclosure Document ("FDD"). No matter how extensive the negotiations might be, however, keep in mind that, based on the nature of the franchise relationship, the agreement will still be in the franchisor's favor when considering the relative obligations of the parties, the remedies available to them, and the need for franchisor controls to protect the system.

Because of this imbalance, negotiating a franchise agreement is very different than negotiating a typical business contract between two parties with comparable leverage. Parity is unrealistic in franchise agreements. Notwithstanding the foregoing, negotiation is a process, and can benefit both parties without substantial changes to the franchise agreement. The very exercise of requesting changes to the agreement and having a robust discussion about the parties' interests and concerns brings greater clarity to and understanding of the parties' expectations. Franchisee counsel may find that, in the course of dissecting the franchise agreement and consulting with the client about the meaning of the franchise agreement's written terms, the written agreement is contrary to the prospective franchisee's expectations and understanding of the deal, or of franchising generally. Franchisee counsel will have done a service by advising the franchisee as to the true and complete nature of the franchise relationship in light of the written terms of the agreement. Franchisors and their counsel, by having a willingness to listen to a franchisee's business objectives and concerns related to the franchise agreement, are in a better position to understand the prospective franchisee and determine whether or not there is a good fit with the franchised business and the system.

This paper provides certain negotiation strategies from both the franchisee and franchisor perspectives, taking into account each party's respective bargaining position. While an attorney must come to a negotiation prepared with a keen sense of franchise law generally, the focus of this paper is not to give a detailed history of the applicable case law behind franchise agreement provisions. Instead, the goal is to give attorneys a better understanding of what brings parties to the negotiating table, the legal rationales and business concerns of each, and the overall relationship dynamics, so that attorneys can be better equipped to enter into a fruitful negotiation.

II. WHY NEGOTIATE?

A franchisor and its counsel spend considerable time and money preparing an FDD, including the franchise agreement and related documents to offer prospective franchisees. These agreements are drafted and vetted to develop and maintain a successful brand and system. The importance of consistency across the system should not be discounted – and this consistency benefits both sides. Of course, this reasoning begs the question: Why negotiate at all? A number of considerations and factors determine a franchisor's willingness to change the terms of its standard franchise agreement, and how hard a prospective franchisee can push for such changes.

A. State Relationship Laws

Regardless of how much or how little a franchisor and a franchisee may want to negotiate their franchise agreement, many states restrict the parties' ability to do so in an effort to protect the franchisee. In addition to the states regulating the offer and sale of franchises, a number of states regulate the franchise relationship – limiting the franchisor's ability to terminate, not renew, disapprove transfers, or, in some instances, negotiate other changes to the franchise agreement.[1] Franchisors and franchisees should carefully consider these statutory requirements when negotiating provisions like termination and renewal, and franchisors should be mindful of these laws and regulations when determining choice of law and venue. Attached, as Exhibit A, is a quick reference guide to certain of the state relationship laws.

B. Start-Up Franchisors

Many provisions that are not negotiable in the franchise agreement of an established system may be subject to negotiation for a start-up franchisor. A business at the beginning stage of franchising may be willing to make more concessions in an effort to close its first deals. Franchisor counsel should be mindful of their client's propensity to "fall in love" with a deal or with a particular prospect. Often business owners with a successful concept are blinded by dollar signs when a potential franchisee is the first to suggest the concept of franchising. Start-up franchisors should be wary of giving away the farm in exchange for some up-front fees. Franchisors must keep in mind that these first franchisees will be a part of what hopefully will become a larger system over time. Once franchisors concede certain terms, however, it can be much more difficult to gain that leverage back and institute more protective terms going forward. For instance, negotiating lower fees with certain franchisees creates disclosure obligations in the FDD – putting all future prospects on notice of what may be negotiable.

C. Large Systems

An established franchise system usually has a proven concept that has achieved a certain level of success, and that success is contingent upon on the franchisor's ability to

[1] Numerous states regulate some aspect of the franchise/distribution relationship, particularly with respect to termination and non-renewal. In addition to states that restrict a franchisor's ability to terminate or not to renew, Arkansas, Connecticut, Hawaii, Illinois, Indiana, Minnesota Washington and Wisconsin all prohibit a franchisor from discriminating against its franchisees. *See* ARK. CODE ANN. §§ 4-72-202 and 4-27-204; CONN. GEN. STAT. ANN. §§ 42-133e to 42-133h; HAW. REV. STAT. § 482E-6 ; IL ST CH 815 § 705/18; IND. CODE ANN. § 23-2-2.7-2; MINN. STAT. ANN. § 80C.14; WASH. REV. CODE ANN. § 19.100.180; WIS. STAT. §§ 135.02 and 135.03. For a complete list of state statutes regarding franchise relationship laws, *see State Laws; Relationship; Termination*, Bus. Franchise Guide (CCH) ¶ 5001.

maintain consistency throughout the system. Additionally, in contrast to an early-stage franchisor, a larger system will often have more leverage than its prospective franchisees (although this may not be the case with respect to a master franchisee or area developer in some instances, as discussed below). A prospective franchisee is in much more of a "take it or leave it" position with a large, established system, and often times must be willing to forego the ability to negotiate in exchange for the right to join a successful brand and proven concept.

D. <u>Multi-Unit Franchisees and Area Developers</u>

As franchisees become more sophisticated over time, the leverage may shift, even if only slightly. Successful multi-unit operators are more likely to successfully negotiate changes to significant terms in franchise agreements, like royalty rates, minimum royalties, and territorial protections. Similarly, depending on a franchisor's desire to enter a certain market, area developers with a presence and ability to quickly ramp up in new areas may gain certain concessions to which franchisors might otherwise not concede.

E. <u>State of the Economy</u>

As the economy ebbs and flows, so too does the pipeline for development. A policy of no negotiation may change once the environment becomes more challenging. Franchisors may be willing to negotiate previously standard terms in an effort to close a deal and keep the system growing. Franchisees can take advantage of the situation by asking for revisions that are more typically included in heavily negotiated license agreements, where the leverage is more balanced. The same principles hold true with respect to renewal agreements. Given the fluctuating and uncertain state of the economy, existing franchisees are more likely to try and negotiate additional terms that have previously been considered "untouchable" by franchisors. This seems to be especially true with respect to area developers and their development schedules. Franchisors appear to be much more willing to negotiate "work out" arrangements with area developers on prior development schedules that reflected a different reality than operators face in today's economy.

F. <u>International Expansion</u>

International franchise agreements are more commonly subject to negotiation. Rarely, if ever, is a franchisor able to adhere to a "take it or leave it" approach with international prospects. Even franchisors that have such an approach to domestic development are faced with a negotiation process that requires building consensus among various parties in the international context. Although a detailed analysis of the art of international negotiation is beyond the scope of this paper, it is important to emphasize that parties to an international franchise agreement need to consider a number of factors unique to the international setting, when negotiating it. The experience and positional power of the prospective franchisee, the local market, applicable laws and regulations, legal nuances, and cultural differences all add interesting and challenging dimensions to international contract negotiations.

Franchisors taking a hard line on every issue or having a strongly assertive approach may be part of the normal practice of domestic franchising, but, on an international stage, this may be counter-productive. Counsel may find that they need not only to justify their legal position, but also to explain clauses considered relatively standard in the United States.[2]

[2] Stephen Giles, Lou H. Jones & Larry Weinberg, *Negotiating and Documenting Complex International Franchise Agreements*, A.B.A. 29th Annual Forum on Franchising, Tab 21, 4 (2006).

Prospective franchisees in international deals are often large and sophisticated, sometimes more so than the franchisor.

G. <u>Negotiated Changes and Material Modifications in California</u>

Franchisors and franchisees should both be aware of the additional (and somewhat confusing) requirements in California when negotiating a franchise agreement. The California Franchise Investment Law ("CFIL") requires that only a disclosure document and franchise agreement that have been registered with the Department of Corporations can be offered and sold to a person protected by the law.[3] Absent an exemption, any negotiated changes to the franchise agreement would have to be registered with the state.

Unfortunately, California's statutory and regulatory exemption procedures regarding negotiated sales can confuse even the most experienced practitioners. The regulatory requirements for California's negotiated sales exemption are somewhat onerous and require a franchisor to amend its FDD and file notices with the Commissioner of Corporations.[4] Under the regulations, the offer and sale of a franchise on terms different than the terms in the registered FDD are exempt from the registration requirements if all of the following conditions are met:

(1) The initial offer is the offer most recently registered, renewed or amended in California.

(2) The prospective franchisee receives the Franchise Disclosure Document and all copies of all Notices of Negotiated Sales of Franchises filed with California within the last 12 months, if any.

(3) Before selling another franchise, the franchisor amends its Franchise Disclosure Document to provide that:

> "The terms of Items(s) _____ of this disclosure document have been negotiated with other franchisees. A copy of all Negotiated Sales Notices filed in California in the last 12 months is attached as Exhibit ____."

This disclosure should be made in the disclosure document Item that was negotiated or in an appendix to the document. This disclosure must be made if the negotiated sale occurred with 12 months of the offering being made. An amendment making only this disclosure is effective when filed.

(4) The Notice of Negotiated Sale of Franchise must be filed with the Commissioner within 15 business days after the negotiated sale is consummated.

(5) The franchisor certifies or declares in an appendix to its application for renewal that all notices have been filed with the Commissioner.[5]

Notwithstanding the regulatory exemption, in some instances franchisors may rely on California's less onerous statutory exemption. The statutory exemption provides that negotiated

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[3] *See* CAL. CORP. CODE § 31000 et seq.

[4] *See* CAL. CODE REGS. tit. 10, § 310.122.

[5] CAL. CODE REGS. tit. 10, § 310.122.

sales do not have to be registered with California so long as the initial offer is registered in California, the negotiated terms confer additional benefits on the prospect and the prospect receives all of the following in a separate written appendix to the disclosure document: (i) a summary description of each "material" negotiated term for a California franchise during the 12-month period ending in the calendar month immediately before which the negotiated offer or sale is made; (ii) a statement indicating that copies of the negotiated terms are available upon written request;[6] and (iii) the franchisor contact information to whom requests for a copy of the negotiated terms may be made. The franchisor must also certify or declare in an appendix to its application for renewal that it has complied with all of the requirements of this section, if this exemption is claimed.[7] For purposes of this provision, "material" negotiated terms are defined in this section to mean a term "that a reasonable franchisee would view. . . as important in negotiating the franchise. Additionally, the franchisor must maintain copies of all material negotiated terms for which this exemption is claimed for a period of five years from the effective date of the first agreement containing the relevant negotiated term."[8]

Although somewhat beyond the scope of this paper, Section 31125 of the California Corporations Code regarding material modifications to franchise agreements is similarly confusing, and practitioners should be aware of the state's requirements when negotiating a change to an existing franchise agreement.[9] The law basically requires the franchisor to provide disclosure to existing franchisees if the franchisor proposes to change any terms of their franchise agreements (which would have to be agreed to by both parties in any event). Franchisors must file a description of the modification with the state and provide a franchisee with a waiting period during which the franchisee can consider the proposed revision. Alternatively, there are various exemptions to the normal process, the most prominent of which exempts a voluntary offer which does not adversely impact the franchisee's rights and obligations. Franchisors should be mindful, however, that to qualify for the exemption, similar to the statutory exemption for negotiated sales, the modification must, on the whole, confer additional benefits to the franchisee – which may not be entirely clear given the dynamics of negotiations.[10]

The applicable CFIL statutes and regulations related to negotiated sales and material modifications are attached as <u>Exhibit B</u>.

Notwithstanding the foregoing exemptions for negotiated sales in California, anecdotal evidence indicates that these provisions actually make a franchisor less likely to negotiate in California. Given the inconsistency in the statute and regulations, many franchisors are uncomfortable making any changes to their form of agreement for fear of failing to comply with the statutory and regulatory requirements. Many practitioners in California have suggested that California revise its laws related to negotiated sales in an attempt to make the process more straight forward for franchisors and encourage, rather than discourage, the parties' ability to negotiate. More often than not, negotiation tends to benefit the franchisee rather than the

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[6] The franchisor must provide a copy of the negotiated terms described above to the prospective franchisee within 5 business days following the request of the franchisee.

[7] Joe Fittante, Theresa Leets & Rebekah Prince, *Unique and Often Overlooked Provisions of State Franchise Registration and Disclosure Laws*, A.B.A. 33rd Annual Forum on Franchising, Tab 10, 13-14 (2010).

[8] CAL. CORP. CODE § 31109.1.

[9] CAL. CORP. CODE § 31125.

[10] Dennis Wieczorek, Patrick Maslyn, Timothy O'Brien & Anne Connelly, *Go to the Head of the Line: How to Get Registered, Amended, Renewed or Exempted*, A.B.A. 34th Annual Forum on Franchising, Tab 16, 17 (2011).

franchisor. On the other hand, a franchisee attorney's perspective may differ – and some argue that these requirements are simply being used as a "shield" by franchisors to state that it "can't" negotiate the franchise agreement in California. Many times a franchisor salesperson portrays it as a prohibition rather than obstacles that the franchisor can overcome. Also, there is value to the fact that franchisors don't necessarily like to disclose what terms have been negotiated. This is not only in respect to other California franchisees, but to other franchisees (or their attorneys) that may do their due diligence and look up the changes with the Department of Corporations and find what changes have been made and try to use that to their advantage.

III. WHAT TERMS ARE NEGOTIABLE?

A. Grant of Rights

The grant of rights section is the core of the franchise agreement, as it encompasses what the franchisee is authorized to do (and just as critical, what the franchisee is prohibited from doing), where the franchisee is authorized to conduct business, whether the rights are exclusive and what rights are reserved to the franchisor. The discussion surrounding this provision presents a classic example of competing franchisor and franchisee business objectives.[11] It also highlights that negotiation is not necessarily about getting the other party to change his or her mind; often it is about having a thoughtful and thorough analysis behind the language so that the franchisor can provide a solid rationale for the position. Further, this is a provision that is commonly discussed during the sales process, as well as the negotiation phase. It therefore illustrates the need for the sales team and legal team to have the same understanding and unified approach and message regarding the language in this section. Framing up the conversation correctly so that appropriate expectations are set for the franchisee is critical to easing the negotiation relating to this section. Typically, the grant of rights section begins with a relatively brief statement about the franchisee's temporary rights to use the trademarks and system (the business know how) during the term of the agreement.[12] Little, if any, negotiation occurs relative to the initial granting statement. The discussion generally occurs in the following subsections concerning the scope of territory, the limitation of franchisee rights and reservation of franchisor rights.

1. Exclusive or Non-Exclusive Territory

Few areas of the franchise agreement generate more conversation and concern in the development and negotiation phase than the description of the territory; specifically, the scope of the territory and whether it is exclusive. From the franchisor's business perspective, the territory provision exemplifies the difficult balance that it must strike when considering the attractiveness of the franchise offering versus the need to reserve control and flexibility over the expansion of the brand (whether that is through additional outlets or other channels of distribution).[13] As discussed in a previous section, more established brands may be able to offer less by way of territorial protection than those brands just beginning to franchise. The language

[11] Kerry Olson, Robin M. Spencer & Larry Weinberg, *The Annotated Franchise Agreement*, A.B.A. 33rd Annual Forum on Franchising, Tab 3, 12 (2010).

[12] ANDREW J. SHERMAN, FRANCHISING & LICENSING: TWO POWERFUL WAYS TO GROW YOUR BUSINESS IN ANY ECONOMY 107 (AMACOM 3d ed. 2004) (1991).

[13] Olson, Spencer & Weinberg, *supra* note 11, at 13.

of the franchise agreement must consider all of these objectives, and clearly state the franchisee's rights as they relate to territory, distribution, and expansion.[14]

Some franchisors give no territory exclusivity; the franchise rights are truly "site only," and the franchisee will be given no guaranty that the franchisor or its affiliates will not directly compete. If a franchisor has site only language (and a valid rationale for not granting territory protection), they should not change the language in the territory provision as a result of negotiation with a particular franchisee. Franchisors should take great care to draft a site only provision that is appropriately tailored to the business so that it is uniform (within reason) throughout the system. In this situation, there likely is little ability for a franchisee to negotiate, which is not to say that there should not be discussion between the franchisor and franchisee relating to the topic. To the contrary, a franchisor should have solid reasons for offering no territory exclusivity rights, and should be able to communicate the reasons early and thoroughly through the sales process and contract negotiation. If a franchisor has opted for not giving territory simply because the company has adopted what it feels is the norm in the industry rather than basing the decision on a thoughtful analysis, then the franchisor will have a much more difficult time during the discussions on this topic. A franchisee is spending considerable time, effort and expense to become part of the franchisor's system and understandably will have some apprehension over the site only language and the potential effect it may have on the business in the future. A solid rationale behind the decision to not provide a territory will help ease the franchisee's concern and smooth over a difficult discussion topic.

More advanced and mature franchisors are more likely to have site only language in their franchise agreements.[15] There are several arguments that a franchisor may employ for offering no territory protection. Sophisticated franchisors argue that because there is enough value attached to their trademarks that the consumer demand for the franchises themselves, and the franchise's products or services, is high.[16] Because the demand is high, locations in close proximity will likely still succeed.[17] Franchisors generally want to add a number of franchise outlets in densely populated areas and keep exclusive areas small so that they can dominate the market and outpace their competitors.[18] Similarly, the brand popularity, track record or history of well-established franchisors is often enough to incentivize demand by prospective franchisees, regardless of territorial exclusivity.

Although beyond the scope of this paper, some franchisors (particularly those that do not grant territorial exclusivity or protection in the franchise agreement) may supplement their system expansion standards with site clearance procedures, rights of first refusal, minimum performance quotas, impact policies, and so forth.[19] These typically are contained in policy statements, system memos and the like.[20] It is important for franchisors and their counsel to be well versed in the other policies and procedures of the company, as it likely will aid in the

[14] *Id.*

[15] Joseph J. Fittante, Jr. & Dennis E. Wieczorek, *Advanced Drafting*, A.B.A. 27th Annual Forum on Franchising, Tab 5, 3-5 (2004).

[16] Olson, Spencer & Weinberg, *supra* note 11, at 14.

[17] *Id.*

[18] JOE MATHEWS, DON DEBOLT & DEB PERCIVAL, STREET SMART FRANCHISING 189 (Entrepreneur Press ed., 2006).

[19] Olson, Spencer & Weinberg, *supra* note 11, at 16.

[20] *Id.*

negotiation of this difficult topic by giving comfort to a franchisee that the franchisor has tools in place to asses the impact of a new location on an existing franchisee.

Some franchise opportunities offer territory protection, typically by providing for an exclusive territory or a designated area in which the franchisor agrees not to operate or grant others the right to operate the same franchised business. Newer or smaller franchisors might have to provide for some level of territorial protection or exclusivity to attract franchisees.[21] Other franchisors may offer territory rights simply because it makes sense – regardless of the brand's size or maturity. It is very much a function of the type of business being operated. For instance, when provided in a retail restaurant franchise, territorial protection is most often afforded to a franchisee by providing a relatively straightforward, well-defined geographic area ("territory"), within which the franchisor agrees that it will not open, nor franchise others to open physical units.[22] However, in other situations, the territory needs to be considered and articulated in a different manner, such as exclusivity or territorial protection with respect to market segment, or by specifying that a franchisee will in fact only seek customers from within the territory. Franchisors should carefully consider the factors critical to the business, when determining criteria used for determining territory boundaries. The base, density and growth trends of the population may be important, as may be the composition of residential and business entities. Whatever the criteria, franchisors should be well versed in the rationale behind the factors attendant to a territory description. Remember too that franchisors will be required to provide details about the grant of territory in connection with their Item 12 disclosure. The same level of detail that goes into preparation of a franchisor's Item 12 should be a part of the discussion franchisors and their counsel have when discussing the issue of territorial rights.

If a franchise agreement contains territorial exclusivity, franchisees should have the ability to negotiate the provision – to ensure that the territory description accurately reflects details specific to the franchisee's market, location, competitive circumstances and the like. Just as the sections above discuss the need for franchisors to be well prepared on the topic, so too should franchisees be well versed in the appropriate business rationale behind requests for certain territory. Too often the negotiation on this topic can spiral into a conversation about a franchisee's mistrust of the franchisor. Negotiations steeped in that rationale will not be as successful for a franchisee as would be a discussion that focuses around the franchisee's particular knowledge of the area. Franchisees in areas new to the franchisor's expansion may have a particular leg up in the negotiations for territory, if handled correctly. Finally, although difficult, counsel should advise franchisees that it is important to balance the desire for a protected territory with the benefits of brand expansion.

The discussion above focuses on the rights granted to the franchisee, but it is important to also spell out the rights a franchisee is *not* granted. It may seem like overkill, but as previously stated, it is critical for the franchisor to be clear and detailed. When negotiating, the franchisor should consider all aspects (what the franchisee can and cannot do, and what the franchisor reserves the right to do) carefully, and insist on absolutely clarity in the agreement. The example below shows that the description of rights *not* granted to the franchisee may actually be more substantial than the language of rights granted.

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[21] SCOTT A. SHANE, FROM ICE CREAM TO THE INTERNET: USING FRANCHISING TO DRIVE THE GROWTH AND PROFITS OF YOUR COMPANY 133 *(*Pearson Education Inc. ed., 2005).

[22] Olson, Spencer & Weinberg, *supra* note 11, at 14.

The rights granted to the Franchisee are site specific, for use only at the location identified in this Agreement, and provide no rights of exclusivity to the Franchisee. Accordingly, the Franchisee's rights do not include (i) an exclusive area or protected territory within which the Franchisor or its affiliates agree not to issue competing franchises or operate competing businesses, (ii) any right to sell products and items identified by the Trademarks at any location other than the Authorized Location or through any other channels or methods of distribution, including the Internet (or any other existing or future form of electronic commerce) and pre-packaged retail sales, (iii) any right to sell products and items identified by the Trademarks to any person or entity for resale or further distribution, or (iv) any right to exclude, control or impose conditions on the location or development of future stores at any time.

2. Reservation of Rights

The reservation of rights provision is a critical compliment to the grant of rights section, and often the area that generates a good amount of discussion and negotiation. As much as a franchisee may not like to see extensive detail about what they are not permitted to do under the agreement, it causes even more anxiety to learn that the franchisor (or a third party) may have the rights to do those very same things. A franchisor should identify clearly the *franchisor's* territory, expansion and distribution rights, even in the context of a franchise agreement that does not grant an exclusive territory to the franchisee. Although it may cause consternation for the prospective franchisee and result in difficult discussions for those on the franchise development side of the business, it is critical to clearly "call out" the respective rights (or the limitation on such rights, as the case may be) related to territory.[23] The rights typically reserved by franchisors focus on the operation of competing businesses (whether by the franchisor or an affiliate, or another franchisee) and alternative methods of distribution (methods used to offer products or services to the franchise system's consumers that are different than the method used by the franchises of the system). Franchisors should have a well thought out strategy related to future business goals, and include language to cover the ability of the franchisor to best take advantage of opportunities. For instance, if the franchised business is conducive to an airport environment, the tenant opportunities are often limited and only available to certain entities, and therefore a franchisor may want to carve out airports and other special sites and reserve the right to operate the location as a corporate unit, or to franchise to a third party that is able to operate in the space. Just as important, a franchisor should incorporate language that allows for some flexibility in unknown areas. The issues surrounding alternate channels have become especially pronounced with the advent of the Internet, as online sales became a new channel of distribution that was not previously contemplated.[24] Similar to the grant of exclusivity, franchisors are well served by detailed and express provisions when faced with claims of encroachment by a franchisee.

In an attempt to avoid claims, the franchise agreement should speak to acceptable/unacceptable proximity. If this section is left ambiguous, it could lead to problems between the franchisor and franchisee about whether the franchisor breached the terms of the

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[23] *Id.*

[24] *See, e.g., Emporium Drug Mart, Inc. v. Drug Emporium, Inc.*, summarized in (CCH) Bus. Franchise Guide ¶ 11,966 (AAA Sept. 2, 2000) (arbitrators held franchisor's Internet sales encroached franchisee's contractual exclusivity); *see also Armstrong Bus. Services, Inc. v. H&R Block, Inc.*, No. WD 60348 (Circuit Ct. Jackson Co., MO Oct. 2003) (jury found franchisor's Internet program encroached franchisee's rights), discussed in Gary R. Duvall, *Using the Web More Effectively*, 24-WTR Franchise L.J. 173 (2005).

agreement by opening an outlet on the perimeter of the franchise's territory. It is not sufficient to reserve a "general right" above and beyond the agreement.[25] Parties also should be aware that particular state franchise statutes restrict franchisors' freedom with respect to locating new locations, in an effort to protect franchisees from encroachment, and those restrictions override contractual terms and reservations of rights.[26]

This is a provision of the contract that deserves a robust discussion between a franchisor and franchisee. The franchisor's position in the negotiation should be the result of an honest internal assessment and determination of the franchisor's business needs and intentions. Although it is advisable for franchisors to insist on language giving them the most flexibility to expand the business in the future, it is also the time to be realistic. If a franchised business could never realistically operate across the street from an existing location, is it critical to have a site only grant? Although franchisors should come prepared with detailed language and well established reasons for the specific reservations, they should learn about the franchisee's concerns and be open to making changes to accurately reflect the situation.

Some franchisors reserve certain rights, but make the notion more appealing by including terms that "involve" the franchisee should the franchisor ever exercise such rights. For instance, if a franchisor reserves the right to sell products into retail, the franchisor may agree to share revenues with the franchisee, or to contribute the funds to advertising and marketing initiatives for the system. Having the money go toward something beneficial to both parties is much more agreeable to a franchisee than having the cash drop to the franchisor's bottom line. Coming to the negotiating table prepared with some of these alternatives can go a long way to easing the stress attendant to the reservation of rights provision.

Not surprisingly, these provisions are the source of much arbitral and judicial scrutiny, generally in connection with assessing a franchisee's claim of encroachment by the franchisor. Because of that, it illustrates an instance where franchisors and franchisees may have a different desire for the structure and detail of the provision and therefore may approach the negotiation from very divergent angles. Courts have routinely held that a detailed and express contract provision bars the application of other legal theories, such as the covenant of good faith and fair dealing, which has been used by parties and courts to augment or construe certain terms. The franchisor's goal should be to have a detailed section regarding the grant of territorial rights, if any, to help set the parties' expectations and assist in dispute resolution. Franchisees, on the other hand, may negotiate toward less detailed language and more

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[25] Richard M. Asbill, Rupert M. Barkoff & Andrew C. Selden, *Franchise Agreements – New Approaches to Old Problems*, A.B.A. 25th Annual Forum on Franchising, Tab 2, 44 (2002).

[26] *See, e.g.,* IND. CODE ANN. § 23-2-2.7-1 ("It is unlawful for any franchise agreement entered into between any franchisor and a franchisee who is either a resident of Indiana or a nonresident who will be operating a franchise in Indiana to contain any of the following provisions: (2) Allowing the franchisor to establish a franchisor-owned outlet engaged in a substantially identical business to that of the franchisee within the exclusive territory granted the franchisee by the franchise agreement; or, if no exclusive territory is designated, permitting the franchisor to compete unfairly with the franchisee within a reasonable area."); *id.* at § 23-2-2.7-2 (Unlawful for franchisor to "[e]stablish a franchisor-owned outlet engaged in a substantially identical business to that of the franchisee within the exclusive territory granted the franchisee by the franchise agreement or, if no exclusive territory is designated, competing unfairly with the franchisee within a reasonable area…"(exemptions omitted)); IOWA CODE ANN. § 523H.6 (imposing extensive encroachment restrictions); WASH REV. CODE ANN. § 19.100.180 (encroachment restrictions); WIS. CODE ANN. §§ 135.03-135.04 (governing "changes in competitive circumstances").

ambiguity, wishing to instead allow for the option of using a good faith and fair dealing argument. Numerous publications detail the history and the application of the good faith and fair dealing argument.[27] Franchise counsel should be aware of the history and the case law surrounding the theory of good faith and fair dealing and its application to this area of the franchise agreement and relationship. Counsel should be just as aware, however, that a negotiation position based on case law rather than realistic and concrete business objectives, will not serve your client well.

3. Trademarks

Trademarks are the cornerstones of every franchise relationship.[28] A franchisor's trademarks are its most-valued asset and, as such, should be protected thoroughly by the language in the franchise agreement. Accordingly, franchisors are well advised to permit little, if any, changes to the language surrounding the ownership and use of the trademarks. Without the trademarks there presumably would be no value to doing business under the franchisor's name.[29] In other words, the franchisee believes that there is value in the franchisor's trademarks - enough so that the franchisee is willing to commit to spending a significant capital outlay, fees and royalties so that it can do business under such trademarks.[30] The value of the asset, combined with the franchisee's appreciation of the value (as evidenced by the desire to enter in a franchise relationship) results in little negotiation on this topic.

The franchisor should explicitly state its outright ownership and make sure that the franchisee cannot contest ownership of the trademarks under any circumstances.[31] The franchisor should state that any goodwill as a result of the trademarks remains the sole and exclusive property of the franchisor.[32] In drafting clauses relating to the franchisor's trademarks, it is important that at least the specific principal trademarks are identified (e.g., in an appendix to the franchise agreement).[33] The agreement should also specify how those trademarks may permissibly be used by the franchisee and that the franchisor has the right to modify the trademarks from time to time.[34]

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[27] For a compilation and history of encroachment case law by legal theory, *see* Erika L. Amarante, Andraya C. Frith & Karen B. Satterlee, *Territory, Exclusivity and Encroachment – Thinking Ahead of the Curve and Dealing with the Fallout*, A.B.A. 32nd Annual Forum on Franchising Tab 23, 17-36 (2009). *See also* Ann Hurwitz & Brian B. Schnell, *Tough Issues: Drafting Challenges for Franchisors Operating in the New Economy*, A.B.A. 23rd Annual Forum on Franchising, Tab 3, 6 (2000). *See also* J. Michael Dady, Sandra J. Wall, & David Kaufmann, *Franchise Agreements, How Complicated Do They Need to Be?*, A.B.A. 30th Annual Forum on Franchising, Tab 8, 2 -7 (2007).

[28] Asbill, Barkoff & Selden, *supra* note 25, at 37.

[29] Olson, Spencer & Weinberg, *supra* note 11, at 52.

[30] *Id.*

[31] *Id.*

[32] *Id.*

[33] *Id.*

[34] *Id.* at 52.

4. **Infringement of Trademarks**

Most franchisors take great care when drafting clauses concerning the infringement of their trademarks, given the importance of those marks to their systems. As demonstrated in the sample clause below, it is typical for a franchisor to maintain control over the handling of actions with respect to trademark infringements and to expressly provide how quickly the franchisee is expected to notify the franchisor of any infringement of the trademarks and it is rare to have negotiation on this point.

Although much of the language related to infringement of trademarks is not negotiable, franchisees should take care to analyze how a challenge to the trademarks, or a change to the trademarks, may affect them and their businesses. Particularly, if the franchisor is new and/or key trademarks are not yet well established (or not yet registered), franchisees will want to push for language to ease uncertainty and protect their interests.

The paragraph below is an example of the franchisor's indemnity of the franchisee in the event the franchisee is sued for infringement by a third party for using the trademarks permitted by the franchise agreement. From the franchisor angle, the provision is drafted such that franchisor's liability is limited to a maximum aggregate amount equal to the initial franchise fee paid by the franchisee. A franchisor with a system that is not yet mature may feel that it needs to provide for this extra certainty to attract deals, or it may make the determination that it is fair to share in the risks of having a new, potentially vulnerable, trademark associated with the brand. On the other hand, franchisors with well-established brands also may be comfortable adding this type of language and allowing for a "give" in the negotiation, since the risk of a challenge to the use of the trademarks is low.

> *The Franchisor agrees to indemnify the Franchisee against and to reimburse the Franchisee for all damages for which Franchisee is held liable in any proceeding arising out of the use of any of the Trademarks in compliance with this Agreement and for all costs reasonably incurred by the Franchisee in the defense of any such claim brought against Franchisee or in any such proceeding in which he is named as a party, to a maximum aggregate amount equal to the initial franchise fee paid hereunder.*

5. **Additions and Substitutions of Trademarks**.

The provision above is for an unbeknownst franchisee or a franchisor that has the upper hand in the bargaining power. Ideally, from a franchisee perspective, there should be no ceiling on the amount of an indemnification. If there is a trademark infringement, then the franchisor should cover any and all costs and damages associated with such so long as it was not due to the acts or omissions of the franchisee.

Most franchise agreements give exclusive rights to the franchisor to modify or discontinue any of its trademarks, and that is likely not an area ripe for negotiation as franchisor counsel should insist on maintaining this absolute right for their franchisor clients. The business purpose behind this clause is to allow the franchisor to make any necessary changes to the system to meet business needs, respond to a successful challenge to the trademark, remain relative to the consumer, and stay competitive in the marketplace. It is in the best interests of the franchisee to allow for such changes because the franchisee presumably will benefit from the business judgment of the franchisor in this regard.[35] Some agreements even delineate which party should pay for the re-branding costs.[36]

Not all portions of the trademark language should be off limits for negotiation. How and when a franchisor may change its marks, as well as who pays for costs relating to any such change, should be discussed, and franchisee counsel should push to build some parameters into the agreement. Limitations on the time period for which a franchisor can make a change (for instance, not within a certain number of years of the effective date of the agreement), references to other provisions in the agreement (such as ensuring it is considered part of a required modernization), and cost sharing are all appropriate things to be considered. The example below illustrates a balance between the franchisor's right to change the mark with the franchisee's desire to have certainty in the timelines associated with and the expenses resulting from such a change.

The Franchisor has the absolute right to modify or discontinue the use of any of the Trademarks and/or use one of more additional or substitute names or marks, for reasons including, but not limited to, the rejection of any pending registration or revocation of any existing registration of any of the Trademarks, or the superior rights of senior users thereof. The Franchisee will immediately, upon written notice from the Franchisor and at the Franchisee's expense, make all changes or modifications to the Trademarks as specified by the Franchisor. If the changes to the Trademarks require substantial remodeling due to a modernization in trade dress, the expenditure will be considered toward the Franchisee's Maximum Modernization Amount. If the changes to the Trademarks result in a required change to outdoor signage, Franchisor will pay for 1/3 of the cost to replace Franchisee's outdoor signage if: (i) Franchisee's Restaurant's sign is less than 2 years old and (ii) Franchisor requires that Franchisee replace the sign within one year from the date of notification.

B. <u>Initial Fees and Continuing Royalties</u>

Although initial fees and continuing royalties are critical economic terms of a franchise agreement, these provisions are not often heavily negotiated absent a special circumstance (e.g., a franchisor needs help in a new territory or the prospective franchisee wants to develop a number of units or act as an area developer). The "market" rates for initial franchise fees are typically tied to the franchise system's specific industry, and generally include the costs of start-up services to be provided by the franchisor, as well as the right to open the franchised business. Initial franchise fees may vary depending upon the length of the franchise agreement term. Franchise agreements with longer terms typically have higher initial fees, since there is usually some exclusivity (however limited it may be) associated with the grant of franchise rights.

Although the amount of an initial franchise fee may not be negotiable, whether any portion of the fee is refundable is often a point of discussion. Franchisors will assert that the entire fee is earned upon the execution of the franchise agreement, and usually include specific language to that effect in the franchise agreement.[37] Franchisees may seek to mitigate some of

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[35] *Id.*

[36] Asbill, Barkoff & Selden, *supra* note 25, at 38.

[37] Franchisors will include this language to make it clear that the fee is not contingent upon the franchisor providing any additional services and that there is adequate consideration. *See* Olson, Spencer & Weinberg, *supra* note 11, at 11.

their risk prior to opening the business, however, and ask that at least a portion of the fee be refunded in the event the franchisee is unable to open the business (unable to complete the initial training, cannot find a suitable site, etc.).

Similar to the initial franchise fee, and absent special circumstances, continuing royalty payments are not often negotiated in franchise agreements. While some start-up franchisors desperate to open a location may agree to a lower percentage or a grace period for ongoing royalties, established franchisors with experience opening franchised outlets will not. Franchisees with leverage may try to negotiate lower royalty percentages or, at a minimum, seek to put a cap on them.[38]

Although it varies by industry, typically royalties consist of a weekly or monthly percentage of franchisee's "Gross Sales." While there is little debate that conceptually Gross Sales represents all of the revenues from a franchised business, franchisee counsel may seek to negotiate special carve outs for sales tax, taxes collected from customers by the franchisee for transmittal to the appropriate taxing authority, discounts for franchisor promotions and discounts given to employees. See Section III.M.7 below.

The method and application of payments are terms that may be negotiated even when the royalties themselves are not. In recent years, payment by electronic funds transfer ("EFT") has become the norm for most franchise agreements, allowing the franchisor to automatically deduct funds on the required payment date rather than waiting for franchisee payment. Franchisor counsel will often include language that allows the franchisor to deduct amounts from such EFT accounts if the franchisee is late or fails to make any payments (not just royalties). Franchisees will argue that this is overreaching and will either move to strike the clause or attempt to limit the amounts solely to royalties or to undisputed payments, or a combination thereof. This provision is an instance where counsel to the franchisor would be well advised to provide franchisor the unfettered "right" to deduct such amounts rather than including "in its discretion" language. [39] In the event of a dispute among the parties, discretionary language will be subject to interpretation and only muddies the waters when courts are looking at the covenant of good faith and fair dealing.[40]

Like many negotiated terms, the franchisor needs to be cognizant of any possible requirements to not only file with California pursuant to the CFIL, but also the potential requirement to disclose in the FDD that the initial franchise fees and/or royalties are subject to negotiated changes or at least a range of initial franchise fees and/or royalties charged to franchisees as a result of negotiations.

C. <u>Term</u>

1. <u>Initial Term</u>

The term provides the starting point from which the rights and obligations of the agreement begin, and it establishes the length of the relationship between the parties. Generally, there are average terms per industry, and it is ordinarily not a term up for negotiation,

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[38] Lawrence V. Ashe & Harris J. Chernow, *Negotiating Franchise Agreements: The Franchisee Perspective*, A.B.A. 23rd Annual Forum on Franchising, Tab 8, 12 (2000).

[39] William L. Killion, *Putting Critical Decision Making Where it Belongs: Scouring the Franchise Agreement of the "D" Word*, 24-SPR FRANCHISE L.J. 228, 230 (2005).

[40] *Id.*

although that is not to say that franchisors shouldn't conduct independent analysis of what is appropriate for their system and that the topic should be open for discussion. There are many factors that affect the parties' perspectives on the initial term and if and how they want to negotiate the language in the provision. However, from a business perspective, both parties should have the similar goal of establishing a term that is long enough for each to benefit from the franchise relationship.

Some of the key factors for franchisors when determining the term and for use in discussions related to the topic are: the flexibility desired by the franchisor to make administrative changes (which are more easily done at renewal than during the term), administrative ease, and maturity of the system. As discussed in previous sections, this too may be an area that young franchisors may be more generous with the length of term than established franchisors, since the additional term can be an attractive feature of the franchise offering. Franchisors should recognize that is in the best interests of the franchisor to give the franchisee enough time to recoup the initial investment. For instance, a large restaurant franchise with a significant build out cost will typically require a term of at least ten years, if not more, to justify the investment being made. In contrast, a home-based, low-cost service franchise, without a significant up front investment, can and often does have a shorter initial term.

Key points for a franchisee to raise in the negotiation of the franchise term include the market conditions, the start-up costs and build out time, and the lengths of associated agreements (i.e., lease agreements, bank loans). Franchisees should take into consideration the time necessary for site selection and build out of the premises, since it may be wise to ask for an additional term if they do not want to start the clock ticking on the initial term prior to the franchised unit being open for business. Franchisors can respond by being willing to be creative and draft so that the initial term begins earlier than the opening of the location but also takes into account the realities of build out time, lease terms, and other factors. Franchisees also want to keep in mind how the term may affect their exit strategy. The longer the term, the greater the opportunity to build up equity and be in a better selling position (a prospective purchaser will be more willing to purchase a business with a remaining agreement term of ten years than one with three years remaining).

2. <u>Renewal Term</u>

There are generally four approaches that the parties can take to the renewal provisions. First, the franchisor might prohibit renewal of the franchise agreement. Second, the franchisee may have the right to renew, but only under certain conditions and upon the approval of the franchisor. Third, renewal might be automatic upon expiration of the initial term. Fourth, the parties might agree that the agreement is perpetual ("evergreen").

At the outset, a franchisee often seeks the broadest possible renewal rights in an attempt to recapture the initial investment fully and have a business to sell as a going concern. On the other hand, the franchisor will want to draft for flexibility at the end of the term so that necessary changes can be made in the pursuit of system goals, profit and financial success. The franchisor will usually benefit from a franchisee with a long-term, vested interest in the franchised business. However, the wise franchisor also understands that it will be best protected by incorporating certain considerations into the renewal clauses and restricting them to a certain extent. If done properly from the franchisor's perspective, it can negotiate to treat "each franchisee uniquely and create its own calculus to determine whether renewal is desirable." As such, the franchisor will try to include some degree of flexible language regarding term and renewals. Much of the detail contained in the renewal provision relates to the conditions that a franchisee must satisfy to exercise its right to renew.

Franchisor attorneys should consider applicable state laws when drafting a renewal provision and analyzing if changes should be made in the context of negotiation, as this is an area where the law may place certain restrictions on nonrenewal of a franchise agreement. The franchise statutes in some jurisdictions, for example, require franchisors to provide notice of and have "good cause" for nonrenewal under some circumstances, notwithstanding contract terms to the contrary. In other jurisdictions, even if good cause is not required, franchisors must provide statutory-set, minimum notice of non-renewal and take other mandatory steps. From the franchisor perspective, the considerations related to state law are more of a drafting tip than a negotiating issue, as most state laws will be favorable to the franchisee. From a franchisee perspective, attorneys should know the details of the applicable laws, so that they can request appropriate changes on behalf of their client. Although the law should trump the contract at the time of renewal, franchisees are best served to have the appropriate language included in the contract, as too often parties rely on the contractual language.

In drafting, some franchisors prefer to exclude a renewal provision altogether while others will allow for a renewal period or two, or even (although rare in modern agreements) choose an evergreen renewal into perpetuity. Essentially, the choice of renewal provisions depends on the particular situation of the franchisor at the time of the agreement, including its business plans, bargaining power, and the law of the relevant jurisdictions. Often times a renewal term refers to the "then current form" of franchise agreement and drafters should consider adding a fair amount of detail to avoid future ambiguities about to what the "then current form" refers. If the franchisor wishes to change one or more of the fundamental business terms, such as royalties, advertising or other fees, in the then current form, it is recommended that this be specifically stated. This is an area ripe for negotiation by experienced franchisees and franchisee attorneys, who are likely to request that certain terms from the original agreement (generally relating to fees) are preserved in the new agreement.

Many renewal conditions are controversial with franchisees, and should provide some room for negotiation. For example, a requirement that the franchisee refurbish the premises as a condition of renewal often causes difficulty, especially if the costs are going to be significant or if "refurbish" is not well defined. Franchisee attorneys should strive for clarity and detail as it relates to this clause. It is fair to argue for this to be well defined, to give the franchisee a degree of certainty when it comes to budgeting for renewal. Suggestions include incorporating the cost into the modernization provision, specifically excluding franchisor's right to force relocation, etc. Often, renewal clauses state that a franchisee must execute a release as a condition to renewal, and franchisors are wise to insist on the inclusion of such release. However, in some states, such releases are void and unenforceable. Franchisee counsel that are armed with the knowledge of where and how releases are restricted are in a good position to negotiate revisions to the release portion of the renewal clause.

A renewal fee can vary greatly, sometimes as a fixed amount, while other times an amount that can fluctuate. It is not uncommon for the renewal fee, if any, to be tied to the then-current initial franchise fee, so that it can increase over time, which may be important when renewal will take place many years in the future. The negotiation surrounding the renewal fee may be a time too for franchisee attorneys to leverage the relationship. If things are going well between the franchisee and the franchisor such that the franchisee wishes to renew and the franchisor approves without issue, why should a fee be charged to merely continue business "as usual"?

Both parties should be thinking ahead and realize that any renewal, but particularly if a renewal is deemed a new contract, will result in administrative implications. For instance, if the franchisee is required to sign a new agreement in connection with the renewal, the franchisor must comply with franchise disclosure laws, even though the franchisee likely knows most (if not all) of this information contained in the franchisor's FDD by virtue of its involvement in the system during the initial term. Additionally, a new or renewed contract may come within regulations that presently exist but did not exist or apply to the "old" agreement (because those laws were enacted after the original agreement was executed and did not apply retroactively). As a result, both parties should be aware of whether the renewal triggers a new agreement and if so, how the current regulatory landscape may affect the relationship and the costs and time associated with the renewal process.

D. <u>Training and Operational Assistance</u>

1. <u>Initial Training by the Franchisor</u>

Franchise agreements generally require that the franchisee successfully complete initial training to the franchisor's satisfaction. Franchisors may or may not charge a fee for initial training for certain individuals, but franchisees must pay for any travel or living expenses virtually without exception. Training is imperative to opening the franchised business and ensuring consistency among units. Often the franchise agreement language will be somewhat vague with respect to specific requirements for initial training. This broad language mitigates the risk of success for any future claims by the franchisee alleging insufficient training, and recognizes that the training program is likely to evolve over time. Franchisors must evaluate the potential benefit of including more specific initial training requirements that the franchisee must complete, against the burden of having to provide such training.[41] Franchisees are likely to request specific training requirements and may seek to include an exhibit to the franchise agreement – which, as discussed, can cut both ways for the franchisee and franchisor alike. One point that franchisees may seek to negotiate is with respect to tuition and additional students. Franchisors may be willing to allow additional people to attend training at no additional cost. This is a good example of a provision that can be negotiated and benefit the franchisee without (depending upon the cost) adversely affecting the overall system.

2. <u>Ongoing Training by the Franchisor</u>

Depending on the industry, the franchisor may or may not require additional or ongoing training throughout the course of the agreement. Franchisors are also likely to keep this additional training language very vague and, similar to initial training, will require the franchisee to pay for any travel, lodging, and meal costs, as well as any tuition it imposes. The franchisee is likely to negotiate that additional training be conducted either in close proximity to the franchised business or that classes be made available on line, if possible. Franchisors will also include provisions that the franchisee is required to attend any additional or refresher training, but that the franchisor is not obligated to provide it. In some limited circumstances, franchisees may successfully argue for language that the Franchisor will (or will use commercially reasonable efforts to) provide additional or refresher training upon franchisee's request. These provisions are often very specific to certain industries and can depend upon the franchisee's leverage, as well as how much ongoing education is required to successfully run the business. Finally, the operations manual often includes specific requirements

[41] *See, e.g.,* Olson, Spencer & Weinberg, *supra* note 11, at 19.

regarding ongoing training. Prospective franchisees and their counsel should ask to see and review these requirements prior to executing the franchise agreement.

An example:

Franchisor from time to time may provide, and if it does, may require that previously-trained and experienced franchisees, their managers and/or employees attend and successfully complete refresher training programs or seminars to be conducted at Franchisor's headquarters or at such other place as Franchisor shall designate. Attendance at such refresher training programs or seminars shall be at Franchisee's sole expense, provided, however, that attendance will not be required at more than 4 such programs in any calendar year and shall not collectively exceed 8 business days in duration during any calendar year.

3. Franchisor's Operating Assistance

Most franchise agreements include obligations on the part of the franchisor to provide certain services to the franchisee both prior to and after the opening the franchised business. Obligations with respect to site selection, training, pre-opening assistance, as well as sales of products or services during the term of the franchise agreement, are generally found in most franchise agreements, however, the specificity and extent of such services may be a point of negotiation.

Franchisors will typically negotiate to keep any provision regarding operating assistance vague and at their discretion. Language regarding operating assistance is often drafted to require only what is absolutely necessary for the success of the franchised business. Franchisees, on the other hand, may seek to include specific requirements. Although provisions with specific language regarding ongoing assistance may invite disputes with respect to what was or was not included, franchisors should be careful not to draft provisions that are too vague. Such provisions could similarly lead to disputes about the franchisor's exercise of discretion (what should or should not have been provided and whether it was sufficient). Requirements negotiated by franchisees will usually include: visits from the franchisor, availability to answer questions, specific help with site selection, guidance regarding advertising and marketing, administrative, bookkeeping and accounting procedures, use of authorized computer systems, etc.[42] An example of typical ongoing assistance language:

Franchisor will provide Franchisee continuing consultation and advice as Franchisor deems necessary and appropriate regarding the management and operation of the Franchise Business. Franchisor will provide such assistance, in Franchisor's discretion, by telephone, facsimile, intranet communication and on-site visits.

In addition to keeping operating assistance requirements vague, some franchisors will seek to limit future claims by franchisees that pre-opening or ongoing assistance was insufficient by including acknowledgement and waiver language in the franchise agreement. An example of such a provision is set forth below:

[42] *Id.* at 19-20.

> *If Franchisee believes that Franchisor has failed to adequately provide pre-opening services to Franchisee in regard to the initial training, selection and purchase of equipment and supplies, or any other matter affecting the establishment of the Franchised Business, Franchisee shall notify the Franchisor in writing within 30 days following the opening of the franchised business. Absent the timely provision of such notice to Franchisor, Franchisee is deemed to have conclusively acknowledged that all pre-opening and opening services required to be provided by Franchisor were sufficient and satisfactory in Franchisee's judgment*.[43]

This language not only puts the franchisee on notice, it requires the parties to resolve any disputes with respect to pre-opening obligations in a timely manner (when they are more likely to still be committed to the "relationship") and relieves the franchisor from any lingering worries about such a claim arising in the future. While the language above provides some protection with respect to the timing of a claim, the following provision actually gives a standard by which to judge the potential claim.

> *Franchisor is not obligated to perform services set forth in this Agreement to Franchisee's particular level of satisfaction, but as a function of Franchisor's experience, knowledge and judgment. Franchisor does not represent or warrant that any other services will be provided to Franchisee, other than as set forth in this Agreement. To the extent any other services, or any specific level or quality of service is expected, Franchisee must obtain a commitment to provide such service or level of service in writing, signed by an authorized officer of Franchisor, or Franchisor shall not be obligated to provide any other services or specific level or quality or service*.[44]

Both franchisors and franchisees should consider incorporating the concepts in both of the foregoing provisions into their franchise agreements. These concepts provide each side with a clear understanding of the expectations for services, as well as the standard by which such services will likely be judged.

E. <u>Modernization or Replacement</u>

Franchise agreements commonly include a modernization provision, which is included by franchisors to permit them to adapt and change the business over time to stay current in the marketplace. After all, most franchise agreements span a considerable period of time relative to other business arrangements, and franchisors don't want to be restricted as to when and where they can implement changes to existing units. The obligation generally involves the franchisee's commitment to upgrade the premises throughout the franchise agreement term, or as triggered by a particular event, such as renewal or transfer. The franchisor should be mindful of this clause so that the general image of the trademarks is being adequately preserved and improved throughout the term of the franchise agreement. If this clause is absent or inadequately drafted,

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[43] Joseph J. Fittante, Jr. & Dennis E. Wieczorek, *Advanced Drafting*, A.B.A. 27th Annual Forum on Franchising, Tab 11, 10 (2004).

[44] *Id.*

the franchisor might risk not being able to require that franchisees keep their locations up to its standards, or their brand competitive and relevant to the consumer, which in turn might end up damaging the goodwill of the overall franchise. New franchised businesses appear every year and pose competitive threats to existing businesses; the modernization clause gives the franchisor a tool to address these challenges over the life of a franchise agreement. This is an example of a clause where it is particularly important for the franchisor to understand its position as the steward of the brand. The conversations can be difficult, and the franchisee will not like the uncertainty of the provision, but it is a critical element of a franchise agreement and to protecting the system as a whole.

Franchisees will often balk at the notion of this type of provision, especially if it is drafted in such a way as to provide the franchisor with a "blank check" in terms of what renovations the franchisee can be required to undertake. Franchisees should negotiate for certainty in timeframes and expenditures. Request, for instance, that (i) no changes can be required during the first few years of the agreement, (ii) a maximum modernization amount is set at the time of entering into the agreements, (iii) the requirement is not applicable if the property's lease expiration is imminent, and (iv) there is a time period to complete the modernization. Restrictions such as these can provide franchisees with some clarity and comfort regarding the applicability of this provision and the potential effect on the bottom line. Although beyond the scope of the negotiation, counsel should also advise their franchisee clients to keep excellent records of improvements done throughout the term and to communicate such improvements to the franchisor so they are ensured credit against any required modernization.

F. Operation of the Franchised Business

1. Request for Change of Supplier

The typical franchise agreement requiring that a franchisee obtain its products in connection with the operation of the franchised business from either the franchisor, an affiliate of the franchisor, or an approved supplier, carries with it the debate of how much control is enough and to what extent should the franchisor control the supplying of products and services to the franchisees and how will it affect the relationship. As is the reason for many provisions in the franchise agreement, the concept of a franchise system starts with the concept of uniformity throughout the system and the need for the franchisor to control certain aspects in order to oversee and enforce such uniformity. One of the main ingredients (pun intended) is the products and services that the franchisor and/or franchisees are offering to the consumer. In that sense, the franchisor wants (or needs) to make sure that the products and services meet certain criteria and standards, which will define the franchise system. Assuming a typical provision that reserves to the franchisor the right to designate where and what a franchisee must purchase (based upon franchisor specifications, criteria and standards), what can a franchisee do if it feels that change is warranted or if there is a better or more efficient supplier or product? A typical franchise agreement usually provides a procedure for franchisees to present an alternative vendor or product to the franchisor and for the franchisor to review the request by the franchisee. However, in the typical franchise agreement, the franchisor is not obligated to approve any of the franchisee's requests. Faced with this situation, the prospective franchisee has a couple of points that it could raise. First, the prospective franchisee can seek to modify the supplier provision to provide that the products required to be purchased based upon certain specifications and through certain supply chains will not exceed the pricing that the franchisee could obtain if it did not use the "approved" vendors (assuming the product is identical in terms of specifications, criteria and standards). In addition, the prospective franchisee can seek to limit Franchisor's right to consent to any franchisee requested changes to products and suppliers, so long as the franchisee follows the standard procedures for obtaining approval and the product meets the same criteria, specifications and standards of the required product or approved supplier. The caveat to all of this is if the product is proprietary. Then the franchisor does and should have complete control over process, including the suppliers, as proprietary products are the keystone of the system and should require the highest protections possible within reason. "Within reason" means that a franchisor should consider requests for changes, even in connection with proprietary products, if the franchisee(s) have been able to obtain a more efficient and/or less costly distribution of the product. One of the competing issues with the purchasing/supply requirements is whether or not the franchisor benefits from the requirements, whether through a rebate, discount or allowances. Supply arrangements are a topic that extends beyond the scope of this paper, but should be carefully considered by the franchisee if there is a request for change and how that change could possibly affect some of the benefits or services that the franchisor provides to the franchisee. For example, a number of systems that do receive certain rebates, discounts or allowances, contribute such monies to the franchise system's national advertising fund. If those monies are not available through the supply chain system, the franchisees will then need to step up on their own to fill in the gap. Ultimately, the new supply chain may prove to be more costly than the previous one when all factors are considered.

2. <u>System Modifications</u>

A common argument, and one for which there may not be an answer, is the importance of product supplier designations compared to the importance of system modifications. System modifications relate to the overall operation of the franchise system and how the system operates in terms of processes, appearance, products and services offered, or anything and everything related to the actual franchise system. Typically, throughout a franchise agreement, there are numerous references to the right to change the system from time to time at the sole discretion of the franchisor. If you ask franchisors what one provision would they not allow modifications to if they had to pick one, you may find that the right to modify the system at any time is the number one choice. Keeping in mind that a franchise agreement is typically for five, ten and even twenty or so years, there has to be flexibility within the franchise agreement for the franchisor to adapt not only to the times and changes in the world, but to its competition and, possibly more important, how the franchisor desires to operate its system. The right to system modifications may be even more critical for a start-up franchisor who is "learning" its way through the franchise process. On the other hand, a franchisee who reads the franchise agreement may wonder, how do I enter into an agreement that allows for the other party to make any and all changes that it wishes on the spur of the moment to which I, the franchisee, would then be obligated to implement without having any basis for what the change may mean in terms of cost (time and money) and relevance to the business that supposedly I bought years ago? Can there be a middle ground in this area? A franchisee could request a number of suggestions to this language. They could ask that the any fundamental material changes be "reasonable" in nature or to not have a dramatic/significant monetary effect on its operations. Similarly, they could add language to add certainty in the timing of the changes, such as the ability to have a lead in time for changes to be implemented or not to be mandated if a franchisee is in its last one or two years of the remaining term of the franchise agreement. Perhaps an uphill battle, but the franchisee could also request that the franchisor demonstrates to the franchisees the benefits of the changes (or even that the franchisor must go through to prove to the franchises the benefits of the material change to system, prior to implementation) and/or agrees that material changes will not to occur more often than a certain number of years.

G. Advertising

This is an area that from time to time receives a lot of scrutiny in part because it requires the franchisee to pay funds either directly or indirectly to the franchisor, or requires the franchisee to spend certain amounts for advertising even if such amounts do not go to the franchisor. Therefore, this is a direct out of pocket expense of the franchisee and which, at times, is considered to be no different than a royalty since many advertising provisions operate similar to a royalty in that there is a requirement of a certain percentage of Gross Sales to be paid into an advertising fund or spent on advertising. Any time there is money involved, the typical thought process is that such can be negotiated.

The advertising provisions run the gamut from the requirement of monies to be paid into a national advertising fund operated and controlled by the franchisor or its affiliate to, and including, the requirement for franchisees to spend certain dollars on regional advertising and/or local advertising and, at times, in conjunction with advertising cooperatives. Typical provisions provide everything from x percentage for the national advertising fund, y percentage for a regional fund, z percentage for local advertising, and certain requirements for monies to be paid to a cooperative, assuming all are in place in a particular system. Some systems allow for offsets, such as if there is an advertising cooperative, then the amounts paid into the cooperative count toward local and regional advertising and sometimes even count toward the national advertising fund. In analyzing what the pros and cons of negotiating or modifying advertising provisions, like all provisions, depends on the exact arrangement. In general, advertising is another one of those areas that franchisors do not necessarily want to negotiate or modify. First, there is a sense that advertising requirements should be equal for all franchisees and therefore, the franchisor does not want to negotiate or modify the requirements for one or two franchisees. However, in a start-up situation, there is more likelihood to negotiate the advertising and for such to be based upon certain threshold standards. For example, the franchisee in a new system, zero to five units, may request that advertising or at least national advertising payments only be required once the franchisor has x number of franchisees within the system or y number franchisees within a certain area. Secondly, if advertising is to be required in the new system, the franchisee may request that the advertising dollars be targeted to the franchisee's general geographic area, rather than the typical national sole discretion advertising which allows the franchisor to advertise in any manner it so desires and not have to target any specific geographic area.

Another area of potential contention is the "fees" that are generated by a franchisor in connection with advertising programs that generate dollars directly from the franchisees. The contentious area is the allocation of the funds toward expenses. In many typical advertising provisions, it allows for the franchisor to allocate overhead to the advertising fund and for the advertising fund to in turn reimburse/pay the franchisor for such overhead. Also, many advertising provisions contain an administrative fee component such as five (5%) percent to fifteen (15%) percent to be paid to the franchisor for administrative services.

What should a franchisee request in connection with advertising fund provisions? There are a number of areas that can be reasonably raised in connection with the advertising provisions. They are as follows:

a. Modifications to the expenses to be contributed to the advertising fund and paid to the franchisor to make sure that such expenses are reasonable and directly related to advertising. Keep in mind that a franchisor typically includes in the definition of advertising, advertisements for "franchises for sale" and to be paid for by the advertising fund. A debate for another day is whether or not that should be part of the advertising fund, which for purposes of this paper, we will assume that advertising for a franchise that is available does indeed help create brand loyalty and brand recognition by having more units and, thus, having more potential customers and more people knowledgeable with the system, which are the goals of advertising – brand recognition and brand loyalty;

b. The ability to have an accounting and/or audit of the advertising fund on a yearly or semi-yearly basis;

c. The ability to have franchisee input or the formation of a franchisee committee in connection with the franchisor advertising programs;

d. If there are no offsets for monies paid to national, regional, local advertising and cooperatives, the possibility of offsets, at least as far as a cooperative or the regional advertising is concerned in connection with national advertising. However, that will be a product of what actually is required in terms of dollars and cents if the national advertising is relatively low and the others when added together, equate to a "typical" advertising fund requirement, then this may be an unnecessary point; and

e. A requirement that all units, including company and affiliate units, contribute to the advertising requirements at the same level as all franchisees. However, this creates the issue of what happens if there are different "deals"; what is the amount that the company and/or affiliate units pay? In this situation, linking the contribution to the form of franchise agreement attached to the then-current FDD might be a workable solution.

H. <u>Restrictive Covenants and Trade Secrets</u>

These provisions provoke an ongoing debate as to whether or not there should be such a provision in the agreement and, if so, to what extent it is to be enforced. The debate among franchisees is between (a) those that are on their way out who do not want a restrictive covenant and (b) those that are within the system that want a restrictive covenant to protect themselves from the former franchisees. This debate is illustrated in the example of an accountant practicing for ten years, who decides to purchase an accounting franchise system which contains within the franchise agreement a restrictive covenant. A year later, when the accountant leaves the franchise (without cause), he is forbidden from pursuing a business competitive to the accounting franchise. This person is now forbidden from pursuing the one occupation/skill that he has been trained in from day one. This may be an extreme example, but a true one. Moreover, with respect to the radius of a restrictive covenant, an argument can be made that the restrictive covenant area should be equal to the exclusive or protected territory of the franchise or other franchisees. What is sauce for the goose should be sauce for the gander.

I. <u>Transfer</u>

1. <u>Transfer by the Franchisee</u>

Transfer provisions are often the subject of negotiation and they raise a number of the same issues as renewal. While the franchisor may want to impose an exhaustive list of conditions to the approval of a transfer, practitioners should keep in mind that these transfer restrictions are limited by certain state laws.[45] Many franchisees will lobby to add language that the franchisor cannot unreasonably withhold consent to a franchisee's proposed transfer, which is actually required by some states (making it a bargaining chip for franchisors).[46] Obviously franchisors have a strong interest in maintaining qualified and capable franchisees in their system and will want an unfettered ability to approve (or deny) the transfer of the franchised business. Notwithstanding this interest, franchisees may have some leverage in this area. The ability to transfer the agreement is the only way the franchisee can liquidate its investment if needed.[47] Furthermore, although ideally the franchise agreement will continue between the franchisor and the original operators, it is not realistic to assume there will never be issues or instances when the agreement will need to be transferred in order for the business to stay successful, or even survive; or as a mechanism for a franchisee to extricate itself from the system for whatever reason. A healthy secondary market can indicate that units are in demand and people want to own them.[48] On the other hand, it could be a sign of franchisees wanting out of the system. In order to protect the system going forward and ensure that the prospective transferee meets its standards, the franchisor will insist upon certain conditions for transfer. Regardless of how few or how many conditions are imposed, both franchisor and franchisee will want to minimize potential transaction costs and provide for a smooth transition.

2. Conditions of Transfer

Typical franchisor transfer conditions in a franchise agreement include the following (certain conditions the franchisee may seek to negotiate are included in bracketed notes):

a. Transferee is not a competitor of the Franchisor;

b. Franchisor must approve/be provided with a copy of the transfer documents;

c. No defaults under franchise agreement;

d. Franchisee is current as of date of transfer;

e. Franchisee delivers a complete release of Franchisor [***Note: this provision may be negotiated in some instances in the event franchisee has multiple agreements or locations with the franchisor. The franchisor will likely want a complete release of all claims under any agreements with the franchisee, and the franchisee will seek to limit such a release to claims under the specific franchise agreement.***];

f. Proposed transferee signs then-current form of franchise agreement [***Note: franchisee counsel may negotiate to allow***

[45] See, e.g., ARK. CODE ANN. § 4-27-205; CAL. BUS. & PROF. CODE § 20027; HAW. REV. STAT. § 482E-6; Ind. Code Ann. §23-2-2.7-2(3); Iowa Code §523H.5; MICH. COMP. LAWS ANN. § 445.1527; MINN. STAT. ANN. § 80C.14; NEB. REV. STAT. § 87-405; N.J. STAT. ANN. §56:10-6. Note that the transfer restrictions in California and Indiana only apply to certain transfers upon the death of the franchisee.

[46] *See* Olson, Spencer & Weinberg, *supra* note 11, at 60.

[47] *Id.* at 60.

[48] *Id.*

the assignment of the existing franchise agreement rather than the execution of a "then-current" form since such a requirement may make the franchised business significantly less marketable. The "then current" form may well provide for significantly higher royalty payments and more onerous terms than the franchisee's existing agreement. Franchisor counsel can likely counter that the proposed transferee is buying into a more valuable brand and system than the existing franchisee, and thus should be subject to the same requirements as new franchisees];

g. Proposed transferee provides guaranties from anyone whom the Franchisor may request;

h. Proposed transferee completes training to satisfaction of Franchisor;

i. Proposed transferee provides evidence satisfactory to Franchisor, that proposed transferee meets standards for system franchisee;

j. Purchase price is reasonable in the circumstances with respect to the debt and interest charges being acquired or already in existence;

k. Proposed transferee (or franchisee) pays transfer fee [***Note: this provision may be negotiated in an attempt to limit the fee to a fixed percentage of the initial franchise fee or to franchisor's costs associated with evaluating the proposed transfer in the event franchisor does not consent to the transfe*r**]; and

l. Franchisee and the proposed transferee agree to perform all maintenance and upgrades as required by Franchisor.

3. Right of First Offer or Right of First Refusal

Franchisors will often include a right of first refusal or, less common, a right of first offer to purchase the franchisee's business prior to any proposed transfer. Franchisees frequently argue that such a right actually depresses the value of the business – since it makes it less certain that a potential purchaser can actually close on the transaction – i.e., if it's a good deal, the franchisor may take it. Negotiating to remove the right of first refusal is likely a losing battle for most (if not all) franchisees, but certain limitations on such rights may be agreeable to the franchisor. Franchisors will usually include the ability to review the proposed transfer documents, as well as a right to follow up with additional information requests, the right to negotiate with the prospective buyer regarding the terms of the deal without it being deemed a rejection of the offer, the right to substitute cash for in-kind payments by the proposed buyer, and a reasonable period of time to review and approve or reject the offer.[49] Franchisees and franchisors alike would be well advised to establish even an informal procedure for handling the right of first refusal that allows the franchisee to raise a potential transaction informally with the

[49] *Id.*

franchisor. Timing is often difficult when trying to coordinate closing a transaction while complying with the franchisor's right of first refusal.

4. Transfer or Assignment by the Franchisor

Allowing the franchisor to freely assign the franchise agreement is a crucial term for franchisors. Without explicit language to this effect, franchisors may be required to seek consent from every operator in the event of a merger, acquisition, sale or reorganization. Typically, this provision also includes an acknowledgement that the franchisor is released from any and all obligations following such transfer and sometimes includes a waiver by the franchisee of any claims related to the transfer. Particularly in light of the increase in private equity investment in franchise systems, flexibility with respect to financings, sales, mergers, reorganizations and restructurings is critical to franchisors, as well as their potential investors.

Short of requesting a consent or approval right over transfers, franchisees may try to negotiate certain threshold requirements for prospective franchisor transferees. Franchisees may ask for net worth or identity requirements. Negotiating changes to the franchisor's absolute right to transfer could jeopardize the franchisor's overall exit strategy and delay or prevent the transaction from closing, since such restrictions may invite claims from disgruntled franchisees, particularly in the event of a franchisor transfer to a competing system.[50]

J. Termination

1. Events of Default and Right of Termination

Termination provisions, like those for transfer and renewal, are crucial to a franchisor's ability to control the system. Franchise agreements include a lengthy list of conditions that constitute an event of default under the agreement. Typically, there are distinctions between events of default that can be cured after notice to a franchisee, and those that allow a franchisor to terminate the agreement immediately upon notice to a franchisee (or in some instances even without notice). As with all provisions discussed in this paper, the circumstances and bargaining power of the franchisee will ultimately dictate the extent to which these provisions may be negotiated. Franchisee counsel may argue that allowing a franchisor to terminate without notice or providing very short cure periods could put a franchisee at serious risk for a technical default. Franchisor counsel will likely counter that consistent cure periods and remedies are important for managing the overall system, and that agreeing to modify termination provisions not only puts the franchised business at risk, it creates an undue administrative burden on the franchisor.

Typical events of default that constitute "good cause" without notice or the opportunity to cure include the following example provisions (in some instances the language in bold may be negotiable, or at least worth raising with franchisor counsel). Practitioners should also be mindful of state relationship laws that may limit a franchisor's right to terminate – some states require "good cause," mandatory notice periods, and a right to cure[51]:

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[50] *See* Kirk W. Reilly, L. Seth Stadfeld & Philip L. Wharton, *Litigation After Acquisition of a Competing Franchise System*, A.B.A. 29th Annual Forum on Franchising, Tab 6, 12-13 (2006).

[51] *See* Exhibit A attached.

a. *Franchisee becomes insolvent or admits in writing Franchisee's inability to pay its debts as they mature, or makes an assignment for the benefit of creditors, files a petition under any foreign, state or United States bankruptcy act, receivership statute, or the like or if such a petition is filed by a third party, or if an application for a receiver is made by anyone and such petition or application is not resolved favorably to Franchisee within* [***ninety (90) days***] [***Note: this provision will be preempted and ineffective under the Federal Bankruptcy Code, however, many franchisors include it***];

b. *abandons the Franchised Business by failing to operate it for five (5) consecutive business days or for any shorter period in such circumstances that render reasonable the conclusion that Franchisee does not intend to continue operating the Franchised Business, unless such failure is due to disaster or similar reasons beyond Franchisee's control*;

c. *has made any material misrepresentation or omission in the application for the Franchised Business or in any report that Franchisee submits to Franchisor pursuant to this Agreement;*

d. *is convicted by a trial court of or pleads no contest to a felony or other crime or offense or engages in conduct that reflects materially and unfavorably upon the operation and reputation of Franchisor, the System or the Franchised Business, or if any Principal is convicted of or pleads no contest to a felony or other crime or offense or engages in such conduct*[52] *[**Note: this may be negotiated on a case by case basis depending on the system and the impact of such a conviction – and for what**];*

e. *attempts to make or makes an unauthorized assignment, encumbrance or other transfer of Franchisee's rights or obligations under this Agreement*;

f. *makes any unauthorized use of the Marks or Confidential Information or makes any duplication or disclosure of any Confidential Information, including, but not limited to, any portion of the Manual*;

g. *fails on **[three (3)]** or more separate occasions during **[any twenty-four (24) month period during the Term]** to pay on a timely basis any fees payable hereunder or otherwise fails to comply with this Agreement, whether or not such failures to comply are corrected after notice is delivered to Franchisee and whether or not such failures to comply relate to the same or different requirements of this Agreement*;

[52] See *International House of Pancakes, LLC v. Parsippany Pancake House, Inc.*, 2012 U.S. Dist. LEXIS 89112 (D.N.J. June 27, 2012) (district court holding that a franchisee's felony conviction for endangering the welfare of a child was insufficient under New Jersey law to permit immediate termination of the franchise).

h. *shall at any time have the Franchised Business or its assets or premises seized, taken over or foreclosed by a government official in the exercise of such official's duties, or by a creditor, lien holder or lessor of Franchisee, or a writ or levy of execution shall issue against the franchise granted hereunder or the goods and chattels of Franchisee*;

i. *fails, for a period of **[ten (10) days]** after notification of noncompliance, to comply with any federal, state or local law or regulations applicable to the operation of the Franchised Business provided such cure period shall be **[three (3)]** days for any noncompliance that poses a threat to health or safety*;

j. *engages in an activity that conflicts with Franchisee's obligations under this Agreement; including involvement in a Competitive Business*; **[*Note: "Competitive Business" may be negotiated to include carve outs depending on the nature of a franchisee's existing businesses and franchisor's desire to have franchisee in the system*]**; or

k. *if Franchisee's right to operate under any license or permit material to the operation of the business is suspended, terminated or interrupted* **[*provided, however, this provision shall not apply if such suspension, termination or interruption results solely from Franchisor's noncompliance with any franchise or business opportunity law*]**.

In addition to the foregoing events of default, franchisors will provide events of default giving rise to franchisor's ability to terminate but only after providing notice and the opportunity to cure:

> *This Agreement will terminate upon Franchisee's failure to cure any of the following, each of which is deemed to be "good cause":*

x. *noncompliance with any requirement in this Agreement not listed in Subsection (a) through (k) above within thirty (30) days after notice thereof is delivered to Franchisee; or*

y. *failure to make payments to Franchisor for any amounts due within **[five (5) days]** after notice thereof is delivered to Franchisee*.

2. <u>Liquidated Damages</u>

Liquidated damages provisions provide a contractually agreed formula for calculating the damages to the franchisor as a result of the early termination of the franchise agreement.[53] Liquidated damages provisions are negotiated in franchise agreements in a couple of ways – both as to whether to include them in the franchise agreement at all, and with respect to their actual terms. Many franchisees may be hesitant to agree to such a provision

[53] *See* Olson, Spencer & Weinberg, *supra* note 11, at 53.

and put the burden on the franchisor to show actual damages, which can certainly cut both ways. Although a franchisor may wish to include a liquidated damages provision to eliminate the challenge surrounding the proof of actual damages, a franchisor cannot use such a provision as a penalty and must be careful to negotiate an amount that is not disproportionate to the harm caused to the franchisor. Additionally, the parties should be mindful of the enforceability of liquidated damages provisions in certain jurisdictions.

3. Franchisee Obligations on Termination

All franchise agreements include provisions regarding the franchisor's rights and franchisee's obligations upon termination. Typically, these provisions include a requirement that the franchisee pay all amounts due, discontinue operation of the business, discontinue use of the mark, de-identify the franchised business, return all materials (including the operations manual), etc. This is a very important provision for franchisors and, similar to the events of default and termination rights, one of the most powerful ways for a franchisor to protect its trademarks and system. As such, this is not usually a negotiated provision, although franchisees may seek additional time to comply with the obligations. Additionally, franchisees may also seek to limit any required post-term modifications to de-identify the premises, rather than agreeing to make "such modifications as the franchisor may require," a common provision included by franchisors.

4. Franchisor's Right to Repurchase

Often franchise agreements will include a provision allowing the franchisor to repurchase some or all of the assets of the franchised business upon expiration or termination of the franchise. These assets may include inventory, fixtures and equipment. Franchisors will often include this provision in order to prevent the former franchisee from re-selling or using the assets. One point that may be negotiated is the purchase price for such assets. Franchisors will seek the right to repurchase at the book value (to avoid having to pay any amounts for goodwill associated with the mark), whereas franchisees will try and negotiate for a fair market value concept. Notwithstanding the foregoing, both sides should be aware that a number of states require franchisors (at the franchisee's option) to repurchase equipment or inventory upon termination.[54] Depending on the state, this requirement may only apply if the franchisee is terminated without cause, or it may only apply to inventory purchased from franchisor or materials that bear the franchise mark or logo. Most states with these requirements are silent with respect to the determination of value and whether or not goodwill must be included.

5. Right of a Franchisee to Terminate

While franchisee counsel may seek to negotiate a contractual termination right for their clients, they should proceed with caution. Often franchisors will agree to include a termination provision, but it may actually end up limiting a franchisee's common law rights to terminate upon a franchisor's material breach. These termination provisions often include: (a) allowing termination only if the franchisee is not itself in breach of the agreement; (b) requiring the franchisee to give notice to the franchisor of the franchisor's default; and (c) allowing the

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[54] *See* Clay A. Tillack & Mark E. Ashton, *Who Takes What: The Parties' Rights to Franchise Materials at the Relationship's End*, 28 FALL FRANCHISE L.J. 88 (2008). State statutes grant varying rights to franchisees and franchisors, so choice of law often becomes important. Hawaii, Illinois, and Washington require franchisors to pay their former franchisees for local goodwill generated during the life of the relationship in certain circumstances, and Delaware, Indiana, Minnesota, Mississippi, Missouri, Nebraska, New Jersey, and Virginia include loss of goodwill as compensable damages for wrongful termination.

franchisor a cure period.[55] In such instances, a franchisee would be better served if the franchise agreement remained silent on the matter.

K. Accounting, Records, Reports, Audits and Inspections

1. Accounting, Reports and Financial Information

Franchise agreements are based on royalties and fees paid by the franchisee to the franchisor over the life of the agreement, and often such fees are based on a percentage of "Gross Sales" or a similar concept. As a result, franchisors will often require that franchisees use a certain accounting or bookkeeping system. Franchisors want to minimize the likelihood that a franchisee may be able to mask sales or underreport royalties. In addition to the type of accounting or bookkeeping system, franchisors also may require that the franchisee provide certain reports, including financial information and supporting documentation for royalty calculations. The timing, nature, and content of the reports is frequently a source of negotiation.

From the franchisor's perspective, periodic reports vetted by third parties (i.e. audited financial statements) are the best way to reduce the likelihood of underreporting by franchisees. Unfortunately, these reports come with a significant price tag, and franchisees will argue that requiring audited financial statements is an undue burden. Franchisors may compromise and agree to accept either reviewed or compiled financial statements, together with unaudited periodic reports that include specific supporting financial information. In addition to financial information prepared by or on behalf of the franchisee, many franchisors will also require that the franchisee provide the franchisor with access to financial information regarding the franchisee from banks, suppliers, and other creditors of the franchised business.[56]

From a practical perspective, franchisors and franchisees are likely better off with an agreement that specifically spells out what information is required and when it is due, as well as the party responsible for preparing and delivering it. This can help avoid any ambiguities going forward on both sides. Given the ongoing, symbiotic relationship between the franchisors and franchisees, carefully vetting these provisions is crucial for a successful relationship.

2. Inspection and Audit of Books and Records

In addition to requiring certain financial reports and information, franchisors will often require the right to inspect the franchisee's books and records. While some iteration of this requirement is likely present in almost all franchise agreements, the scope of such inspection and audit rights is often a negotiated term. For instance, how frequently can the franchisor inspect or audit the books? How much notice may be required? What if there is a discrepancy? Who pays for the cost of the audit or inspection? All of these points may be negotiated.

While franchisors will want the broadest rights possible with respect to an inspection or audit, franchisees may counter that certain inspection or audit rights are unnecessary and unduly time consuming or burdensome. Moreover, franchisees will want to be able to operate their business without unnecessary or disruptive interruptions caused by inspections or audits. The franchisee will seek to limit the number of inspection or audits within a given time period, as well as insert language requiring some advance or written notice of any

[55] *See, e.g.,* Asbill, Barkoff & Selden, *supra* note 25, at 52.

[56] *See* Olson, Spencer & Weinberg, supra note 11, at 53.

audit or inspection by the franchisor. Franchisors may agree to a compromise that limits the number of inspections, but in turn require the franchisee to cover the expenses of the audit or inspection to the extent it uncovers underreporting of Gross Sales by the franchisee. Often there will be some negotiation regarding the amount of underreporting required to trigger such reimbursement requirement by the franchisee. Franchisee counsel will argue that it should be a material amount, rather than a small discrepancy (which could be due to a rounding or accounting error). Between two percent (2%) and four percent (4%) seems to be where many franchise agreements require the franchisee to cover such costs. The inspection or audit costs typically include reasonable accounting and legal fees and travel expenses, room and board and compensation for franchisor's representatives. Furthermore, franchisors should also make it clear that any such payments are in addition to any other rights or remedies the franchisor may have under the Franchise Agreement.

3. <u>Right to Inspect Franchised Business and Premises</u>

Separate and apart from the right to inspect the franchisee's books and records, the franchisor will need the ability to inspect and/or audit the franchised business and premises. This is the only way that the franchisor can accurately confirm whether the franchisor is conforming to the franchisor's required system standards. Similar to the inspection of books and records, a franchisee may seek to negotiate restrictions and limitations on the franchisor's right of inspection or audit (i.e., require prior notice and only during reasonable hours that will not interfere with operation of franchised business, etc.).

L. <u>Governing Law; Dispute Resolution</u>

The governing law and dispute resolution provisions may be some of the more difficult ones to negotiate even with a startup system. Typically, these provisions are "controlled" by the lawyer drafting the FDD and to which the franchisor typically does not have an opinion (especially startups); and many times will acquiesce to the advice of the professionals. However, a franchisee should still be concerned with the governing law, as to what state laws will apply if so designated, and how that may or may not affect the franchisee in terms of how the franchise agreement will be interpreted and enforced. Keep in mind that many states have additional franchise-related laws and statutes (that were discussed earlier) which may not be waived and will apply no matter what the governing law provision states in the agreement. In such cases, a franchisor may ignore this provision once the governing law has been established and as a result, it may not reflect what is currently best for the franchisor. For example, a franchisor may have a provision that states that the governing law is now at the state which its headquarters are located, even though it has moved its headquarters three times since the provision was last reviewed. A franchisor definitely should be aware of the applicable governing law in its negotiations with franchisees. When a franchisee is reviewing the agreement, it typically believes that the laws of its state should apply but that may not necessarily be of benefit to the franchisee and one should not just simply jump to the conclusion of where the franchisee is located should be the governing law. A franchisee's home state laws may not be as favorable as those of the franchisor.

A bigger issue, but again one that is not often modified through negotiations is the type of litigation - courtroom litigation or arbitration. There are numerous papers discussing the pros and cons to arbitration which will not be addressed in this paper; but, suffice to say, that there are many opinions as to which may be more beneficial and that debate is also true within each subsection of franchisor and franchisee. It used to be a general rule of thumb that a franchisor desired arbitration and a franchisee did not. However, those rules of thumb have somewhat changed, at least in the authors' opinions, and arbitration is not as desirable from a franchisor prospective, and on the franchisee side of the table, there is still debate as to which is more beneficial. The authors are of the belief that franchisees would be better suited in courtroom litigation instead of arbitration given the costs, timing, limited procedures, lack of appeals, etc.

However, items that could be negotiated by the franchisee if arbitration were to be the venue of choice for dispute resolution would be as follows:

1. Arbitration to be held in or near the franchisee's location;

2. Appeal rights to be negotiated into the arbitration provision;

3. Discovery rules such as the Federal Rules of Civil Procedure and Discovery to be incorporated;

4. The arbitration agency to be used whether it be the American Arbitration Association, JAMS or others, and among others;

5. Rights to injunctive relief whether it be through arbitration or the courts;

M. <u>Venue and Jurisdiction and Waivers</u>

In a typical franchise agreement, any action filed by a franchisee is to be filed in the county or district in which the franchisor's principal place of business is located. In addition, a growing trend is for franchisors to compel arbitration instead of courtroom litigation. Furthermore, some agreements compel franchisees to waive such things as jury trial, punitive damages, consequential damages, special damages, etc. There is an ongoing debate regarding those issues even among the franchisee bar.

In general, most franchisee-oriented attorneys (based upon the authors' informal discussions) tend to favor courtroom litigation over arbitration due to the cost factors, abilities to utilize discovery tools and the opportunity for appeals. Obviously, many of these factors can go either way. Venue, however, from a franchisee's perspective should be where the franchisee's principal place of business is located or, at the very least as a compromise, the party bringing the action against the other must file at the principal place of business of the defendant/respondent.

As far as waivers are concerned, why should a franchisee waive "rights" that are "constitutional" (jury trial), or waive general and well accepted principals of law? Punitive damages do not occur on a routine basis. Contrary to public belief and probably based upon the publicity they receive in the media, punitive damages tend to be reserved for egregious conduct. If someone has acted in a way meriting punitive damages, why should they not be sanctioned accordingly? These are typical boiler plate provisions that many franchisors will not negotiate because their lawyers say so and most franchisees will not necessarily "push" these issues even though they could be of benefit to them should a dispute arise.

N. General Provisions

1. Indemnification

Although negotiation of indemnification provisions may go on for several pages and account for a significant portion of time with respect to negotiating purchase or financing agreements, franchise agreement indemnities are not often negotiated. Most standard franchise agreements (to the extent there is such a thing) include indemnification of the franchisor only. The only exception to this general principle may show up the trademark section of a franchise agreement. Some franchisors will indemnify franchisee for losses incurred in connection with a third-party trademark or patent infringement claim.[57] Additionally, the only limitation that may be negotiated (in very rare instances) on indemnification of the franchisor may be with respect to gross negligence or willful misconduct of the franchisor. Franchisors are cautioned against agreeing to such a carve out since it will invariably lead to a franchisee claim of gross negligence or willful misconduct under any circumstance where a claim is made. The exception becomes the rule. Typical indemnification language for a franchise agreement is included below, with the franchisee carve out in brackets:

> *Franchisee agrees to indemnify, defend and hold harmless Franchisor and Franchisor's affiliates and Franchisor's and such affiliates respective officers, directors, shareholders, managers, members, employees, agents and representatives, and their heirs, executors, successors and assigns (collectively, "Indemnitees") of and from any and all claims, counterclaims, demands, actions, causes of action, losses, liabilities, damages, set offs, liens, attachments, judgments, suits, demands, debts, costs and expenses (including, without limitation, attorneys' fees) ("Claims") arising out of or in connection with the operation or condition of any part of the franchised business or its premises, the conduct of business there, (whether or not done in compliance with this Agreement), Franchisee's ownership or possession of real or personal property, any act or omission by Franchisee of or any of its agents, contractors, servants or employees, and Franchisee's breach of any obligation of Franchisee under this Agreement [**except to the extent such Claims are caused directly by the gross negligence or willful misconduct of Indemnitees**.]*

Franchisors should be cautioned against agreeing to such a carve out, since it will invariably lead to a dispute.

2. Guaranty by Franchise Owners

With some exception for well-capitalized franchisees (most notably in the hotel industry), a franchisor will almost invariably require the owners of a franchisee entity to guaranty the payment and performance obligations of the party executing the actual franchise agreement. This is based on the fundamental understanding that the franchise relationship is personal – and the use of a guaranty simply maintains that relationship when an entity is added to the equation. There has been some debate among practitioners for as to whether or not personal guaranties actually provide any real additional benefit above and beyond the obligations of the agreement. As one practitioner noted, "Unless performance of the personal guarantee is itself

[57] Asbill, Barkoff & Selden, *supra* note 25, at 44.

secured by a perfected first security interest in valuable collateral, it is no more valuable than the net worth of the guarantor, and can be broken in a bankruptcy proceeding, if the guarantor is willing to endure the cost and downstream consequences of a personal bankruptcy."[58] This argument, however, assumes that a franchisee is not taking advantage of the situation and withholding royalties or breaching obligations with the knowledge that it has no personal responsibility.[59] Also, while this argument may be compelling to seek to limit the payment obligations of a guarantor, a franchise agreement guaranty typically covers performance obligations (including maintaining confidential system information and restrictions on competition), and indemnification for claims brought by third parties as a result of the franchised business' activities.[60] Arguing against a guaranty of such performance obligations is a difficult position to defend for a franchisee guarantor. Why should the franchise owners not stand behind the performance of the agreement? Why should forming an entity allow franchise owners to circumvent their obligations? Although a personal guaranty of both performance and payment obligations is both reasonable and customary in most instances, franchisors in some very limited circumstances may be amenable to negotiating dollar caps on guarantor liability, as well as time limits that allow the personal guaranty to burn off during the initial phase of the franchise relationship (when the risks are particularly high). Another way to reach a compromise for both parties is to require that the franchise entity maintain certain net worth requirements, with a conditional personal guaranty that triggers only if the financial condition of the franchise entity deteriorates below a certain level.

3. Cross-Default

If a franchisee operates more than one unit or is a party to multiple agreements with the franchisor, providing a cross default provision can serve as an effective "stick" rather than "carrot" approach to compliance. Similar to a general release, cross default provisions may present a significant risk for multi unit operators or area developers and franchisees may try to negotiate or remove this provision altogether. Most franchisors are not likely to concede this point. Franchisors can argue that such a provision allows them to more effectively control the standards of all of their locations and franchisees should not be able to pick and choose agreements with which they must comply. Moreover, franchisees should be able to allocate sufficient resources to all of their locations and units.[61]

Although typical cross-default provisions may contain language that covers any and all agreements between the franchisor or any of its affiliates and the franchisee, some franchisors also cover third party arrangements as well, like leases agreements. Franchisors want the ability to terminate the franchise agreement upon an event of default by the franchisee under its lease. Franchisees may argue that such provision is unduly burdensome and at a minimum it should be limited to breaches beyond all notice and cure periods.

4. Set Off by the Franchisor

Although generally franchisors will prohibit a franchisee's ability to set off any amounts owed to it under the franchise agreement (or any other agreements between the

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[58] Rupert M. Barkoff, *Traditional and Avant-Garde Uses of Personal Guarantees in Franchise Relationships*, 23 WTR FRANCHISE L. J. 137, 138 (2004).

[59] *Id*. at 140.

[60] *Id.*

[61] *See* Olson, Spencer & Weinberg, *supra* note 11, at 60.

parties), franchisors will often explicitly require such a right with respect to any amounts owed by the franchisee under the franchise agreement, or any other agreement between the parties. Contractual common law may already provide the franchisor with such a right, however, franchisors will often negotiate a specific provision to that effect.

5. <u>Discretionary Terms</u>

Negotiation can often focus on a single word, such as “material,” “reasonable,” and “discretion.” They may be used to give comfort to the franchisee, such as, “the approval of a transfer shall not be unreasonably withheld or delayed.” They may also be used to give a seemingly unfettered right to the franchisor, such as, “in the franchisor’s sole discretion.” Franchisor and franchisee counsel alike should be wary of relying on these terms to provide comfort to their clients. The words are subject to interpretation and often times only add uncertainly. The addition of a modifier such as “reasonable” or “material” may move the parties closer to finding a mutually agreeable position on language in the contract, but be mindful of how a single word may add more ambiguity to an obligation or right. It is best in the context of negotiation to determine the specific issue of concern and draft to address such concern, rather than rely on a term that will be subject to interpretation. For instance, franchisees should request a specific time frame by which a franchisor must provide their approval, rather than relying on a general clause that approval shall not be unreasonably delayed.

The term discretion deserves specific mention. Although franchisors may wish to provide training only in their “discretion,” it should be noted that the term “discretion” has become a loaded word that tends to open franchisors to judicial review, such that alternative ways of reserving the franchisor’s options should be employed.[62] Although franchisors and their counsel may be under the impression that the term “discretion” gives the franchisor greater power, they should be aware that it also exposes the franchisor to good faith and fair dealing claims. To address this problem, some drafters have begun using the phrase “reasonable business judgment.” The purpose of that phrase is to give the franchisor some flexibility in its decision-making abilities under the agreement without facing judicial scrutiny of that decision making. More specifically, the franchisor reserves the right to use reasonable business judgment in making decisions that affect the franchisees. Some drafters go even further to disclaim any harm the franchisor’s reasonable business judgment might cause.

Reasonable Business Judgment

Whenever the Franchisor reserves discretion in a particular area or where the Franchisor agrees to exercise its rights reasonably or in good faith, the Franchisor will satisfy its obligations whenever it exercises Reasonable Business Judgment in making a decision or exercising a right. The Franchisor’s decisions or actions will be deemed to be the result of Reasonable Business Judgment, even if other reasonable or even arguably preferable alternatives are available, if the Franchisor’s decisions or actions are intended, in whole or significant part, to promote or benefit the System generally even if the decision or action also promotes Franchisor’s financial or other individual interests. Examples of items that will promote or benefit the System include, without limitation, enhancing the value of the Trademarks, improving customer service and satisfaction, improving product quality, improving uniformity, enhancing or encouraging modernization and improving the competitive position of the System.

[62] *See,* e.g., Killion, *supra* note 39 at 229-30.

6. Definition of "Gross Sales"

An often overlooked provision is the definition of Gross Sales. From a franchisee prospective, the Gross Sales definition should include a provision that provides for the deduction of returns, refunds or the like so long as the revenue was included in a prior calculation of Gross Sales. Also, the definition should not include taxes or similar charges that are paid directly to a third party. Further, there are franchise agreements that provide for Gross Sales not to be based upon revenue collected, but simply calculated upon a "sale." Therefore, the franchisee could have placed a sale on credit or even by credit card and eventually not receive the funds, but would have paid a royalty on such. This should also be addressed by the franchisee.

7. Tax Liability Issues

This is a growing concern for franchisors as state taxing authorities are trying to implement taxes on the receipt of royalty payments by franchisors and, in turn, franchisors are now implementing provisions, akin to, "if any state imposes a sales or other tax on the royalties, then the franchisor has the right to collect this tax from you, the franchisee."

One thought is why is the franchisee responsible for this tax? It is almost the equivalent to an income tax or even a sales tax that is part of the normal course of business in the operation of a franchisor's business and, thus, should be assumed directly by the franchisor. Like all other expenses and taxes, there eventually is a trickle down effect and prices rise which may be so in terms of how a franchisor determines the royalty it charges, but should a franchisee in a particular state be hit with a franchisor's state tax issue? Also, there are issues as to what happens if the franchisor appeals the tax assessment and receives a refund x years later. Does the franchisor refund such to the franchisee? Further, would this then give the franchisor the ability to simply pay the tax imposed because it knows that the franchisee will ultimately pay it or reimburse it and, thus, de-incentivise the franchisor from challenging any such taxes? Again, this is an area that franchisees should keep an eye on and attempt to either delete or modify.

IV. STRATEGIES FOR GETTING TO YES

A. Franchisee and Franchisee Counsel Perspective

There is no hard and fast way to get to "yes" with the franchisor but there are some tactics that can be used to possibly get to "yes." As noted from the outset, there are a number of factors that will go into whether or not a franchisor is willing to negotiate its franchise agreement, including its length of time in business, its size, its desire for a particular franchisee, its desire for a certain geographic location, its desire to open up a certain number of units, its desire to fulfill commitments to its venture capital partners, its desire to fulfill commitments to its credit facilitators and so on and so on. Without knowing what exact "button" needs to be pushed, there are some things that every franchisee contemplating entering into a franchise agreement can do which not only may help them with negotiating a franchise agreement, but also give them a better overall sense of the system and more knowledge into making an informed decision as to whether or not to proceed with the venture. The following are some tips.

1. Research with Current Franchisees

A useful resource is Item 20 of the FDD which provides, usually by an exhibit, the last known address and telephone number of current and terminated franchisees for the past three years. Prospective franchisees should be encouraged to call many, if not all, of these franchisees as part of their own due diligence. One question to ask is whether or not the franchisees were able to negotiate their franchise agreement and, if so, what clauses were negotiated. Keep in mind, however, that just because others were able to negotiate certain provisions does not mean that any particular franchisee or prospective franchisee will be able to obtain the same negotiated terms. However, it is helpful to know what terms have been negotiated in the past and to what extent they were negotiable.

2. Franchisee Counsel Experiences

The most valuable resource at the bargaining table is information. Would it not be nice to know the favorable terms negotiated by existing franchisees? While a franchisor may have its reasons for "discriminating" or favoring one franchisee over another, more often that not it is simply who you talk to, how much discretion they have, how badly the franchisor needs to develop the market, and a multitude of other factors. Franchisees who have done their homework will have a pretty good idea of these market factors, but will have no idea what they are worth to the franchisor. By consulting with experienced franchisee counsel (with the permission of the franchisee), it may be possible to get a peek at the franchisor's cards. Then the franchisee's counsel can just smile when he or she is told, "We don't modify that term for anyone."

3. Redlined Changes to Franchise Agreement

At the bargaining table, the devil is in the details. If franchisee counsel is fortunate enough to meet with the decision maker and/or his or her counsel (both are preferable), any potential compromise on substantive terms will require review of specific language. The best and often the only real opportunity to agree on specific changes is at the bargaining table. Otherwise, the hard fought battle that results in "Okay, we'll consider any language that you send us," will die a slow death on the desk of reviewing counsel.

There is nothing more time consuming than reviewing the entire franchise agreement and preparing redlined changes of those terms the franchisee wants to negotiate. Depending on the franchise and its history of negotiating changes, it may be time well spent.

4. Previous Versions and Other Systems

Another useful tool is to look at previous versions of the franchise agreement and compare and contrast the previous versions to the current version. This will give you some idea as to what the franchisor is living with as to current franchisees and what it may be willing to go back to on a negotiated basis. Also, it may be helpful to compare and contrast competing franchise agreements as a form of bargaining leverage, using language from competitors' agreements as suggested modifications.

5. Market Forces

The franchisor's growth plans as disclosed in its FDD will give the franchisee a good idea of the franchisor's flexibility to compromise on its terms. Another indicator is the growth in the industry and the relative growth of the franchisor's competition. In remote areas of the country or new markets, the franchisor may be more willing to compromise on terms in order to compensate for the lack of name recognition, advertising and marketing reach. In such a case, for example, a franchisor may be willing to shift the funding of a national advertising program to local store marketing until the market reaches the optimal number for media placement. Demand for the franchise will also factor into the franchisor's flexibility on terms.

B. Franchisor Attorney Perspective

Typically, attorneys for franchisors spend significant time and effort, including considerable time working with the client, to prepare and vet a form of franchise agreement for franchisees to sign. As a result, they may be reluctant to negotiate any of the agreement terms for fear of exposing their client to undue risk. Similar to non-franchise transactions, franchisor (and franchisee) lawyers must strike a balance between their desire to protect their client and closing a franchise sale. Lawyers must advocate for their client without creating an impediment to the business. Moreover, refusing to negotiate a franchise agreement or insisting on an agreement that is completely one-sided often creates an environment of mistrust and resentment. Given the length of most franchise relationships, it is important for both sides to feel comfortable with the deal that has been struck at the outset. Notwithstanding the foregoing, negotiating a franchise agreement is not like a typical contract negotiation. A franchisor must protect its brand, and maintaining system wide consistency is imperative to the success of the franchisor. This principle should not be lost on franchisees and their counsel, as the franchisee's success is directly tied to the success of the overall brand. While there may be some flexibility in terms of non-system related terms (i.e. landlord conditional assignments, parties covered by the personal guaranty, etc.), the form and overall substance of the agreement must stay intact.

V. CONCLUSION

The suggested points and strategies throughout this paper hopefully provide insight and understanding as to the reasons why a franchisor or franchisee want certain language in the contract, and what provisions may be negotiable in a typical franchise agreement. However, that does not mean that the franchisor will substantially change the provision or that the franchisee will achieve the position it wants from the negotiations. At the very least, you, as a franchise attorney, are in a position to educate your clients in the process and position them to have a good discussion on various issues of importance. Lawyers have a tendency at times to spend an inordinate amount of time on issues that our clients deem trivial or non-factors. It is, however, the lawyers that know about the "what ifs," enabling counsel to be cognizant of what could happen should certain provisions be left unchecked in the negotiation process. Those that have been practicing in the franchise law area recognize that many prospective franchisees and, to a certain extent, even current franchisees, do not really understand franchising, and the difference between franchising and owning their own businesses. The same can be said for franchisors. It is far too common that a franchisor attorney realizes that their franchisor client does not know their own franchise agreement. Why, because the lawyers or business consultants wrote it and "told" the franchisor "here's your FDD," without explaining it to the franchisor or having the franchisor go through it carefully to make sure that it captures the true essence of the franchise system and as to what the various provisions mean – even if they are so-called "boiler plate."

Being able to negotiate a franchise agreement requires the practitioner to understand franchising in general, the particular franchise system, its agreements and the client. It is the duty of the franchise attorney to be able to explain the franchise agreement and the FDD not only for purposes of trying to negotiate more favorable terms, but to educate the prospective franchisee, or even the renewing franchisee entering into a new agreement under the terms of the “then current franchise agreement.” Some may contend that in order to negotiate, you must have the power and resources of an independent franchisee association; or that you must institute litigation in order to get the franchisor’s attention; or that you must be a multi-unit purchaser for the franchisor to talk to you about negotiating terms. In certain systems, these observations may be true. In others, however, a franchisee with competent franchise counsel can negotiate the agreement on their own even if it is only for one unit. Many factors go into determining whether or not a franchisor will negotiate. On most occasions, no one will even know why the franchisor did or did not negotiate, except the franchisor. In conclusion, using an adage that we use many times with our own children, “You don’t know, unless you ask.”

Exhibit A

State	Restriction on Termination?[1]	Restriction on Non-Renewal?	Additional Comments[2]	Statutory References[3]
Arkansas	Termination for "good cause"	Non-renewal for "good cause" or based on non-arbitrary or non-capricious policies of franchisor	90 days' notice for termination or non-renewal (not required in certain circumstances under "good cause")	ARK. CODE ANN. §§ 4-72-201 to 4-72-210 (CCH Bus. Franchise Guide ¶ 4040)
California	Termination for "good cause" or "reasonable grounds"	Must meet specific requirements in statute for non-renewal	Sufficient notice to cure required for termination (not required in certain circumstances under "reasonable grounds") 180 days' notice for non-renewal Repurchase obligation if termination or non-renewal in violation of law	CAL. BUS. & PROF. CODE §§ 20000 to 20043 (CCH Bus. Franchise Guide ¶ 4050)
Connecticut	Termination for "good cause", voluntary abandonment or criminal conviction	Non-renewal for "good cause", voluntary abandonment or criminal conviction or certain circumstances where Franchisor leases premises to Franchisee	60 days' notice for termination or non-renewal; 30 days' notice if termination for voluntary abandonment; no advance notice if criminal conviction 6 months' notice for non-renewal under certain circumstances where Franchisor leases premises to franchisee and elects not to renew. Repurchase obligation for termination (regardless of reason)	CONN. GEN. STAT. ANN. §§ 42-133e to 42-133h (CCH Bus. Franchise Guide ¶ 4070)

[1] "Good cause" definitions vary among states – several states provide that the reasonable requirements imposed by the franchise agreement may constitute good cause.
[2] There are exceptions to many of the notice provisions required for termination and non-renewal – please refer to state statutes for specific requirements.
[3] These references include statutes related to state relationship laws in general and are not limited to termination and non-renewal. Please refer to specific state statutes for information that may affect the parties' ability to negotiate other terms in certain states (i.e. anti-waiver provisions, non-discriminatory provisions, dispute resolution, etc.)

State	Restriction on Termination?	Restriction on Non-Renewal?	Additional Comments	Statutory References
Delaware	May not terminate "unjustly" (i.e. without cause or in bad faith)	May not refuse to renew "unjustly" (i.e. without cause or in bad faith)	90 days' notice for termination or non-renewal	DEL. CODE ANN. tit. 6, §§ 2551 to 2556 (1980) (CCH Bus. Franchise Guide ¶ 4080)
Hawaii	Termination for "good cause" or in accordance with nondiscriminatory terms/standards of franchisor	Non-renewal for "good cause" or in accordance with nondiscriminatory terms/standards of franchisor	Reasonable period of time required to cure after written notice Unreasonable discrimination against franchisees prohibited Repurchase obligation for termination or non-renewal (regardless of reason)	HAW. REV. STAT. §§ 482E, 482E-6 (CCH Bus. Franchise Guide ¶ 4110)
Illinois	Termination for "good cause"	Must meet certain conditions for non-renewal	30 days' notice and chance to cure required for termination 6 months' notice required for non-renewal (not required in certain circumstances)	815 ILL. REV. COMP. STAT. §§ 705/18 to 705/26 (CCH Bus. Franchise Guide ¶ 4130)
Indiana	Termination for "good cause" or bad faith of franchisee	Non-renewal for "good cause" or bad faith (or if franchise agreement says not renewable or gives conditions to renew)	90 days' notice for termination or non-renewal (except as otherwise provided in franchise agreement)	IND. CODE ANN. §§ 23-2-2.7-1 to 23-2-2,7-7 (CCH Bus. Franchise Guide ¶ 4140)
Iowa	Termination for "good cause" or as set forth in list in statute	Non-renewal for "good cause", mutual agreement or franchisor withdraws from market	30-90 days' notice for termination Six months notice require for non-renewal	IOWA CODE § 537A.10 (CCH Bus, Franchise Guide ¶ 4152)

State	Restriction on Termination?	Restriction on Non-Renewal?	Additional Comments	Statutory References
Michigan	Termination for "good cause" required	Must provide renewal terms available to other franchisees	Must provide notice and reasonable opportunity to cure before termination 6 months' notice required for non-renewal (otherwise subject to repurchase obligation in certain circumstances)	MICH. COMP. LAWS §§ 445.1527 &445.1535 (1989) (CCH Bus. Franchise Guide ¶¶ 4220 & 3220.34 & 35)
Minnesota	Termination for "good cause"	Non-renewal for "good cause" or 180 days' notice (and time for franchisee to recover FMV of franchise)	180 day's notice required if non-renewal without "good cause" 90 days' notice for termination (60 days to cure prior to termination) Notice not required in certain circumstances (voluntary abandonment, criminal conviction, failure to cure material impairment of goodwill)	MINN. STAT. § 80C.14 (1993) and MINN. R. § 2860.4400 (CCH Bus. Franchise Guide ¶¶ 4230 and 5230.31)
Mississippi	Notice only	Notice only	90 days' notice for termination or non-renewal No notice required in certain circumstances (criminal misconduct, fraud, abandonment, bankruptcy, insolvency, or NSF check)	MISS. CODE ANN. § 75-24-51 to 75-24-63 (CCH Bus. Franchise Guide ¶ 4240)
Missouri	Notice only	Notice only	90 days' notice for termination or non-renewal No notice required in certain circumstances (criminal misconduct, fraud, abandonment, bankruptcy, insolvency, or NSF check)	MO. REV. STAT. §§ 407.400 to 407.420 (CCH Bus. Franchise Guide ¶ 4250)
Nebraska	Termination for "good cause"	Non-renewal for "good cause"	60 days' notice for termination or non-renewal 15 days' notice if termination or non-renewal for abandonment No advance notice required if criminal conviction, insolvency, payment default, fraud, danger to public health/safety, loss of right to premises	NEB. REV. STAT. §§ 87-401 to 87-410 (CCH Bus. Franchise Guide ¶ 4270) *only applies if gross sales exceed $35K for 12 months prior to claim

State	Restriction on Termination?	Restriction on Non-Renewal?	Additional Comments	Statutory References
New Jersey	Termination for "good cause"	Non-renewal for "good cause"	60 days' notice for termination or non-renewal 15 days' notice if termination or non-renewal for abandonment No advance notice required if criminal conviction	N.J. REV. STAT, §§ 56:10-1 to 56:10-12 (CCH Bus. Franchise Guide ¶ 4300) *New Jersey's statute applies only if gross sales between Franchisor and Franchisee for 12 months preceding a suit exceed $35,000 and more than 20 percent of Franchisee's gross sales are intended to be derived from the franchise
Rhode Island	Termination for "good cause"	Non-renewal for "good cause"	60 days' notice for termination or non-renewal (including 30 days to cure; 10 days for payment default; 24 hours for health safety violation) No advance notice required in certain circumstances	R.I. GEN. LAWS §§ 6-50-1 to 6-50-9 (CCH Bus. Franchise Guide ¶ 4390)
Virginia	Termination for "reasonable cause"	N/A		VA. CODE ANN. §§ 13.1-557 to 13.1-574 (CCH Bus. Franchise Guide ¶ 4460)
Washington	Termination for "good cause"	Only repurchase obligation in certain non-renewal circumstances	Must provide notice and reasonable opportunity to cure prior to termination Non-renewal requires repurchase obligation if franchisee not given 1 year notice and a waiver of non-compete	WASH. REV. CODE §§ 19.100.180 to 19.100.190 (CCH Bus. Franchise Guide ¶ 4470)
Wisconsin	Termination for "good cause"	Termination for "good cause"	90 days' notice (including 60 to cure) for termination or non-renewal (10 days to cure non-payment) No advance notice required termination or non-renewal for insolvency, assignment for benefit of creditors, or bankruptcy	WIS. STAT. §§ 135.01 to 135.07 (CCH Bus. Franchise Guide ¶ 4490)

Exhibit B

Negotiated Sales and Material Modifications in California

California Corporations Code § 31109.1. Offer or sale of registered franchise on different terms; exemption from disclosure provisions; requirements

(a) There shall be exempted from the provisions of Chapter 2 (commencing with Section 31110) the offer and sale of a franchise registered under Section 31111, 31121, or 31123 on terms different from the terms of the offer registered thereunder if all of the following requirements are met:

(1) The initial offer is the offer registered under Section 31111, 31121, or 31123.

(2) The prospective franchisee receives all of the following in a separate written appendix to the offering circular:

(A) A summary description of each material negotiated term that was negotiated by the franchisor for a California franchise during the 12-month period ending in the calendar month immediately preceding the month in which the negotiated offer or sale is made under this section.

(B) A statement indicating that copies of the negotiated terms are available upon written request.

(C) The name, telephone number, and address of the representative of the franchisor to whom requests for a copy of the negotiated terms may be obtained.

(3) The franchisor certifies or declares in an appendix to its application for renewal that it has complied with all of the requirements of this section, in the event this exemption is claimed.

(4) The negotiated terms, on the whole, confer additional benefits on the franchisee.

(b) The franchisor shall provide a copy of the negotiated terms described in subdivision (a) to the prospective franchisee within five business days following the request of the franchisee.

(c) The franchisor shall maintain copies of all material negotiated terms for which this exemption is claimed for a period of five years from the effective date of the first agreement containing the relevant negotiated term. Upon the request of the commissioner, the franchisor shall make the copies available to the commissioner for review. For purposes of this section, the commissioner may prescribe by rule or order the format and content of the summary description of the negotiated terms required by subparagraph (A) of paragraph (2) of subdivision (a).

(d) For purposes of this section, “material” means that a reasonable franchisee would view the terms as important in negotiating the franchise.

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California Code of Regulations § 310.100.2. Negotiated Sales.

(a) General. The offer or sale of a franchise on terms different from the terms of the offer registered under Section 31111, 31121 or 31123 of the Law is exempt from the requirements of Section 31110 of the Law, if all of the following conditions are met:

(1) The initial offer is the offer registered under to Section 31111, 31121 or 31123 of the Law.

(2) When the prospective franchisee receives the offering circular, he or she also receives copies of all Notices of Negotiated Sale of Franchise filed with the Commissioner within the last 12 months, if any.

(3) Before selling another franchise, the franchisor amends its registered offer to disclose: “The terms of Item(s) _________ of this Offering Circular have been negotiated with other franchisees. A copy of all Negotiated Sales Notices filed in California in the last twelve months is attached as Exhibit _________.” This disclosure should be made in the UFOC Item that was negotiated or in an appendix to the UFOC. This disclosure must be made if the negotiated sale occurred within twelve months of the offering being made. An amendment making only this disclosure is effective when filed.

(4) The Notice of Negotiated Sale of Franchise in the form set forth in subsection (b) is filed with the Commissioner within 15 business days after the negotiated sale is consummated.

(5) The franchisor certifies or declares in an appendix to its application for renewal that all notices have been filed with the Commissioner as required by paragraph (a)(4) (see Section 310.122 of these rules).

(b) The Notice of Negotiated Sale of Franchise required by subsection (a)(4) of this rule shall be filed on the following form:

Department of Corporations
File No. ____________
(Insert file number of currently effective franchise registration)

STATE OF CALIFORNIA
DEPARTMENT OF CORPORATIONS
FRANCHISE INVESTMENT LAW
NOTICE OF NEGOTIATED SALE OF FRANCHISE
UNDER SECTION 310.100.2, TITLE 10,
CALIFORNIA CODE OF REGULATIONS

1. (a) Name of FILER: ____________
   (b) The above-named filer is filing as a (check one):
   ( ) FRANCHISOR ( ) SUBFRANCHISOR
   (c) If FILER is a SUBFRANCHISOR, the name of FRANCHISOR: ____________

2. (a) Name of FRANCHISEE: ____________
   (b) Contact Person: ____________
   (c) Address: ____________
   (d) Telephone: ( ) ____________
3. A. (a) Offering Circular Item Number: ____________
   (b) Description of Provisions in Currently Registered Offering Circular: ____________
   (c) Description of Change: ____________
   B. (a) Offering Circular Item Number: ____________
   (b) Description of Provisions in Currently Registered Offering Circular: ____________
   (c) Description of Change: ____________
   C. (a) Offering Circular Item Number: ____________
   (b) Description of Provisions in Currently Registered Offering Circular: ____________
   (c) Description of Change: ____________
   (If additional space is needed, attach separate sheet(s) with respect to each additional item being changed using the above format)
4. Date of Sale of Negotiated Franchise: ____________
5. Name, title, business address and telephone number of individual to be contacted by the Department regarding this notice:
   Name: ____________
   Title: ____________
   Business Address: ____________
   Telephone: ( ) ____________
6. Date of this notice: ____________

____
Authorized Signature

____
Printed Name of Signatory

California Code of Regulations § 310.100.4. Negotiated Sales Exempt Under Section 31109.1 of the Corporations Code -Summary Description.

The summary description of each material negotiated term required by Corporations Code Section 31109.1(a)(2)(A) shall contain the following content:

1. (a) Offering Circular Item Number:

(b) Description of Provisions in Currently Registered Offering

Circular:

____

(c) Description of Change:

2. (a) Offering Circular Item Number:

(b) Description of Provisions in Currently Registered Offering

Circular:

____

(c) Description of Change:

3. (a) Offering Circular Item Number:

(b) Description of Provision in Currently Registered Offering

Circular:

____

____

(c) Description of Change:

____

California Code of Regulations § 310.122. Registration Renewal Statement.

(a) Applications for renewal of a registration pursuant to Section 31122 of the Code shall be made upon the Uniform Franchise Registration Application, as defined in Section 310.111(b).

(b) The following statement shall be attached as an appendix to the application, if the franchisor has effected any negotiated sales exempt from registration by Section 310.100.2:

I certify (or declare) that all Notices of Negotiated Sale of Franchise have been filed with the Commissioner as required by paragraph (a) (4) of Section 310.100.2 of these rules. Executed at ________________, California, on the date of _________, _____.

____

Name of Franchisor

BY:______________________________________

Signature of Franchisor

Title:______________________________________

____

Printed Name of Signatory

If executed at any place within or without this state; I certify (or declare) under penalty of perjury under the laws of the State of California that the foregoing is true and correct. Executed at ________________, California, on the date of __________, _____.

____

Name of Franchisor

By:_______________________________________

Signature of Franchisor

Title:_______________________________________

California Corporations Code § 31125. Modification of existing franchises; application for registration; written disclosure; exemption

(a) An application for registration of a material modification of an existing franchise or of existing franchises shall be in a form and contain information as the commissioner may by rule prescribe, and shall be accompanied by a proposed disclosure form as specified in subdivision (b). The application may be included with an application pursuant to Section 31111 or 31121.

(b) Except as provided in subdivisions (c) and (d), it is unlawful to solicit the agreement of a franchisee to a proposed material modification of an existing franchise without first delivering to the franchisee a written disclosure, in a form and containing information as the commissioner may by rule or order require, identifying the proposed modification, either five business days prior to the execution of any binding agreement by the franchisee to the modification or containing a statement that the franchisee may, by written notice mailed or delivered to the franchisor or a specified agent of the franchisor within not less than five business days following the execution of the agreement, rescind the agreement to the material modification.

(c) Any modification of a franchise agreement with an existing franchisee of a franchisor shall be exempted from the provisions of this chapter, if all of the following are met:

(1) The franchisee receives the complete written modification at least five business days prior to the execution of a binding agreement, or providing that the franchisee may, by written notice mailed or delivered to the franchisor or a specified agent of the franchisor within not less than five business days following the execution of the agreement, rescind the agreement to the material modification; provided (A) the agreement is not executed within 12 months after the date of the franchise agreement, and (B) the modification does not waive any right of the franchisee under the California Franchise Relations Act (Chapter 5.5 (commencing with Section 20000) of Division 8 of the Business and Professions Code), but the modification may include a general release of all known and unknown claims by a party to the modification.

(2) The modification meets one of the following:

(A) The proposed modification is in connection with the resolution of a bona fide dispute between the franchisor and the franchisee or the resolution of a claimed or actual franchisee or franchisor default, and the modification is not applied on a franchise systemwide basis at or about the time the modification is executed. A modification shall not be deemed to be made on a franchise systemwide basis if it is offered on a voluntary basis to fewer than 25 percent of the franchisor's California franchises within any 12-month period.

(B) The proposed modification is offered on a voluntary basis to fewer than 25 percent of the franchisor's California franchises within any 12-month period, provided each franchisee is given a right to rescind the modification agreement if the modification is not made in compliance with paragraph (1) of subdivision (c).

(d) Any modification of a franchise agreement with an existing franchise of a franchisee shall be exempted from this chapter if the modification is offered on a voluntary basis and does not substantially and adversely impact the franchisee's rights, benefits, privileges, duties, obligations, or responsibilities under the franchise agreement.

(e) For purposes of this section, “California franchise” means: (1) an existing franchise of a franchisee with any location in this state from which sales, leases, or other transactions between the franchised business and its customers are made or goods or services are distributed, or (2) an existing franchise of a franchisee that is a resident of this state and that owns, controls, or has an equity interest in the franchise.

(f) A franchisor shall not make modifications in consecutive years for the purpose of evading the 25 percent requirements set forth above.

California Code of Regulations § 310.125. Application for Registration of a Material Modification of Existing Franchises.

An application for registration of a material modification of franchises pursuant to Section 31125 of the Code shall, in addition to the facing page of the Uniform Franchise Registration Application, as defined in Section 310.111(b), continue on the following form:

EXHIBIT 1

Attach a copy of the item(s) of the Uniform Franchise Offering Circular, complying with Section 310.114.1 of these rules, if the information is changed. State the existing arrangement and the new arrangement with respect to the item(s). The cover of the Offering Circular shall state: “The changes set forth herein are voluntary. If a franchisee does not receive the attached disclosure at least five business days prior to the execution of a binding agreement, the franchisee may, by written notice, mailed or delivered to the franchisor or (specify agent of the franchisor), within five business days following the execution of the agreement rescind the agreement to the modifications.”

Describe the proposed modifications, including:

(a) An identification of the section of the franchise contract or document being modified.

(b) The nature of the modification.

(c) Whether additional cost will accrue to the franchisee and, if so, an estimate of the additional cost.

(d) State the effect on a franchisee who accepts the change and on a franchisee who does not accept the change.

EXHIBIT 2

Attach a copy of the franchise contract or document which embodies the modification(s).

EXHIBIT 3

State the number of franchises presently operating, the number of such franchises presently operating in California and the number of franchises proposed to be modified and the number of franchises proposed to be modified in California.

EXHIBIT 4

Attach the Consent to Service of Process if required by Section 31155 of the California Corporations Code, if one has not previously been filed.

EXHIBIT 5

The applicant has duly caused this application to be signed on its behalf by the undersigned, thereunto duly authorized.

____

(Applicant)

By___________________________________

____

(Title)

I certify or declare under penalty of perjury that I have read this application and the exhibits thereto and know the contents thereof, and that the statements therein are true and correct. Executed at___________________, California, on the date of ____________, ______

____

(Signature)

If executed at any place within or without this state: I certify (or declare) under penalty of perjury under the laws of the State of California that the foregoing is true and correct. Executed at _____ ____, on the date of ___________, ____

Signature ___________________________

HARRIS J. CHERNOW

Harris J. Chernow is a member of Chernow Kapustin, LLC, with offices in Pennsylvania, New Jersey, Maryland, and South Carolina, representing franchisors, master franchisors, area developers, multi and single unit franchisees and others in franchising and retail distribution throughout the United States. Harris's franchise practice includes franchise transactional, disclosure, regulatory, compliance and dispute resolution matters. By virtue of a broad base of legal experience, he also serves as "general counsel" to his clients by coordinating and overseeing other attorneys and matters. Harris has received a number of honors including being selected by *Franchise Times* as a "Legal Eagle" and "Hotshot Franchise Lawyer", Pennsylvania law weekly one of "Fifty on the Fast Track", and as a "Super Lawyer" by *Law & Politics* and *Philadelphia Magazine*. He has also been appointed to the CPR panel of distinguished neutrals Franchise Mediation Panel. Harris, as a result of his balanced approach, is routinely selected as a mediator and an arbitrator (as a neutral and party appointed) for franchise and business disputes.

Harris served on the American Bar Association Forum on Franchising ("Forum") Governing Committee and served as its Finance Officer. He has also served on the Forum's Publications Committee and was chair of its Litigation and Alternative Dispute Resolution ("LADR") Division. He serves as co-chair of the Montgomery County Franchise Law Committee, served twice on the Forum's Nominating Committee for the Board of Governors of the Forum and was on the International Franchise Association's ("IFA") Legal Symposium Task Force. He is an active member of the Forum, the New Jersey Bar Association's Franchise Law Committee, the Philadelphia and Montgomery County Franchise Law Committees, and the International Franchise Association, among others.

KERRY J. OLSON

Kerry Olson is Vice President and Assistant General Counsel for International Dairy Queen, Inc., based in Minneapolis, Minnesota. As part of her responsibilities at DQ, Kerry provides franchise and legal support to the international division. She has done extensive work with matters in China, Thailand, Saudi Arabia and Egypt, and is in the due diligence phase of several new countries on slate for development in the upcoming years. Before joining Dairy Queen, Kerry was Associate General Counsel at Buffalo Wild Wings, Inc., for two years and in private practice for over four years at the Minneapolis law firm of Gray Plant Mooty, where she specialized in franchise corporate counseling and worked with franchisors in the retail, restaurant, hospitality and service-based industries. Kerry is a frequent speaker locally and nationally on topics related to franchising and is an active participant in the franchise community and industry, holding several leadership roles. Currently, she is a member of the American Bar Association's ("ABA") Forum on Franchising and serves on the Steering Committee of the International Franchise and Distribution Division. She also is an active member of the International Franchise Association, with leadership roles as the Chair of the Women's Franchise Committee from 2009 to 2011 and prior to that, as Chair of the Legal Legislative Committee from 2007 to 2009. She also served on the IFA Convention Committee in 2010 and on the Task Force for the 2007 and 2008 IFA Legal Symposia.

In 2011, Kerry was honored as part of the "40 under Forty" list published by the *Minneapolis St. Paul Business Journal.* She was named a "Rising Star" of Minnesota lawyers for 2006, 2007, 2008 and 2009 by *Minnesota Law and Politics* magazine and listed as a "Legal Eagle" by *Franchise Times* in 2006, 2007 and 2008. Recently, *Franchise Times* named Kerry as one of "20 to Watch" in 2010. Kerry graduated summa cum laude, Phi Beta Kappa, from St. Olaf College in 1997. She earned her law degree, magna cum laude, from the University of Minnesota Law School in 2000, where she was awarded membership in Order of the Coif.

Rebekah Prince

Rebekah Prince is Counsel at Eisner, Kahan & Gorry, a professional corporation, in Beverly Hills, California. Rebekah's practice includes franchise and distribution law, as well as business and finance, with a strong emphasis on mergers, acquisitions and related financings. She advises clients regarding domestic and international franchise ventures, including registration and disclosure issues and development of franchise systems. Rebekah is a member of the American Bar Association's Forum on Franchising and served on the Forum's 2012 Nominating Committee. She also served as the ABA Young Lawyers' Division Liaison to the Forum on Franchising Governing Committee from 2009 to 2011 and is currently a member of the Forum's Publications Committee. She is a member of the State Bar of California's Franchise Law Committee where she served as the secretary from 2009 to 2011.

Rebekah was listed in *Chambers USA: America's Leading Lawyers for Business®, Franchising* in 2011 and 2012 as an up-and-coming young lawyer. She was listed as a "Legal Eagle" by *Franchise Times* in 2010, 2011 and 2012. Rebekah graduated from Washington & Lee University with a B.S. in Accounting and earned her law degree from the University of Texas at Austin.