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FEDERAL TRADE COMMISSION

REVIEWING THE FRANCHISE RULE

TUESDAY, NOVEMBER 10, 2020

1:00 P.M.

VIRTUAL EVENT

First Version

Reviewing the Franchise Rule - Workshop

11/10/2020

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1 P R O C E E D I N G S

2 - - - - -

3 (1:02 p.m.)

4 MS. TODARO: Good morning, and welcome to  
5 reviewing the Franchise Rule, an FTC Virtual Workshop.  
6 My name is Christine Todaro, and I'm the FTC's  
7 Franchise Rule Coordinator.

8 On behalf of the entire FTC Workshop team,  
9 we are delighted that you are joining us here today  
10 via our live webcast. Before we begin, I have a few  
11 administrative details to cover.

12 First, a video recording and transcript of  
13 these proceedings will be available on our workshop  
14 event page soon. Second, as with any virtual event,  
15 we may experience technical issues. If these occur,  
16 we ask for your patience as we work through them.

17 Finally, we will be accepting audience  
18 questions via our dedicated email address,  
19 franchiserule@FTC.gov. Due to time constraints, we  
20 may not be able to get through all the questions we  
21 receive, but we will review all of them.

22 Now, I am pleased to introduce the director  
23 of the FTC's Bureau of Consumer Protection, Andrew  
24 Smith.

25

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Reviewing the Franchise Rule - Workshop

11/10/2020

1 WELCOME AND INTRODUCTORY REMARKS

2 MR. SMITH: Thank you, Christine. Welcome  
3 to "Reviewing the Franchise Rule," An FTC Virtual  
4 Workshop. My name is Andrew Smith. I'm the Director  
5 of the FTC's Bureau of Consumer Protection.

6 Today's workshop features three panels  
7 presenting franchisor, franchisee, and regulator  
8 perspective on key Franchise Rule issues, as well as  
9 opening remarks from Congressman and McDonald's  
10 franchisee, Kevin Hern. I would like to thank  
11 Congressman Hern and each of the panelists for helping  
12 to make this virtual workshop possible.

13 Let me start today's discussion by giving  
14 some background on why we're here. The franchising  
15 business model is an important one. It enables  
16 individuals to develop small businesses without having  
17 to start from scratch and franchisors to expand their  
18 reach and serve new customers. In fact, the  
19 International Franchise Association estimates that  
20 there are more than 733,000 franchise establishments  
21 that employ more than 7.5 million individuals.  
22 Nevertheless, joining a franchise system isn't without  
23 risk.

24 The primary purpose of our Franchise Rule,  
25 which was adopted by the Commission in 1978 and last

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1 amended in 2007, is to provide prospective franchise  
2 purchasers the material information they need in order  
3 to weigh the risks and benefits of such an investment.  
4 Accordingly, the Rule requires franchisors to provide  
5 prospective purchasers with 23 items of key  
6 information about the franchise in the form of a  
7 franchise disclosure document, also known as an FDD.

8           The FTC's Franchise Rule is, thus, a presale  
9 disclosure rule, which was designed to address  
10 deception in the offer and sale of franchises. The  
11 Rule does not regulate the substantive terms of the  
12 franchisor/franchisee relationship, nor does it  
13 require the franchisor to register or file any  
14 documents with the Commission.

15           The FTC routinely reviews its rules to seek  
16 information about their costs and benefits, as well as  
17 their regulatory and economic impact. We are here  
18 today because of the FTC's ongoing review of the  
19 Franchise Rule.

20           Last year, we requested public comment on  
21 the Franchise Rule and received 39 comments in  
22 response. I'd like to thank those who took time to  
23 comment. Your input is critical to the review  
24 process. While all commenters suggested that there is  
25 a continuing need for the Rule, some commenters

1 proposed modifications they believe would make the  
2 Rule more effective. And now, after considering those  
3 comments, we are hosting this workshop and seeking  
4 additional public comment until December 17 on the  
5 issues discussed today.

6 The goal of today's workshop is to dive more  
7 deeply into three topics that were raised by several  
8 commenters. The first panel, Financial Performance  
9 Representations: What Should be Disclosed? And Why?,  
10 will focus on whether the current Item 19 disclosures  
11 are effective or whether additional or modified  
12 disclosures are necessary to prevent deception in the  
13 marketplace.

14 The second panel, A Discussion of  
15 Disclaimers, Waivers & Questionnaires, will address  
16 their use by franchisors and whether such use  
17 undermines any of the rule's protections.

18 The final panel, The Pros and Cons of the  
19 Current FDD Format, will explore whether the format of  
20 the FDD can be improved to take into account  
21 technological advances or otherwise make the FDD more  
22 readable.

23 I anticipate a lively and informative  
24 discussion. Each panel includes relevant  
25 stakeholders' perspectives, and I look forward to

1 hearing what each of them has to say.

2 Now, I'd like to introduce Congressman Kevin  
3 Hern from Oklahoma. Congressman Hern is a franchisee  
4 himself gaining expertise in the industry by owning  
5 several McDonald's franchises in the Tulsa area and  
6 employing hundreds of people. He has also held  
7 various leadership positions within the McDonald's  
8 system.

9 In addition, Congressman Hern serves on the  
10 House Small Business Committee, where he is the  
11 ranking member on the Economic Growth, Tax, and  
12 Capital Access Subcommittee. This subcommittee deals  
13 directly with franchises and franchisors as they seek  
14 to obtain capital.

15 Please join me in welcoming Congressman  
16 Hern.

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Reviewing the Franchise Rule - Workshop

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1                                    OPENING ADDRESS

2                            CONGRESSMAN HERN: Thank you, Andrew.

3                            And as mentioned, I'm a U.S. Congressman  
4 from Oklahoma's First Congressional District here in  
5 the Tulsa area. For over 30 years, I've been involved  
6 in the McDonald's franchisee program.

7                            After spending a year as an aerospace  
8 engineer, a job that was cut short by the Space  
9 Shuttle Challenger disaster, I had the opportunity to  
10 get into the program by working for a longtime  
11 franchisee who owned six restaurants in the Little  
12 Rock, Arkansas area. At the time, he was the chairman  
13 of the Owner-Operator Leadership Group that was for  
14 all the 4,000 U.S. franchisees at that time. His role  
15 -- early on for me in my career at McDonald's at that  
16 time, his role allowed me to see how the relationship  
17 -- having a good relationship between the franchisors  
18 and the franchisees is extraordinarily important to  
19 the overall success of any franchise brand.

20                            For 10 years, I worked in the various  
21 management roles coming through all the different --  
22 from entry-level management all the way to Director of  
23 Operations for a multi-unit organization and worked 10  
24 years to save \$100,000 to get my first McDonald's  
25 restaurant. I became a McDonald's franchisee in 1997,

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1 and since that time, in almost 24 years, I've owned 24  
2 McDonald's restaurants.

3 So now I have five left and my family runs  
4 those here in the Tulsa area. And, you know, prior to  
5 running for Congress in 2017, I served for 13 years on  
6 the McDonald's National Leadership Council. The first  
7 eight years of that, I was the Chairman of the  
8 Franchise Relationship Team and five as the Chief  
9 Financial Officer for the McDonald's franchisee  
10 organization. As the chairman of the Franchise  
11 Relations Team, I saw firsthand how a firm but fair  
12 franchise agreement not only protected the  
13 intellectual property of the franchisor, but also the  
14 equity of the franchisees.

15 My corporate counterparts were the Chief  
16 Financial Officer and the Senior Vice President of  
17 Franchising for McDonald's in the USA. For a period  
18 of almost 13 years, I was involved in almost every  
19 franchise agreement issue that developed across the  
20 United States among the almost 4,000 franchisees. In  
21 fact, I've often said that franchising relationships  
22 are much like the interactions of the states with the  
23 Federal Government. The people are best represented  
24 by our republic when they -- each entity, the state  
25 and federal and the franchisor/franchisee -- stays in

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1 their appropriate lanes of responsibilities of  
2 oversight and acts within its limitations of good  
3 governance.

4 I have reviewed literally hundreds of  
5 franchise agreements over the past 20-plus years of  
6 competitors, just to see how they benchmark against  
7 the McDonald's franchise agreement and also as a  
8 potential investor in other franchise brands. I've  
9 looked at these across all industries, and I will tell  
10 you this firsthand, that none are perfect. Most all  
11 are different.

12 It's incumbent upon each party to desire a  
13 strong partner. Therefore, an FDD must be restrictive  
14 enough to create a natural selection process of only  
15 the best franchisee candidates for that particular  
16 brand. Once the franchisee agrees to the terms of the  
17 FDD, it is necessary for all parties to work within  
18 that document as the relationship moves forward.

19 I have spoken a lot over the past three  
20 years about the similarities of the franchising model  
21 as compared to the U.S. Government. The relationship  
22 between states and the Federal Government is bound  
23 together by the framework of the U.S. Constitution.  
24 We have elected politicians that debate the very  
25 merits of these ideas contained in our great doctrine.

1 I see that firsthand today.

2           Also, the relationship between the  
3 franchisees and the franchisor is bound together by  
4 initially the FDD and, ultimately, the franchise  
5 agreement. Most of the brands have elected  
6 representatives that debate the merits of the ideas  
7 contained in their franchise agreement. So as you go  
8 about your work in reviewing possible updates to the  
9 FDD, I would ask that you keep the thought in mind  
10 that there must be a balance in the responsibility as  
11 to each party in the relationship.

12           Each franchisor needs to represent or sell  
13 its brand to the prospective buyer without  
14 overpromising or misleading the potential franchisee.  
15 The franchisee needs to take necessary steps to do the  
16 proper due diligence in making what will be most  
17 likely the greatest career change they will ever  
18 experience.

19           There is a natural tendency for those with  
20 very little franchising experience to pick sides. And  
21 I will tell you from years of experience, only the  
22 brands that work together will see long-term  
23 sustainable success. As with life, there will never  
24 be a relationship that doesn't experience  
25 disagreements. There are remedies for the franchisees

1 and the franchisors when those disputes develop, as  
2 both sides seek protections of their assets, the  
3 franchisor, in trying to select the top-notch  
4 franchisees to grow their brands and increase overall  
5 system value for the stakeholders, and the franchisee,  
6 who is looking for incredible rewards in return for  
7 their investment of cash, hard work, and risk taking.

8 I believe the current FDD has functioned  
9 effectively over the past decade, and I would  
10 encourage you to implement very few changes during  
11 this review. A couple of small changes that I would  
12 suggest that would be for you to look at might be  
13 having brokers to disclose what level of commission  
14 they're receiving for each brand they're recommending  
15 to potential franchisees. This would allow the  
16 prospective owner to determine if there was any undue  
17 influence for the recommendations that might be made  
18 by the broker.

19 And have all the franchisees put their FDDs  
20 online. I think that's one of the panels today, using  
21 technology. So it would be easier to search for  
22 specific topics that might help the prospective owner  
23 make a more informed decision, and for all, a more  
24 robust updating of the FDD as the mandated period, as  
25 set forth by the FTC.

1                   Finally, I would say franchising has been a  
2 life changer for so many, including myself. It  
3 allowed a person like me, who grew up very poor, to  
4 work hard, take risk, and become extraordinarily  
5 successful. I want to thank you for allowing me to  
6 share my thoughts on the importance of franchising and  
7 the franchising model. It's given thousands of  
8 aspiring businesspeople the opportunity to realize the  
9 American dream.

10                   Thank you.

11                   And, Andrew, thanks again for allowing me to  
12 be on here today.

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1 FINANCIAL PERFORMANCE REPRESENTATIONS: WHAT SHOULD  
2 BE DISCLOSED? AND WHY?

3 MS. TODARO: Thank you very much,  
4 Congressman Hern, and thank you to everyone joining us  
5 for our first panel of the day, Financial Performance  
6 Representations: What Should be Disclosed? And Why?

7 My name is Christine Todaro. And I'm an  
8 attorney in the FTC's Division of Marketing Practices  
9 and also the FTC's Franchise Rule Program Coordinator.

10 This panel will explore some of the comments  
11 about financial performance representations that the  
12 FTC received last year. If we have time, I will try  
13 to incorporate questions we receive from viewers.  
14 Please submit those questions to franchiserule@  
15 FTC.gov.

16 We have a lot to cover, but I would first  
17 like to briefly introduce our esteemed panelists. I  
18 highly recommend you review each of their bios on our  
19 event page to learn more about their impressive work.

20 First, Dale Cantone is an Assistant Attorney  
21 General for the State of Maryland and a Deputy  
22 Securities Commissioner, as well as the Chief of the  
23 Franchise and Business Opportunity Unit for the  
24 Maryland Securities Division. Mr. Cantone also served  
25 as the Chair of the Franchise and Business Opportunity

1 Committee and Project Group of the North American  
2 Securities Administrators Association.

3 Susan Grueneberg is a partner at the law  
4 firm of Cozen O'Connor and a certified specialist in  
5 franchise and distribution law by the State Bar of  
6 California.

7 Justin Klein is a partner at the law firm of  
8 Marks & Klein, where he represents both franchisees  
9 and franchisors.

10 Keith Miller is the founder of Franchisee  
11 Advocacy Consulting. And he also serves as the  
12 Director of Public Affairs and Engagements for the  
13 American Association of Franchisee Dealers and he is  
14 also the Director of the Legislative Affairs for the  
15 Fair Franchising Initiative. In addition, he's a  
16 Subway franchisee.

17 Sandy Wall is of counsel at DLA Piper. She  
18 previously served as in-house counsel for McDonald's  
19 and Sears Roebuck.

20 Thank you, panelists, for joining us.

21 On behalf of myself and the panelists, I  
22 would like to note that the views we express today are  
23 our own and do not necessarily reflect the views of  
24 the Commission or any one particular organization, law  
25 firm, or company.

1 I'd like to start today's discussion by  
2 talking about the issue of mandatory financial  
3 performance representation, also known as FPRs. Many  
4 of you may recall that the FTC previously considered  
5 whether to mandate FPRs and ultimately decided not to  
6 when it amended the Rule in 2007. In reaching this  
7 decision, the Commission considered several different  
8 arguments in favor of and against mandatory FPRs. I  
9 would like to frame today's discussion on mandatory  
10 FPRs by going through some of those arguments and  
11 asking the panelists what, if anything, has changed  
12 since the Commission chose not to mandate FPRs several  
13 years ago.

14 First, we often hear that FPR data is the  
15 single most important piece of information to  
16 prospective franchisees. During the last Franchise  
17 Rule review, an estimated 20 percent of franchisors  
18 provided FPRs in their FDDs. That's a franchise  
19 disclosure document. The Commission noted that  
20 prospects could thus find a franchise that made FPRs  
21 if they wanted to. The FTC also noted that ordinary  
22 market sources might compel more franchisors to  
23 disclose without government regulation.

24 Now, IFA estimates that 66 percent of  
25 franchisors make FPRs in their FDDs. My first



1 question is does the fact that 66 percent of  
2 franchisors, if we assume those numbers are correct,  
3 now disclose FPRs affirm the Commission's thinking and  
4 weigh against mandating FPRs?

5 Dale, I'll ask you to respond first.

6 MR. CANTONE: Thank you, Christine, and  
7 thanks for the opportunity to participate in this  
8 workshop. There's no question that 60 percent -- and,  
9 by the way, 60 percent is closer along the statistics  
10 that my State of Maryland and other registration  
11 states are experiencing. Sixty percent is certainly  
12 better than the 20 percent or the 10 percent that we  
13 had seen prior to 2000. So that's definitely a  
14 positive trend.

15 But that still leaves around 40 percent or  
16 somewhat close to 40 percent of prospective  
17 franchisees that are left without the disclosure item  
18 that is certainly what most prospective franchisees  
19 desire most and is, arguably, one of the most  
20 important parts of the disclosure document. So we're  
21 currently left, you know, in a regulatory scheme that  
22 allows a franchisor who, with a failing system in  
23 which franchisees are losing a lot of money, to simply  
24 choose not to disclose financial performance  
25 representations.

1                   And the FTC did go through an analysis in  
2   2007, and there are reasons why they chose not to  
3   mandate FPRs at that time. Some of those reasons, you  
4   know, exist in this day. There is an additional cost  
5   to a franchise system for compiling financial  
6   performance data. However, 60 percent of franchisors  
7   have managed to figure out a way to absorb those  
8   costs. And that also doesn't really take into account  
9   the cost to prospective franchisees who have to put  
10  together a business plan of their own, and there's got  
11  to be increased costs for coming up with a business  
12  plan without that most important data.

13                   Then, also, one of the reasons the FTC  
14  decided not to mandate this disclosure is the  
15  perceived availability of getting financial  
16  performance data elsewhere. And while there are  
17  different avenues for obtaining financial performance  
18  information, noting could compare having an Item 19.  
19  One of the methods is to contact existing and former  
20  franchisees, but that's easier said than done in many  
21  cases. It sometimes works in some systems, but there  
22  are other systems where it's very difficult for  
23  prospective franchisees to get financial information  
24  from existing franchisees, who may simply choose not  
25  to disclose that information.

1           So the costs are there, but if you do a  
2 cost-benefit analysis, the benefits of requiring this  
3 disclosure -- which, again, everybody agrees is the  
4 single most important piece of information that  
5 prospective franchisees want the most -- far outweighs  
6 the -- the benefits far outweigh the costs that there  
7 might be to franchise systems. And some of those  
8 costs are, quite frankly, a little overstated. A lot  
9 of franchisors collect data directly from their  
10 franchisees and probably even more so now than they  
11 did in 2007. And they could be doing that directly  
12 through POS systems.

13           So for the vast majority of franchise  
14 systems, they already have the data. And, in fact,  
15 some of them, who choose not to make an FPR to  
16 prospective franchisees, end up making FPR-type  
17 disclosure to banks to facilitate loans. So it's a  
18 really important disclosure. And on a cost-benefit  
19 analysis, in my own personal opinion, it's the  
20 disclosure that really should be made to prospective  
21 franchisees, and not requiring it is bad for  
22 prospective franchisees and it's bad for franchising  
23 in general.

24           MS. TODARO: Thank you, Dale. And we're  
25 going to go through some of the other considerations,

1 like the costs, liability, and other issues that you  
2 raised. But, right now, I want to stick to this 66  
3 percent disclosing FPRs, and I want to follow up with  
4 Susan.

5 In your opinion, does the fact that 66  
6 percent currently disclose weigh against the  
7 Commission mandating FPRs?

8 MS. GRUENEBERG: Well, thanks, Christine.  
9 And, again, thank you for inviting me to be a panelist  
10 today.

11 I agree with what both and you Dale said  
12 about this information, financial performance  
13 representation probably being the most important  
14 information that a prospective franchisee wants and a  
15 franchisor wants them to have. I disagree with the  
16 conclusion that if a franchisor is not disclosing a  
17 financial performance representation, it's probably  
18 hiding something and it's probably hiding the fact  
19 that the system isn't making money.

20 I think the anecdotal reasons you see for  
21 franchisors deciding not to make FPRs, in my  
22 experience, is, number one, their brand may be so  
23 strong they don't need to. Number two, there may be  
24 sufficient information out there in the marketplace  
25 through existing franchisees and other sources. Or in

1 many, many cases, it may be an emerging franchise  
2 system, and they feel they don't have enough data or  
3 reliable enough data to make an FPR going into  
4 franchising, or in the early stages.

5           If you think about it, it make no sense to  
6 maintain a system of franchises that are not making  
7 money and make the argument that the initial fee is  
8 what you're after. Because a franchisor is not making  
9 its revenues based on the initial fee. That is  
10 initial fee goes to providing the pre-opening  
11 obligations that the franchisor has and they go to a  
12 broker, in large part. And it's the ongoing revenues,  
13 it's the ongoing stream of royalties or other payments  
14 that makes a healthy franchise system, and for that  
15 you need healthy franchisees as well.

16           So again, I realize I view all of this  
17 through the prism of a lawyer who primarily represents  
18 franchisors, but we all have our own prisms, and  
19 that's why we're here today. For me, I would not look  
20 at it as an argument of market forces, but, rather, is  
21 this information important to mandate? Of course,  
22 your initial reaction is yes. But then you have to  
23 ask yourself, can you do that without resulting in  
24 some FPRs that are misleading or that don't have a  
25 reasonable basis? And after you start thinking about

1 it, the exceptions sometimes tend to be overwhelming.  
2 And are we even thinking of everything we should be  
3 thinking of?

4 Of course, we're talking about ramp-up and  
5 all of that. But I'm more of a mind that if you are  
6 going to encourage FPRs, market forces comes in on a  
7 very important basis when you look at what's being  
8 disclosed because that's going to vary. What's  
9 reasonable in different industries is going to be  
10 different. And so it's very difficult to go into it  
11 and think, oh, we can just mandate gross revenues or  
12 we can tell everybody to do breakeven in Item 19.  
13 That's just not going to work, in my opinion.

14 MS. TODARO: Thank you.

15 Sandy, to follow up on what Susan just said  
16 about market forces, is it your impression or  
17 understanding that the trend will continue, that more  
18 franchisors will continue to disclose, or do you agree  
19 with Susan that there are reasons why some franchisors  
20 just won't be making FPRs?

21 MS. WALL: Again, thank you for having me  
22 here today, Christine. It's a little of both. I  
23 think, again, we're all in agreement that providing an  
24 FPR and an FDD is good for the franchisor and good for  
25 the franchisee. But there are clear reasons, as Susan

1 pointed out, why a franchisor may be unable to do  
2 this.

3 Another example is, you know, you've got an  
4 international company that has been doing business  
5 outside the United States and coming into the U.S.,  
6 has no U.S. operating history. If you mandated an  
7 FPR, you would basically be saying that they can't  
8 franchise in the U.S. without having U.S. operations  
9 here. You know, clearly mandating this would be a  
10 barrier to entry of certain franchise systems.

11 And as Susan pointed out, the exceptions --  
12 you know, there would have to be vast lists of  
13 exceptions. In addition, since exceptions won't cover  
14 every circumstance, the FTC would have to be prepared  
15 to issue opinions on certain circumstances so that  
16 certain companies could be exempted out of the FPR  
17 requirement. Again, something that's going to take  
18 valuable time and resources while, again, most  
19 franchisors choose to do this in their -- you know,  
20 for many, many reasons.

21 And, again, one thing -- and I understand,  
22 Dale, your position on -- you know, that it's because  
23 people -- you know, franchisors may be hiding  
24 information. And, you know, there are bad actors  
25 everywhere in the world from time to time, and there

1 may be a small percentage of franchisors that don't  
2 provide information for that reason. But franchisees  
3 have choice. A franchisee who does not get an FPR,  
4 does not get the information from a franchisor, can  
5 always elect not to buy the franchise. This is  
6 important information and if they can't -- they don't  
7 feel comfortable that they can get this information  
8 through other sources, or they're not comfortable with  
9 the reason why the franchisor says they cannot provide  
10 this information, they don't need to proceed.

11 MS. TODARO: Okay. Well, that's actually a  
12 great segue into the next topic that I'd like to talk  
13 about. Another factor that was considered was whether  
14 mandatory FPRs would reduce the level of false  
15 earnings claims made to prospective franchisees.

16 And my next question goes to Keith. Do you  
17 have a sense of how prevalent false claims about  
18 financial performances are, and what evidence would  
19 you use to support your position?

20 MR. MILLER: Well, again, thanks, Christine,  
21 and thanks for all the staff at the FTC for putting  
22 this together.

23 When looking at false or unsubstantiated  
24 claims outside of the FDD, I think we first have to  
25 understand that no prospective franchisee is going to



1 buy a franchise without some understanding of revenue  
2 and cost information. Knowing that about 34 percent  
3 or 40 percent of franchises put nothing in the Item 19  
4 makes me assume that those franchisees of these brands  
5 are getting information outside of the FDD. Of  
6 course, that doesn't make that information false, but  
7 it also doesn't mean that a franchise giving Item 19  
8 data isn't giving information beyond what's in the  
9 FDD.

10 And, you know, the information isn't always  
11 direct information. For example, one brand I worked  
12 with in this last year that captured a lot of news  
13 stories seemed to float 1.5 million as a revenue  
14 number. Every franchisee I talked to gave that  
15 number. Some of them got it direct, but, for most, it  
16 was actually more subtle. As they were talking about  
17 how they would build out the store and what would be  
18 in the restaurant, they were told, well, you have to  
19 put in a Coke freestyle machine because that was what  
20 was required for a \$1.5 million operation. Same with  
21 other build-out and equipment requirements, that they  
22 were told, well, we have to do this to build for a  
23 \$1.5 million operation, yet not a single unit ever  
24 reached that number.

25 You know, I try to tell people that the only

1 financial information you should trust and believe is  
2 what is in the FDD. Everything outside of that can  
3 be suspect, especially if it's verbal or implied. And  
4 I would also argue that franchisors who avoid giving  
5 even basic revenue and cost data -- you know, when we  
6 talk about the fear of giving these numbers, I think  
7 people get more into the weeds and want to talk about  
8 EBITDA type numbers, which would be great. But I  
9 think that's a big step and I think even some even  
10 basic revenue data and cost data probably needs to be  
11 required.

12 And the reason someone buys a franchise is  
13 because that brand has supposedly been tested and  
14 proven as a business model. Now, that doesn't mean or  
15 guarantee any success. But for franchisors who can't  
16 show the data that the model was proven, I would ask  
17 why they're franchising. You know, the intent of the  
18 Franchise Rule is to protect the consumer, the  
19 prospective franchisee. Yet, often, discussions on  
20 the rule seem to get steered towards protecting the  
21 franchisor from liability. The franchisor is the one  
22 with all the resources and leverage.

23 And, you know, I would kind of end this part  
24 of how prevalent it is -- look, most franchisors are  
25 good. I agree with that. But we do rules and

1 oversight not to damage the good franchisors, we do it  
2 to protect from the bad franchisors. But with all  
3 these concerns, can someone tell me the last time the  
4 FTC took action against a franchisor for a financial  
5 representation made in the disclosure document? I  
6 think most of the people would answer it's been a long  
7 time.

8 MS. TODARO: Thanks, Keith.

9 I want to follow up on something that you  
10 said earlier. I mean, in terms of the number of  
11 representations that you're seeing being made outside  
12 of the FDD or inconsistent information that's being  
13 provided to prospective franchisees outside of the  
14 FDD, have you seen a decrease in the number of times  
15 that's happening or the number of complaints or  
16 stories you hear from your members and other  
17 franchisees now that more franchisors are disclosing?

18 MR. MILLER: Well, I'd have to say  
19 personally, I'd be a little biased in this answer. I  
20 would say it's on the increase, but that's probably  
21 only because I've become more known out in the  
22 industry and I get more calls on it.

23 Look, I have to understand that the people  
24 who call me are calling me because they have problems  
25 and issues, not -- you know, everyone who's happy

1 isn't calling me. So I guess as I've become more well  
2 known, I've probably seen an increase in it. But I  
3 wouldn't say that's because there is an increase in  
4 false representations.

5           And I know we'll talk about later the  
6 sources, but that's kind of what gets to be  
7 interesting, is the sources that the representation is  
8 coming from. The false representations tend to be  
9 more at an arm's length and not from inside the  
10 franchise company, whether it's brokers or consultants  
11 or loan brokers, for that matter. And I think we'll  
12 touch on that a little later.

13           So I think the sources of false  
14 representation have -- most franchisors know what they  
15 can and can't do and have moved away from that. But  
16 that doesn't mean that false information isn't getting  
17 to franchisees.

18           MS. TODARO: Okay, I'd like to turn to  
19 Justin. Have you seen much litigation over false FPR  
20 data or FPRs that are given to prospects outside of  
21 the FDD?

22           MR. KLEIN: Yes, I think we're all using  
23 interesting adjectives; namely, the word "false." I  
24 think there's a very big distinction between false and  
25 impermissible. One of the bigger concerns that I have

1 is about -- the largest concern is false data.  
2 Impermissible data or impermissible disclosures  
3 outside of the realm of the document is something that  
4 I think is going to be really hard to ever regulate  
5 around. I mean, salespeople are going to be  
6 salespeople. They're going to say what they're going  
7 to say. You know, presumably franchisors are doing  
8 the right thing by training their staff the right way,  
9 by training their sales people. Presumably, they're  
10 talking to their brokers and the folks who they are  
11 engaging to bring into their universe what is  
12 permissible and what is not permissible.

13 Obviously, nobody on this panel, I would  
14 presume -- and by the way, thank you for having me on  
15 the panel; I'm honored to be amongst all these  
16 distinct colleagues -- but nobody wants false data.  
17 And I think, you know, when you look at -- and I will  
18 answer your question directly -- but when you look at  
19 the concept of mandatory FPRs, my bigger concern is  
20 somebody who represents more franchisees, like Keith,  
21 is garbage in/garbage out. If there is no way to  
22 properly check and balance the information that's  
23 being provided -- and we've heard reasonable basis and  
24 everybody is familiar with kind of the concept around  
25 the FPR -- are folks who range from John Q and Mary Q

1 Franchisee up to sophisticated private equity groups  
2 who are all reading the same FDD, are all looking at  
3 and analyzing the same information.

4           So my bigger concern is what is the  
5 relevance of the data that's being provided and the  
6 form with which it's being provided in to ensure that  
7 the prospective investor -- the consumer, if that's  
8 what we want to call them -- is given the information  
9 that is going to be most relevant to the decision to  
10 make the investment.

11           From a law firm perspective, we have not  
12 seen an uptick in what I would call impermissible FPR  
13 claims. The claims of "I was promised I was going to  
14 make \$1 million and I didn't make \$1 million," over  
15 the last decade or so have significantly declined,  
16 from our perspective. I don't know that that's  
17 directly FPR-related, quite frankly. I think that's  
18 more probably related to some of the other barriers to  
19 litigation that exist out there, be it the franchise  
20 agreement, be it the cost, be it the time, be it the  
21 nature of the type of claim that's being brought and  
22 where either the franchisor or the franchisee stands  
23 at the time that claim is being brought in connection  
24 with those factors.

25           So, you know, I don't know that -- just to

1 round it all back to the topic and the theme, I don't  
2 know that there's been an uptick, but I also don't  
3 know that mandatory FPR positively or negatively  
4 impacts the amount of those types of lawsuits that  
5 ultimately come out of that information.

6 What I can say is I fear that if 40 percent  
7 of franchisors are not providing the information for  
8 one or more of the reasons that any of the folks on  
9 this panel have already addressed, my bigger concern  
10 is that the lack of accuracy and the lack of  
11 professionalism that is required in the disclosure  
12 process isn't going to be met. And that's a negative  
13 impact to prospective investors in terms of my concept  
14 of garbage in/garbage out.

15 MS. TODARO: Keith, do you have anything in  
16 response to that?

17 MR. MILLER: No, and I think we have to  
18 remember who's looking at these FDDs. And I think  
19 Justin brings up, you know, a really good point in  
20 that you have the range of big private equity  
21 franchisees to, you know, a person who has very little  
22 knowledge. The industry always sells itself as be  
23 your own boss, proven business model, no experience  
24 necessary. Yet, then it bashes those people with "no  
25 experience necessary," when they make a mistake.

1           And I think we have to really look at -- and  
2 I know one of the other panels is actually more  
3 talking about the structure. I think you also have to  
4 look at, when you talk about uptick or lack of uptick  
5 in lawsuits on it, I think it's almost impossible for  
6 a franchisee to have the resources to do that fight.  
7 I mean, that's what I think franchisees depend on the  
8 FTC to do and especially when there's no private right  
9 of action on the Franchise Rule.

10           The average franchisee, when they fail --  
11 and it may have been falsely disclosed -- has been  
12 wiped out. All their assets are at risk. So what  
13 resources do they have to fight, you know, what's  
14 happened to them, whether it's false or  
15 unsubstantiated claims? It's very difficult for them  
16 to fight it. They just don't have the resources.

17           MS. TODARO: Sandy, do you want to follow up  
18 on that?

19           MS. WALL: Well, Christine, from the FTC's  
20 perspective, have you seen in the last ten years, a  
21 lot of complaints from franchisees alleging that  
22 unlawful FPR information has been provided or  
23 information outside of an FDD?

24           MS. TODARO: I mean, I have to say that this  
25 is something that I haven't looked at recently. The



1 last time that I looked at complaint data, I can tell  
2 you we get far fewer franchise complaints than we do  
3 for other types of business opportunities, at least  
4 from the data set I had looked at.

5 MS. WALL: And, you know, just to -- go  
6 ahead.

7 MS. TODARO: No, go ahead.

8 MS. WALL: And just to the point about  
9 litigation, you know, franchisee litigation continues,  
10 and it may be on other issues, but you don't -- you  
11 know, my experience is from a franchisor's  
12 perspective, you're not seeing a huge amount of  
13 litigation specifically related to FPRs. There is --  
14 you know, I don't agree with the fact that franchisees  
15 are not suing franchisors. It's just not based on  
16 these types of claims for the most part.

17 MS. TODARO: Dale, is there something you  
18 want to add?

19 MR. CANTONE: Yeah, I think when you talk  
20 about, you know, both complaints and litigation, I  
21 just don't think litigation is a good indicator of  
22 what's going on in the franchise world because, you  
23 know, there are some systems -- I mean, it depends.  
24 Franchising covers a huge realm, you know, of like  
25 McDonald's and the Hiltons. And it also covers the

1 smaller investments, the people that we hear most from  
2 that maybe Sandy and Susan don't represent.

3 And, you know, a lot of those franchisees  
4 simply do not have either the resources to pursue  
5 litigation. There are barriers to filing suit that  
6 franchisors have been brilliant at putting in the  
7 disclosure document. And I know you're having a panel  
8 on disclaimers and these certifications, which I think  
9 is a good topic to go by. But, you know, even a  
10 mandatory arbitration provision in a franchise  
11 agreement -- and they're ubiquitous -- really does put  
12 a barrier in place to bringing a lawsuit.

13 But I will tell you that we also don't get  
14 that many complaints generally from franchisees. I'm  
15 not quite sure -- it's funny, when I read some of the  
16 message boards or when I hear from Keith, there are  
17 lots of complaints out there, but for all sorts of  
18 reasons, they're not necessarily getting to my office  
19 and probably not getting to your office. I don't  
20 think that's an indicator there aren't problems out  
21 there. We're just not necessarily hearing about them.

22 MS. TODARO: Justin, was there a followup?

23 MR. KLEIN: Yeah, I just think as a  
24 followup, I think that's a fair statement. I will  
25 tell you, as somebody who reviews these documents on

1    behalf folks who are looking to make the investment,  
2    you know, one of the initial things that we look at  
3    is, first of all, is there an FPR? That's number one.  
4    I mean, look, lawyers are notoriously bad at math, so  
5    I can't really provide much insight into what the FPR  
6    does or says or what it means. But the FDD, from our  
7    perspective, is step one of the process. That's the  
8    beginning of due diligence. It's a tool for  
9    prospective franchisees to use in connection with the  
10   rest of the due diligence that they're going to do.

11            If the FDD has been approved by Dale's great  
12   state of Maryland, if it's been approved by other  
13   states that have registration requirements, then we  
14   look at it through, to use Susan's word or Sandy's  
15   word, a different "prism," if some state regulator has  
16   reviewed it.

17            So, you know, I think it's -- again, it's a  
18   positive step if franchisors are going to make those  
19   FPRs. But I don't know that FPRs are the point of the  
20   breakdown of the relationship or why even a franchisee  
21   ultimately makes the decision to move forward with a  
22   particular brand.

23            MS. TODARO: Okay, thank you. I think Keith  
24   wants to add something, and then I'd like to move on  
25   to the next topic to make sure we have enough time

1 remaining

2 MR. MILLER: Yeah, one quick comment. One  
3 of the reasons the FTC doesn't see a lot of complaints  
4 is if a franchisee -- and I've heard this from  
5 multiple lawyers that represent franchisees -- if  
6 they're considering legislation, they don't want the  
7 client to file an FTC complaint because the reality is  
8 the FTC is probably not going to act on that complaint  
9 and then that gets used against them in their  
10 lawsuits, that they're told, well, you filed a  
11 complaint with the FTC, they didn't act, so,  
12 therefore, nothing must have happened wrong.

13 So literally, I've heard from multiple  
14 franchisee lawyers telling their clients not to file  
15 an FTC complaint. So that reduces complaints. And,  
16 of course, people really don't know how to file them.  
17 And they're still in that system, they're afraid of  
18 retaliation from their franchisor, if they're still in  
19 the system.

20 MS. TODARO: Okay. Well, I would just like  
21 to add that we always encourage anyone to file a  
22 complaint with the FTC. You can do that on our  
23 website. We have information to walk you through  
24 specifically how to file a complaint. There's also a  
25 phone number on our website that you can call in order

1 to speak with someone live to file that complaint.

2 So I just want to add that the FTC's  
3 position is people should be filing complaints with us  
4 if they feel like they've been wronged or unfair  
5 deceptive practices.

6 MR. MILLER: And I would agree with that, as  
7 you know.

8 MS. TODARO: That being said, I'd like to  
9 move to another consideration, which some of you have  
10 talked about, which is the potential cost to  
11 franchisors or franchisees if FPRs were to be made  
12 mandatory. In 2007, the Commission noted that  
13 mandating FPRs would impose substantial new  
14 accounting, data collection and review costs in all  
15 franchise systems. You know, as Dale mentioned  
16 earlier, most franchisors now collect financial  
17 information through a POS system. That might have not  
18 been the case when the Commission amended the rule.

19 Sandy, to that end, what's your position on  
20 whether mandating FPRs would impose substantial costs  
21 on franchise systems today and what would those costs  
22 be?

23 MS. WALL: I think you're right, Christine,  
24 and, Dale, you're correct. There is -- you know, due  
25 to the emergence of technology over the last 10, 15

1 years, you know, more of that information is provided  
2 to many franchisors. But it is not all franchisors.  
3 There are some franchise systems that are not based  
4 on a percentage of sales in terms of royalty and  
5 they don't collect that information from their  
6 franchisees.

7 In addition, you know, franchise agreements  
8 have a term to them. And depending on when the  
9 franchise agreement was entered into, there may or may  
10 not be sufficient language in a franchise agreement to  
11 allow the franchisor to collect this data from the  
12 franchisee. So for systems that don't get this data  
13 through a POS system, it would be expensive. You  
14 would have to go to the franchisees and ask them to  
15 provide this information. You couldn't mandate it.  
16 You would have -- the franchisor would be required to  
17 devote their resources to collect the data, and then  
18 evaluate and analyze the data to make sure it is  
19 accurate.

20 And, you know, again, I think when you look  
21 today, if you have that type of system, those are the  
22 types of systems that aren't providing FPRs, because  
23 they don't have -- they don't feel comfortable -- and  
24 that is something we'll talk about later -- that they  
25 have the reasonable basis to stand behind the

1 information in the FPR. And, you know, I think this  
2 is -- again, it's not all franchisors, but there are a  
3 number of franchisors that fall into that category.

4 And, again, you know, we're going to talk  
5 about this later, but -- I'll leave it at that point.  
6 I'll leave it at this point right now. We can come  
7 back to this.

8 MS. TODARO: Susan, do you see other costs  
9 that franchisors would incur beyond those that Sandy  
10 mentioned?

11 Susan, we can't hear you right now.

12 MS. GRUENEBERG: Sorry, I've been having  
13 trouble with my audio today. I was going to say, in  
14 terms of pure out-of-pocket costs, of course, you're  
15 going to have more costs to prepare an FPR. You're  
16 going to have additional legal fees, accounting fees.  
17 But I agree with Dale on the cost-benefit analysis. I  
18 don't think this is the factor that should really  
19 weigh in favor of not mandating FPRs.

20 I think more -- it's more of what Sandy is  
21 talking about, the practical difficulties in systems  
22 that weren't born yesterday and don't have the POS  
23 systems in place or don't have the contractual  
24 provisions to mandate use of them. If you look back  
25 at the original statement of basis and purpose, when

1 the Rule was first enacted, the purpose was to level  
2 the playing field of information. Prospective  
3 franchisees were found not to have the same level of  
4 information that franchisors had. So this seems to  
5 me, the particular factor, cost, is something where,  
6 you know, it shouldn't mandate in favor of, you know,  
7 not mandating FPRs.

8 But when you get into the practicality of  
9 gathering this information and making sure it's  
10 reliable, that's where the unspoken costs are, and  
11 those are really difficult to deal with. In fact, if  
12 you look at the FPR commentary that NASAA released a  
13 couple of years ago, you can see by the answers that  
14 the concept of reliability of cost data for  
15 franchisees was something that NASAA considered in  
16 agreeing that franchisors, who didn't have access to  
17 that kind of data, could use their own company or  
18 affiliate's own unit data and make adjustments to it  
19 to account for what a franchisee would experience.

20 So that's kind of a validation of the fact  
21 that this is difficult information to access, in many  
22 cases.

23 MS. TODARO: Dale, did you have a followup  
24 on what Susan just said?

25 MR. CANTONE: Well, there's discussion



1 about, you know, the difficulties in developing a  
2 mandate for FPRs and that, in fact, there are some  
3 systems that everybody would recognize probably  
4 couldn't and shouldn't make an FPR. But that doesn't  
5 mean you don't try. Because what we're left with now  
6 is a system where a franchisor can choose purely, for  
7 whatever reason it wants, not to provide the data.  
8 And there are some franchisors that probably should  
9 not and could not provide an FPR, new and emerging  
10 systems, what have you.

11 But that doesn't mean you don't come up with  
12 an idea where you can move the ball forward because it  
13 is such an important disclosure. I mean, the one  
14 thing that the Rule has consistently agreed upon is  
15 this is the number one thing the franchisees want and  
16 they really deserve it. So leaving it entirely up to  
17 franchisors, some of whom are absolutely doing the  
18 right thing, but not all of them may. If you do  
19 mandate -- if you do provide a mandate that is a  
20 common sense mandate, that takes into account the  
21 practicalities and the realities of the situation, I  
22 think it would benefit everybody. And it's just  
23 something that we could trial.

24 MS. TODARO: Sandy, do you have a followup  
25 to Dale on that?

1                   MS. WALL: Look, Dale, you know, again,  
2     prospective franchisees have the choice. If they ask  
3     for the information and they do not get a legitimate  
4     reason as to why the information can't be provided,  
5     they don't proceed with the franchise purchase. It's  
6     like every decision that a consumer makes day to day.  
7     And I think trying to craft the rules, as we've  
8     discussed, and come up with the exceptions about who  
9     would have to produce it is going to make a lot more  
10    -- create more impediments to franchising than it's  
11    going to help prospective franchisees.

12                  MS. TODARO: Okay. Justin, is there  
13    something you want to add? And as a followup to  
14    whatever you're going to say, I was wondering if you  
15    could address whether you think that there will be  
16    increased costs to franchisees if FPRs were mandated.

17                  MR. KLEIN: So I don't hate Dale's idea in  
18    theory. From a regulatory perspective, I'm not sure  
19    how you come up with that common sense structure. And  
20    the scale of franchisors that are out there and the  
21    sophistication level of franchisors and who is  
22    advising them and guiding them is from top to bottom  
23    in terms of who's out there.

24                  I guess my bigger concern, as somebody who  
25    reviews these on behalf of somebody else as an

1     adviser, is I'm more concerned about bad info than  
2     mandated info. And, again, if it's mandated, I'd be  
3     more concerned about the cost associated with what  
4     folks have -- and, listen, we've seen some really bad  
5     FDDs. We've seen FDDs with other brand's names in  
6     them. We've seen FDDs written on spiral notebooks.  
7     We have seen FDDs that don't comply with any  
8     regulations that are out there whatsoever and there  
9     just is a cover sheet that says "FDD" on it and that  
10    doesn't stop our clients from necessarily wanting to  
11    invest in the franchise and/or, quite frankly, even  
12    being successful with that brand. It just means that  
13    they're not necessarily getting the best guidance from  
14    their professionals.

15                 So, you know, my bigger concern is who's  
16    preparing the information and the reliability is  
17    critical. And if it's mandated, unless there is some  
18    regulatory component to figuring out how reliable that  
19    information is for a prospective franchisee, that's my  
20    bigger concern.

21                 From a cost perspective for franchisees, I  
22    mean, most franchisees, no matter how sophisticated  
23    they are, that come to us, whether they own one unit  
24    or they're involved in many, many businesses, they ask  
25    basically two questions of the franchisor. How much

1 does it cost and how much can I make? That's all they  
2 care about. I don't know that the FPR, again, is the  
3 be-all/end-all of the mindset of a prospective  
4 investor in terms of how much they can make. I think,  
5 again, the FDD, at least the way we counsel our  
6 clients, is that is only a piece of the puzzle to  
7 gather that information and determine its reliability  
8 to use it in terms of talking to other franchisees,  
9 talking to competitors and talking to figure out  
10 whether or not it's relevant to your particular  
11 market. So I think reliability is the big question.

12 I fear, again, if we are just lawyers that  
13 they are bringing it to and they're not bringing it to  
14 accountants or other business advisers to check the  
15 veracity of the numbers, now there's another  
16 component, which, footnote, prospective investors  
17 should be having on their team in any event to help  
18 them analyze the data and everything else. But I do  
19 think there is an increased cost to franchisees to do  
20 their own reliability test with their own  
21 professionals to determine the veracity of any  
22 information that's being provided to them.

23 MS. TODARO: Justin, do you have --

24 MR. KLEIN: And just to caveat that, I don't  
25 think that's necessarily a negative thing. I think

1 that's probably a positive thing that they should be  
2 doing in any event, but I do think it's an added cost.

3 MS. TODARO: Do you have a sense whether  
4 prospective franchisees compare offerings based on  
5 FPRs? One hundred percent. You know, a lot of folks  
6 go on and look at -- go on the internet, and they say  
7 what does this FPR say versus what does this FPR say,  
8 and they make their initial decision to pursue a  
9 prospective investment based on the information that  
10 the franchisor is providing in the document.

11 Again, from our perspective, the FDD and the  
12 FPR is step one or step negative one of the process,  
13 and I do think that's information that prospective  
14 franchisees are looking at. And, oftentimes, they're  
15 looking at the quality of the product or the service  
16 that's being provided, and sometimes they mistake the  
17 quality of the product for the ability to be  
18 successful selling that product or service. And I  
19 think a component of that is the information that's  
20 being provided in the FDD creates an initial mindset  
21 as to whether or not they think it's an appropriate  
22 investment for them. How much does it cost and how  
23 much can I make?

24 Line up five FDDs across the board because  
25 this is the industry that I'm interested in and let me

1 see what the information says.

2 MS. TODARO: Dale, is there something you  
3 want to respond to on that?

4 MR. CANTONE: I just wanted to point out  
5 that Justin is talking about a category of prospective  
6 franchisee that is coming to somebody like Justin to  
7 help them review the disclosure document. I can tell  
8 you the people that -- a lot of people we hear from at  
9 the state level who have had issues do not go to a  
10 lawyer, they can't afford to go to a lawyer, or they  
11 choose not to go to a lawyer. From the number of  
12 filings that we see, we can tell that there's a  
13 significant number of franchise systems out there,  
14 that are targeting people that probably are not going  
15 to a lawyer, much less an accountant, much less fully  
16 reviewing the disclosure document to make this  
17 determined choice whether or not to buy something  
18 based on the disclosure.

19 So I just wanted to point out, I'm glad,  
20 Justin, you do what you do, but I wish every  
21 franchisee had a lawyer to counsel him or her before  
22 they purchase. But the reality is a lot of them  
23 simply don't do that and they're relying on that  
24 disclosure document on their own.

25 MS. TODARO: Okay. Susan, I think you have

1 a followup and then I would like to go on to the next  
2 topic just being cognizant of time.

3 MS. GRUENEBERG: Yeah, I just wanted to add  
4 that in terms of market forces, franchisors will look  
5 and compare different FPRs with their competitors in  
6 their industry. And they know they are being  
7 compared, so they are going to logically try to get a  
8 better representation in their FDD in terms of what  
9 they're disclosing. So it does encourage the use of  
10 FPRs when you have this comparison going on. So I  
11 think it's very healthy.

12 MS. TODARO: Okay, thank you.

13 I would like to move to the next  
14 consideration which was potential liability. Another  
15 factor that the FTC considered was whether mandatory  
16 FPRs might subject franchisees to potential liability  
17 for providing inaccurate data to franchisors who then  
18 use that information in their FPR. And I'd like to  
19 direct this question to Sandy. Since 2007, have you  
20 seen an increase in litigation between franchisees and  
21 franchisor on this issue?

22 MS. WALL: Christine, not at all. I mean, I  
23 think you could ask really any litigator and they will  
24 tell you that up to this point -- you know, I'm not  
25 aware of any franchisor that has ever tried to bring

1 an action against a franchisee on the basis of  
2 information provided that became the basis for an FPR.  
3 However, I think that the reason for that is that FPRs  
4 are not mandated and franchisors that provide FPRs  
5 need to have a reasonable basis for putting the  
6 information together. If the information they get  
7 from prospective franchisees is, in their judgment,  
8 not reliable, they are not going to put an FPR  
9 together.

10 In addition, if you go forward and you  
11 mandated an FPR, you know, today, in many franchise  
12 agreements, there are provisions that require  
13 franchisees to provide reports and records and  
14 information to the franchisor. And in the default  
15 section, the franchisor may often have a right to  
16 terminate the franchisee if the franchisee  
17 misrepresents the information in the FDD. And, again,  
18 if there was a mandate going forward and a franchisee  
19 provides inaccurate information that becomes the basis  
20 for an FPR, the franchisors may have recourse against  
21 the franchisees for this.

22 In addition, most franchise agreements have  
23 identification provisions that state that the  
24 franchisee has to indemnify the franchisor for issues  
25 related to the operation of the business and, again,



1 you could see that those types of provisions could be  
2 used. Again, it's unprecedented. You haven't seen it  
3 today because if the franchisor is not comfortable  
4 with the information, they don't prepare the FPR.

5 MS. TODARO: Susan, do you have a followup  
6 on that?

7 MS. GRUENEBERG: Well, I would just say that  
8 my experience has been anecdotally the same as Sandy.  
9 I have not seen those kind of claims. To try to  
10 protect against being in that situation to begin with,  
11 however, what I think what you're seeing more of in  
12 FPRs is an explanation of where this data came from,  
13 why it could be different from a prospective  
14 franchisee's experience, and those explanations are  
15 really crucial to explaining how there is a reasonable  
16 basis for the information being presented.

17 I know that later on in this workshop you're  
18 going to be talking about disclaimers and I assume  
19 that a lot of that discussion is going to center  
20 around disclaimers in Item 19. But what you'll have  
21 to be very careful about is not wiping out these  
22 explanations along with the disclaimers because it's  
23 crucial for a prospective franchisee to understand  
24 that their experience is not necessarily going to be  
25 the same as the franchisee on whose data that this FPR

1 was made.

2 MS. TODARO: Dale, from a regulator's  
3 perspective, do you have any thoughts on this  
4 consideration?

5 MR. CANTONE: Sorry. As a regulator, I  
6 don't know that we would be in a position to have that  
7 information. So honestly, I wouldn't know.

8 MS. TODARO: I would like to move now to the  
9 final consideration that we're going to discuss today  
10 which was the Commission's view that the FDD is not  
11 the only way for a prospective franchisee to get  
12 financial performance information. Some of you have  
13 touched on that already, that FPR is our one piece of  
14 the puzzle when a prospective franchisee is deciding  
15 what they want to participate in.

16 So I guess at the outset, Justin, I'm  
17 wondering if you could give us a sense of what are all  
18 those sources aside from just talking to existing or  
19 former franchisees. Are there others?

20 MR. KLEIN: Yeah, and I'm sensitive to  
21 Dale's comment that most, if not many, if not the  
22 majority of franchisees don't hire lawyers or business  
23 advisors or counselors to help them with this very  
24 important decision. You know, as a lawyer, I highly  
25 recommend that to the extent you're going to make a

1 large investment like that, you get the right people  
2 around you to help you make that investment decision.

3 One of the things that we suggest to folks  
4 who are looking to get into franchising who have never  
5 done it before is to also look at market conditions.  
6 You know, is the business that you're looking to buy,  
7 is it appropriate for the area that you're looking to  
8 operate in and have you spoken to people in the area,  
9 have you spoken to competitors, have you spoken to --  
10 you know, to the extent that the franchisor has  
11 multiple brands, have you spoken to franchisees of  
12 other brands that they operate in. You know, how are  
13 the training programs? Talking about, you know, what  
14 the franchisor has to offer separate and apart from  
15 what is actually in the document.

16 Christine, I'm big on trust but verify as a  
17 lawyer, I guess. So I presume that everybody is good  
18 at heart and the information that's being included in  
19 the FDD is accurate. But when I say the FDD is really  
20 step one, you know, the FDD is really step one because  
21 it's giving you information to then go out and verify,  
22 whether it's with other franchisees, whether it's with  
23 competitors in the market, whether it's with other  
24 systems that they have, whether it's with, you know,  
25 folks who may be in independent businesses that are

1 not necessarily operating under a franchisee system  
2 but are in a similar type of a business.

3           Again, I guess because I'm a lawyer, I am  
4 way risk adverse, so I'm not a prime candidate to buy  
5 a franchise anyway. There's never enough information  
6 that you could gather from an investment perspective.  
7 And I think the real value of the FDD is it gives you  
8 a starting point to start from to use that information  
9 to begin the journey of your due diligence.

10           MS. TODARO: Okay. I want to now turn to  
11 Keith, and say, what are your thoughts on these other  
12 sources for a prospective franchisee to use?

13           MR. MILLER: Of course, looking at what are  
14 the other sources, I mean, sometimes it's someone  
15 internal improperly giving data outside the disclosure  
16 document. But I think that's not the big problem. I  
17 think one of the biggest problems is from the third  
18 party, what I would call unlicensed, unregulated  
19 franchise brokers and consultants who have no  
20 fiduciary responsibility to that prospective  
21 franchisee. I mean, they get paid by the franchisor  
22 when the sale happens.

23           One of the things I'm often quoted in saying  
24 is one of the problems in the industry is far too many  
25 people profit from the sale of a franchise, far too

1 few are held accountable for the success of the sale.

2 Another one that I found quite often is loan  
3 brokers, when people start working on their financing  
4 even in advance of signing the franchise agreement.  
5 These loan brokers often know what needs to put on the  
6 loan applications to qualify for loans, especially the  
7 government guaranteed SBA 7a loans, and they know how  
8 to fill out those forms to get someone qualified to  
9 buy that business, and they are reverse engineering  
10 the numbers to get up to revenue. Again, they have no  
11 accountability to that person.

12 So I worry there are these people outside of  
13 a franchise company that are throwing around numbers  
14 that people too often take as being gospel and they're  
15 not. You know, people always say, well, do your due  
16 diligence by contacting franchisees, and I would say  
17 to that, well, if the franchisor gives you that,  
18 obviously, the list is in the disclosure document of  
19 existing franchisees, but often a franchisor will give  
20 people a list that's basically the top performers,  
21 which is skewing the information.

22 Then if you try to go out and look for past  
23 franchisees, if you look within the disclosure  
24 document, often the contact information is wrong and  
25 you can't get a hold of that franchisee, and then if

1     there was a bad exit by the franchisee, there's often  
2     a nondisclosure agreement that's been signed. So you  
3     won't hear the downside of the stories, you tend to be  
4     -- when you try to contact franchisees current or  
5     past, tend to get skewed to the better franchisees.  
6     Even with existing franchisees, if it's a troubled  
7     franchisee, you know, there's cases right now where  
8     existing franchisees are being sued in violation of  
9     the nondisparagement agreements that are within the  
10    franchise agreement.

11                 So I really don't see franchisees often as  
12    being a reliable source and that's why, of course, I  
13    push hard for more data in the disclosure document  
14    because there is some liability and responsibility in  
15    that, and I believe that information in general can be  
16    trusted.

17                 MS. TODARO: Sandy, do you have a followup  
18    to what Keith said?

19                 MS. WALL: Yeah, I mean, Keith, again, I  
20    think you're focused on the bad actor here. I mean,  
21    what you're talking about here is if a franchisor  
22    gives a prospective franchisee -- steers them to  
23    specific existing franchisees, that's a violation of  
24    the disclosure requirements. And, again, there is a  
25    list of franchisees given, there is a list of

1 franchisees who have left the system in the last 12  
2 months and the prospective franchisee needs to do  
3 their homework and make the calls.

4           What you're referring to about the  
5 confidentiality agreements is addressed in Item 20 of  
6 the FDD. If the franchisor restricts the ability of  
7 franchisees to talk about their experience with the  
8 system, that has to be disclosed in Item 20 of the  
9 FDD, also. Again, this is -- the purpose of  
10 disclosure is to help prospective franchisees make  
11 informed decision-making. The information is there  
12 and if you see all these things in there, if you're  
13 getting information that's inconsistent with what's in  
14 the FDD or you see that all franchisees are required  
15 to sign these types of confidentiality agreements,  
16 these are red flags. Again, the prospective  
17 franchisee has the choice to proceed or not to  
18 proceed.

19           MS. TODARO: Okay. I would like to jump to  
20 a new topic outside of mandatory FPRs, because the  
21 NASAA commentary which Susan mentioned earlier --  
22 Dale, NASAA noted in its 2019 comment that the FTC  
23 should consider incorporating the NASAA FPR commentary  
24 into the Franchise Rule. Why would this be helpful?

25           MR. CANTONE: The FPR commentary -- well,

1 actually, the FPR commentary that NASAA did, the  
2 original impetus was to correct a misconception about  
3 the use of affiliate data and that stemmed from an  
4 unfortunate footnote in the Compliance Guide of 2008  
5 that suggested that franchisors, if they have adequate  
6 operating experience of their own, should not use  
7 affiliate data, that, in fact, affiliates often are  
8 the owners of company-owned outlets. So the original  
9 impetus was clarify the use of company-owned outlet  
10 data.

11 I may be biased, but I have -- in the last  
12 couple of years, it seems that the NASAA FPR  
13 commentary has been very well accepted in the  
14 industry. It's used extensively. It has not been a  
15 very controversial, for the most part, guidance issued  
16 by NASAA, and it does address a lot of issues that  
17 needed to be addressed that were open, the use of  
18 affiliate data, subsets. And it's been working  
19 extremely well in the state regulatory environment.  
20 That's my perception. The people on the panel can,  
21 you know, share their opinions of it as well. It  
22 really would be a benefit to have the guidance that is  
23 at the state level incorporated at the federal level.

24 MS. TODARO: Susan, do you have a sense how  
25 likely franchisors are to comply with the commentary



1 in nonregistration states?

2 MS. GRUENEBERG: I'm actually a little bit  
3 surprised at the question because I think there is a  
4 view to comply with the commentary and also with the  
5 more recent guidance that's provided about FPR  
6 disclosure in the middle of the COVID-19 pandemic. In  
7 fact, I would also echo Dale's suggestion that it be  
8 incorporated. In fact, I think there's an appetite  
9 for more commentary and more guidance about Item 19  
10 out there on all levels because the commentary is  
11 great as far as the goes, but it certainly doesn't  
12 address every issue that comes up, and there are  
13 constantly new ones. And this kind of guidance is  
14 very helpful to us in preparing FPRs with the  
15 assurance that we're more likely to achieve that  
16 illusive reasonable basis which nobody seems to be  
17 able to define exactly.

18 So I would definitely support it, and I do  
19 think there's widespread or there should be widespread  
20 compliance with it in states that don't have their own  
21 state franchise laws regulating the offer and sale of  
22 franchises.

23 MS. TODARO: Dale, is there a followup that  
24 you want to add?

25 MR. CANTONE: Yeah. I just wanted to add

1 that if there's a concern about the fact that the  
2 commentary might be impacting negatively FPRs, I have  
3 data from my state. The year before the FPR  
4 commentary was adopted, our records show 60.87 of  
5 franchisors registered in my state made some type of  
6 FPR. The year after the NASAA FPR commentary was  
7 adopted, the number actually increased. So it did not  
8 negatively impact franchisors from making FPRs. Just  
9 thought I would add that.

10 MS. TODARO: Okay. And, Justin, just to  
11 follow up on what Susan said, in your practice, do you  
12 see that franchisors in nonregistration states are  
13 following the NASAA commentary?

14 MR. KLEIN: Yeah, no, I agree with both Dale  
15 and Susan on their ultimate conclusions. Again, my  
16 fear goes back to not only the franchisees who can't  
17 hire lawyers who are qualified, but franchisors who  
18 can't hire lawyers who are qualified. My bigger  
19 concern is whether or not folks are actually complying  
20 with the regulations that are out there. So I think  
21 the more information that can be -- the more guidance  
22 that can be given, the better it is. But again, our  
23 biggest fear is garbage in/garbage out. And I think  
24 unless there's some enforcement prospective to what  
25 the requirements are, then I'm not really sure what

1 the value of any of it is.

2 MS. TODARO: And, Sandy, do you have a  
3 followup on that?

4 MS. WALL: Again, I think the FPR commentary  
5 has provided terrific guidance in many areas. The  
6 only caution I would mention at this point is the  
7 whole issue of disclaimers and providing factual  
8 information that explains what the FPRs cover and what  
9 it doesn't cover. That's still an ongoing discussion  
10 that franchisors and state regulators have. And I  
11 just would want there to be caution here that, again,  
12 while some of the language in the commentary is  
13 absolutely clear what you can and cannot do, there are  
14 certain sections in here which are open to  
15 interpretation.

16 Therefore, I guess I would be more for sort  
17 of presumption that if you comply with the commentary,  
18 you're in compliance with the FTC Rule rather than  
19 saying absolutely comply. Because I'm not sure in  
20 some instances it is 100 percent clear you need to do  
21 to comply with the commentary.

22 MS. TODARO: Okay, thank you.

23 Just on the final point I want to note,  
24 Susan, you touched on this, which is reasonable basis  
25 and I think, Dale, you did as well. Is there

1 confusion in the industry about what a reasonable  
2 basis is? And this will be our final point because we  
3 are at the end of the panel.

4 So I'll turn it over to Dale.

5 MR. CANTONE: I think there is. I mean,  
6 first of all, it's not defined anywhere. Under the  
7 Rule, franchisors have the burden to show they have a  
8 reasonable basis. So in some ways, that's kind of  
9 unfair to the franchisors. But I can tell you from  
10 our experience -- somebody mention the NASAA Franchise  
11 Project Group's guidance on making an FPR during the  
12 pandemic. I cannot tell you how many franchisors in  
13 response to questions to state regulators were under  
14 the impression that all you need to have is  
15 historically accurate information. I don't think that  
16 is entirely the reasonable basis.

17 So the fact that that many legitimately  
18 represented franchisors have that impression, I think  
19 leads me to believe there is confusion about what  
20 exactly is a reasonable basis, at least in the  
21 historic -- context of historical FPRs.

22 MS. TODARO: All right. Sandy, do you agree  
23 with that?

24 MS. WALL: Again, I think taking the view  
25 that it's historical isn't really the full analysis

1 that you have to engage in here. If you look at the  
2 FTC Rule and Section 436.7(d), a franchisor is  
3 obligated to notify the prospective franchisee of  
4 material changes that the seller knows or should have  
5 known occurred in the information contained in the  
6 FPR, I think that clearly addresses an obligation to  
7 be looking at your FPRs constantly to make sure that  
8 the reasonable basis that you had when it was prepared  
9 still exists today.

10 Again, also, prospective franchisees have  
11 the right to request substantiation of the information  
12 in the FPR. And, again, I think that's something  
13 that's not used as much as you would think in the  
14 industry.

15 So while reasonable basis isn't defined, I'm  
16 not sure you could ever properly define it. I think  
17 it's based on -- it's a question of fact that the  
18 franchisor is responsible for determining, who would  
19 have to prove in a court of law, if necessary.

20 MS. TODARO: Okay. And with that, I want to  
21 thank each of the panelists for participating today.  
22 We've just run slightly over time. Thanks for bearing  
23 with us. I think this is a very interesting and  
24 informative discussion. So thank you very much.  
25

1

2 A DISCUSSION OF DISCLAIMERS, WAIVERS &amp; QUESTIONNAIRES

3 MR. DOAN: Good afternoon or good morning as  
4 the case may be. My name is Josh Doan and I'm an  
5 attorney in the FTC's Division of Marketing Practices.

6 This panel will explore some of the comments  
7 the FTC received last year about the use of  
8 disclaimers, waivers of reliance, and questionnaires  
9 in connection with franchise disclosure documents and  
10 franchise agreements. If we have time, I will try to  
11 incorporate questions we receive from our virtual  
12 audience. Please submit those questions to franchise  
13 rule@FTC.gov.

14 We have a lot to cover, but first I would  
15 like to briefly introduce our distinguished panelists.  
16 Their bios are available on the event page if you  
17 would like to learn more about their impressive work.  
18 Howard Bundy is a Seattle, Washington attorney who  
19 represents franchisors in dispute resolution and also  
20 works -- or, I'm sorry, represents franchisees in  
21 dispute resolution and also works with franchisors in  
22 preparing contracts and disclosures.

23 Amy Cheng is a partner at Chicago's Cheng  
24 Cohen LLC, where she represents franchisors on the  
25 structuring and operation of their franchise programs

1 through all phases in domestic and international  
2 development.

3 Theresa Leets is the Assistant Chief Counsel  
4 of the Securities Regulation Unit of the California  
5 Department of Financial Protection and Innovation's  
6 Legal Division, where she supervises programs under  
7 the State's Corporate Securities Law of 1968 and  
8 Franchise Investment Law.

9 Brandon Moore is a resident of Northern  
10 Virginia and a former franchisor who will bring a  
11 nonlawyer's perspective to today's panel.

12 And Lee Plave is a partner at Reston,  
13 Virginia's Plave Koch, PLC, where he counsels  
14 franchisors and distributors, drafts and negotiates  
15 agreements for international and domestic transactions  
16 and advises clients on all aspects of franchise and  
17 distribution law.

18 So as we get started, I would like to say on  
19 behalf of myself and the panelists, the views we  
20 express today are our own and do not necessarily  
21 reflect the views of the Federal Trade Commission or  
22 any other organization, law firm, or company.

23 So with that, let's get started by talking  
24 about disclaimers. The Franchise Rule prohibits  
25 disclaimers and representations made in franchise

1 disclosure documents or in its exhibits or amendments.  
2 So I'd like to start by asking Howard Bundy, are  
3 franchisors still making disclaimers in their  
4 disclosure documents despite that prohibition, and if  
5 so, in which items?

6 MR. BUNDY: Josh, yes, they are. They  
7 continue to make them. If anything, we've seen an  
8 increase in the use of what I would generally  
9 characterize as disclaimers since 2007. Disclaimers  
10 come in three forms. There are outright disclaimers,  
11 there are waivers of reliance or statements of  
12 nonreliance; or there are acknowledgments,  
13 acknowledgments that appear to be benign but are not  
14 at the end of the day.

15 So yes, we see an increase. I think it is  
16 approaching the point now where for an attorney doing  
17 compliance work for a franchisor, if you do not  
18 include all of those, you probably are exposed to  
19 legal malpractice concerns. It is that always -- that  
20 much always present that we see those.

21 You also hear back from franchisor clients,  
22 who are going through the process, that everybody else  
23 has these disclaimers, they have read on the internet  
24 or heard in seminars how valuable the disclaimers are,  
25 and they want them, too.



1           So, in my view, this is the most important  
2 of the issues before the FTC today, because unless the  
3 Commission or the states get a handle on the  
4 disclaimer issues, the remainder of the disclosure is  
5 basically wasted. Everything else contained in the  
6 Rule, all of the other issues the FTC is looking at,  
7 get superseded and rendered essentially meaningless if  
8 the franchisor can go outside of the document, outside  
9 of the FDD, and say whatever they want to say in order  
10 to make a sale and then hide behind a waiver and  
11 disclaimer to avoid liability in the end.

12           And, yes, I wish it were not true, but  
13 particularly federal courts and arbitrators broadly  
14 enforce waivers and disclaimers against franchisees.  
15 Maybe we can talk later about what the franchisee  
16 thinks he or she is signing when they sign the waivers  
17 and disclosures. But I'll leave that for later.

18           In terms of where these are found, they are  
19 found, number one, in Item 19, they are found in Item  
20 11, and they are found in a separate section of the  
21 FDD that has become omnipresent that usually follows  
22 just ahead of the receipt pages, but it flows around  
23 in there somewhere in the exhibits portion. It's  
24 usually a one-to three-page document with a series of  
25 questions that the franchisee is required to answer

1 yes or no.

2 Those get presented by the transactional  
3 lawyers and by the franchisors, as necessary to police  
4 potentially problematic salespeople, the rogue  
5 salesperson defense. But the minute the franchisee  
6 makes a claim later they were lied to or misled, that  
7 disclaimer, that questionnaire comes in as Exhibit A  
8 from the defense side, and it's very --

9 MR. DOAN: Well, thank you, Howard. And we  
10 are -- sorry. We are going to get into questionnaires  
11 and acknowledgments a bit. There's a lot of in your  
12 response that I just want to follow up on that a bit.  
13 One of the items that you mentioned where you report  
14 continuing to see disclaimers is in Item 19, and Item  
15 19 was the subject of the first panel today. And as  
16 we left off, I believe Sandy Wall, one of the  
17 panelists, was touching on attention that maybe we can  
18 explore a bit here between adequately explaining, from  
19 a franchisor's perspective, the reasonable basis for a  
20 financial performance representation and an  
21 impermissible disclaimer.

22 So, Lee Plave, do you want to take that up?

23 MR. PLAVE: I'm happy to. Thank you for  
24 having us on this discussion. It's very interesting  
25 and very useful.

1           There's a big difference between explaining  
2   and disclaiming, and a disclaimer is flat out  
3   prohibited under 436.9(h) in any case. So a  
4   disclaimer that's made in the context of the FDD is,  
5   by definition of the rule, ineffective. So I leave it  
6   at that.

7           I think it would be very hopeful, though,  
8   and to pick up on a point that the first panel  
9   discussed, if your goal is to see more FPRs and more  
10  fulsome information, then allow people to give some  
11  explanation and some context, particularly in a year  
12  like this one where there's so much context that's  
13  needed. It is a difficult year in which to try to  
14  provide details without providing some explanation.  
15  Now, that's not to say that it's a disclaimer. It's  
16  an explanation.

17           I don't think anyone would have an objection  
18  if the Commission would take the rule that currently  
19  exists which says no disclaimers and just make it more  
20  obvious as to what they mean by that and to make it  
21  clear that no disclaimers mean that anything that's a  
22  disclaimer is ineffective. I think most franchise  
23  lawyers -- most franchisor side lawyers work from that  
24  presumption to begin with.

25           So I'll answer your specific question with

1 that specific answer. I don't think we need to  
2 overturn things. We already have a clause in the Rule  
3 that says disclaimers are ineffective. You don't have  
4 to go any further.

5 MR. DOAN: Amy Cheng, I see you nodding  
6 along. Is there anything you would like to say to  
7 supplement or complement Lee's response?

8 MS. CHENG: Yes. Well, I absolutely agree  
9 with Lee in that Item 19, there is also already a  
10 required disclaimer, right? The FTC says you've got  
11 to include an admonition, right, that a new  
12 franchisee's results may differ from the information  
13 that's contained in the FDD. I think that's  
14 sufficient in terms of the disclaimer.

15 But as Lee said, especially during these  
16 times -- unprecedented times, we're including  
17 information in Item 19 to provide as up-to-date  
18 information as possible to prospective franchisees.  
19 But that does require some unusual explanation, and if  
20 not only because of 2020 and the pandemic, but as  
21 franchisors provide up-to-date information and provide  
22 more detailed information, it's important to allow  
23 franchisors to include as much information as possible  
24 so they are disclosing the material basis on which  
25 they are including the information.

1           So to conclude that that explanation is a  
2 disclaimer I think would be inaccurate conclusion.

3           MR. DOAN: Teresa Leets, would you like to  
4 jump in and provide the perspective of a state  
5 regulator from a registration state?

6           MS. LEETS: I would. I want to thank you  
7 for inviting me here today and for joining this  
8 fantastic panel.

9           My first comment on disclaimers is that I  
10 think it would be helpful if the FTC added a  
11 definition of disclaimer to the Rule to create  
12 clarity. So I think if everyone was working under the  
13 same definition, there would be less uncertainty in  
14 the space.

15           I understand the term to mean any language  
16 that mitigates, contradicts, or disavows information  
17 presented in an FDD, but to the point about after the  
18 admonition, especially during the uncertain times that  
19 we're living in today, regulators here all the time,  
20 sometimes franchisors add a helpful explanation and  
21 it's not a disclaimer. But if the explanation applies  
22 to all businesses generally, most regulators view it  
23 as a disclaimer because, again, it mitigates,  
24 contradicts, or disavows the FPR, meaning it has no  
25 basis.

1           However, if a franchisor adds language to  
2 explain a circumstance or a condition specific to a  
3 business model, like the size of territory or seasonal  
4 demand for the product, and explains how that might  
5 cause results to vary, that would be allowed. But  
6 regulators generally find if a franchisor adds a  
7 disclaimer to an FPR, it implies the FPR is not  
8 representative or it's not accurate and it's likely to  
9 mislead.

10           Also, I want to add that if a franchisor  
11 knows key factors that causes results to vary and they  
12 don't include it, that is likely to be a material  
13 omission, and I would argue, a deceptive sales  
14 practice under both state and federal law. So I'm on  
15 board with explanations when they're specific and  
16 certainly not when they're general.

17           MR. DOAN: Okay. One of the things that you  
18 mentioned, Theresa, was -- and I believe it was  
19 mentioned by others -- is the Item 19 admonition. So  
20 under the Franchise Rule, a franchisor who makes a  
21 financial performance representation under Item 19  
22 must include a clear and conspicuous admonition that a  
23 new franchisee's individual financial results may  
24 differ from the result stated in that financial  
25 performance representation.

1           The North American Security Administrators  
2 Association, which is sometimes referred to as NASAA,  
3 has issued commentary on what those admonitions may  
4 say. So should the FTC consider adopting the NASAA  
5 commentary on those admonitions?

6           Howard, do you have a perspective on that?

7           MR. BUNDY: Josh, I'm of two minds on the  
8 issue, and I apologize to everyone in advance for the  
9 fact that I have a split personality on that. On one  
10 level, I would not advocate for adoption because NASAA  
11 is more agile than the FTC can ever be, and one of the  
12 beauties of the commentary process is that it allows  
13 for a living document that changes as the world  
14 changes, that responds as problems are heard. So at  
15 that level, I would not like to see it adopted in a  
16 static form.

17           If there is a way to adopt it in a nonstat  
18 form, so it can be a living, breathing, developing  
19 document, I would love that. So split personality  
20 today.

21           MR. DOAN: Amy, you are a franchisor  
22 attorney working in a registration, but non-NASAA  
23 state, so let me ask you. Are franchisors tending to  
24 follow the NASAA guidelines on admonitions in both, I  
25 guess, registration, non-NASAA member states and

1 nationally even in nonregistration states?

2 MS. CHENG: I would say yes. For most of my  
3 clients, I would advise them to follow the NASAA  
4 guidelines in preparing the Item 19 disclaimer  
5 because, one, you don't know if the franchisor is  
6 going to expand into a registration state or not that  
7 we would need to comply with the NASAA guidelines.  
8 And, second, frankly, I don't see any issue with the  
9 NASAA guidelines. I think it's a clear admonition.  
10 Theresa is agreeing with me for once, I think. And it  
11 helps franchisors all have a level playing field for  
12 everyone to say the same thing.

13 So now, if the question is should the FTC  
14 adopt it, I don't have concerns with the FTC adopting  
15 it. However, I'm not sure it's absolutely necessary,  
16 because I think it's -- complying with the guidelines  
17 are complying with the FTC requirement itself. So I'm  
18 not sure that if we're going to recommend for the FTC  
19 to revise the Rule, this would be, from my  
20 prospective, an important focus that the FTC would  
21 want to deal with right now.

22 MR. DOAN: Okay, thank you.

23 Lee, was there anything you wanted to add?

24 MR. PLAVE: Only that most franchisors try  
25 to have one FDD that applies throughout the country.



1 And to echo Amy's point, if you're going to prepare an  
2 FDD, you don't prepare one for some states and others  
3 for other states in the most part. As a consequence,  
4 you typically prepare it so that you're satisfying the  
5 requirements in all of the states.

6 I would add, though, that the NASAA  
7 guidelines, which are perfectly well-intentioned and  
8 are not that difficult to deal with at least on paper,  
9 didn't go through the same kind of rigorous review,  
10 comments, analysis, and sort of rule-making that the  
11 Federal Trade Commission typically adopts under the  
12 APA and the Magnuson Moss Warranty Act. So it's a bit  
13 of a different animal in terms of how it's developed  
14 and how it has become a part of the regulatory  
15 climate. I'm not sure that you would end up in the  
16 same place as you started if you went through that  
17 analysis.

18 MR. DOAN: And are you speaking to the  
19 admonition provisions of the NASAA guidance in  
20 particular or do you feel the same way about the NASAA  
21 guidance on financial performance representations  
22 generally?

23 MR. PLAVE: No, the admonitions don't bother  
24 me. It strikes me that we can all agree on what the  
25 appropriate boilerplate should be and it will end up

1 in the right spot. It's things like an absolute  
2 prohibitional ban on company-owned unit information  
3 being applied if a franchisor has any franchise units  
4 in its network.

5 I'll give you an example. We have many  
6 clients that are fairly innovative and they come up  
7 with a different design for the units they've already  
8 got. Under those circumstances, we've been told that  
9 the examiners will not permanent the use of company-  
10 owned data without franchise data, but the franchise  
11 data is for literally a different concept, different  
12 format of a unit. In the last 15 or 20 years, what  
13 has been previously called nontraditional has actually  
14 become traditional because people are constantly  
15 innovating and trying to fit the needs of the market.

16 So if a franchisor comes up with a different  
17 form out of a unit, whether it's a kiosk, a cart, a  
18 small format, a large format, a store within a store,  
19 whatever the innovation is, they may have company-  
20 owned stores where they've tried it out and given it  
21 an opportunity to pay out and they've got some  
22 results. But they don't have franchisees who have yet  
23 adopted that new format, that new model, and the like.  
24 Being able to provide information about those units is  
25 really useful, but under the NASAA guidelines it's

1 bad, because if you have any franchise units, you must  
2 give that information as well and that information has  
3 nothing to do with the kind of format of units that  
4 they're offering at the present time. So there are  
5 tensions that need to be addressed.

6 I suspect with some rational approaches to  
7 handling those things that could done, but that's just  
8 one of the examples of why I think it would be really  
9 useful to have a more formal vetting of that with  
10 commentary and with responses to the comments and full  
11 analysis that I know is typical of an FTC rule-making.

12 MR. DOAN: Thank you, Lee.

13 Unless anybody else has anything else on  
14 disclaimers, I would like to move to a related topic,  
15 which is waivers of reliance.

16 So under the Franchise Rule, franchisors may  
17 not require franchisees to waive reliance on  
18 representations in the franchise disclosure document  
19 or its exhibits or attachments. The Rule does allow  
20 franchisors to use integration clauses, so long as the  
21 clause does not purport to disclaim liability for  
22 statements authorized by franchisors in their  
23 disclosure documents.

24 So my first question is, do waivers and  
25 integration clauses remain a problem in 2020?

1                   Brandon Moore, do you have a perspective on  
2     this?

3                   MR. MOORE: Yes. Absolutely I think these  
4     clauses are a problem. Essentially, they give any  
5     person involved in the sales process a license to  
6     stretch the truth in order to make a sale. Obviously,  
7     FPRs are the most hotly discussed issue when it comes  
8     to this, so I don't think that we need to discuss them  
9     too heavily. But during the due diligence process,  
10    franchisees are asking dozens of questions and  
11    reviewing marketing materials surrounding the  
12    opportunity. Some of them might relate to the actual  
13    business model, the services that they'll be able to  
14    offer, what product lines they gain access to, even  
15    what level of support or service they can expect as  
16    part of their royalties, or even the experience  
17    necessary to survive in the franchise.

18                  The answers to these questions and marketing  
19    materials are then used as part of their decision-  
20    making process. They repeat it to their business  
21    partners, their family, their friends, and then  
22    they're taken to perform competition analysis. They  
23    study the proposed territory, their location. They  
24    build a business plan and even construct a pro forma  
25    based off of these representations.

1           In some cases, the time comes when the  
2 franchisee realizes that the opportunity wasn't  
3 necessarily as described and perhaps a discrepancy  
4 with the representation that was material to their  
5 purchase decision. By this time, it's frequently too  
6 late and they've already signed a franchise agreement  
7 with an integration clause and then they cannot afford  
8 a multi-year legal battle with bills going into the  
9 hundreds of thousands of dollars.

10           Instead, they likely go on to fail as a  
11 business owner and they file bankruptcy and all of the  
12 negative things that come with that. When this does  
13 happen because the franchisor knew that they could say  
14 whatever was necessary to make the franchisee  
15 comfortable with signing, whether or not it was  
16 accurate, and then hide behind the integration clause,  
17 at that point, there's really no other options left  
18 for the franchisee except to hope for regulatory  
19 intervention.

20           MR. DOAN: Thank you, Brandon.

21           Howard, is your experience representing  
22 clients the same as Brandon's?

23           MR. BUNDY: I think Brandon pretty much said  
24 it all, that it's not even the existence of the  
25 integration clause that's the big issue, it's how it's

1 used. An integration clause, in its pure sense, is  
2 nothing but telling the parties that there are no  
3 agreements outside of the document. Where it becomes  
4 a problem is when it's presented as a defense to fraud  
5 in the inducement or deceit of the inducement. So  
6 there needs to be a way to limit the reach of the  
7 integration clauses and related waivers of reliance to  
8 just the contract issues. I have no problem with  
9 that.

10 But if we can limit it so it doesn't reach  
11 out and become a defense to fraud in the inducement,  
12 then I think we can find some common ground, and I  
13 think that would be extremely beneficial to  
14 franchisees who are investing billions of dollars in  
15 the franchises and often losing it with no remedy  
16 available except, as Brandon said, file for  
17 bankruptcy.

18 Ideally, the franchise industry is not here  
19 to enrich bankruptcy lawyers and to make money out of  
20 the U.S. Treasury, because much of what is financing  
21 for franchises comes directly out of the Small  
22 Business Administration and thus out of taxpayers'  
23 pockets. It's billions of dollars a year in losses to  
24 taxpayers that results because of -- and in large part  
25 because of these waivers and integration clauses

1 improperly applied. So yes.

2 MR. DOAN: All right. Lee Plave, do you  
3 have any reaction to that? Is the issue with allowing  
4 the inclusion of integration clauses -- is the problem  
5 the way courts look to them after there's a contract  
6 dispute? Where do you come down on this?

7 MR. PLAVE: Well, you just hit the nail on  
8 the head. You referred to a franchise agreement as a  
9 contract. It's hornbook, black letter law that in a  
10 contract, parties have the right, if not the need, to  
11 say this is the contract. Look at Corbin on  
12 contracts, California Supreme Court, 9th Circuit, 2nd  
13 Circuit, all of the circuits, a contract with an  
14 integration clause is part of American jurisprudence.  
15 It's not to say that -- again, to go back to the  
16 previous portion of our discussion, it's not to say  
17 that there is anyone disclaiming what's in the FDD.  
18 But it is entirely reasonable for parties to say, our  
19 contract is what's in this document and nothing else.

20 It's no different in the world of  
21 franchising than it is in the world of buying a car or  
22 signing a lease for commercial real estate, buying a  
23 home, or any other transaction. An integration is  
24 fully understood and accepted throughout the American  
25 legal jurisprudence. Changing that here wouldn't make

1 any sense at all.

2           The issue is really being able to read and  
3 understand the contract. And if a franchisee has an  
4 issue with that, and I can certainly understand why  
5 that would be the case, they need to engage counsel,  
6 experienced competent counsel to assist them. If they  
7 choose not to spend the money on counsel when they are  
8 making an investment of this nature, then I feel badly  
9 for them, but that's not the smart decision to make.  
10 You would no sooner buy a home without some lawyer  
11 involved to help you understand the provisions than  
12 you would sign a contract of this magnitude without  
13 having a qualified and experienced lawyer. I think  
14 that's the right way to go.

15           MR. DOAN: Theresa, do you have a  
16 perspective on this as a regulator or do you view this  
17 as more a dispute between the parties to the contract?

18           MS. LEETS: Oh, no, it goes so much further.  
19 I think -- and I realize, technically, as an attorney,  
20 I agree with what Lee is saying, but I think it's only  
21 part of the story, and I think Brandon spoke to the  
22 other part.

23           Integration clauses illustrate the power and  
24 information imbalance in the franchise relationship  
25 that favors the franchisor, and these clauses



1 circumvent investor protection. If the public policy  
2 is to prevent false and deceptive sales practices,  
3 then we need to modify these integration clauses,  
4 right, and they need to have language that don't allow  
5 the franchisor to prevent a franchisee from bringing a  
6 claim for false and deceptive sales practices, right.  
7 And these clauses should also allow franchisees to  
8 rely on representations made by former and existing  
9 franchisees.

10           The Rule recognizes that existing and former  
11 franchisees offer material information about the  
12 franchisor, the franchise system and the relationship.  
13 But these integration clauses say, look, if it's not  
14 in the FDD, you can't rely on it and you're not  
15 relying on any representations made and, yet, they  
16 don't have to make FPRs. So a lot of information that  
17 people need to make an informed decision are not in  
18 the contract, they're not in the FDD, and these  
19 integration clauses circumvent the franchisee's  
20 ability to bring a lawsuit, if they even have the  
21 money to bring a lawsuit.

22           So I think fairness requires disputes over  
23 false and deceptive sales practices should be  
24 determined by a trier of fact and not by an  
25 integration clause, because when allegations of fraud

1 are proven, it allows the industry to identify,  
2 remove, or rehabilitate bad actors. And it's  
3 necessary for investor protection. So transparency,  
4 accountability in the sales process, it preserves the  
5 integrity of franchise channel of commerce.

6 So yes, integration clauses are a normal  
7 part of contract law, but the franchise relationship  
8 is a very different creature, and I think we have to  
9 recognize the power and information imbalance favors  
10 the franchisor.

11 MR. DOAN: Amy Cheng, I couldn't tell  
12 whether you were agreeing with Theresa there and  
13 suspected you might not be. Anything you'd like to  
14 add?

15 MS. CHENG: Not fully in this instance. So  
16 a couple points. I absolutely agree with Lee that you  
17 would be taking away one of the basic principles in  
18 contract law if you take away the integration clause,  
19 and I don't see why this relationship is any different  
20 than any other relationships, right, that are governed  
21 by a contract.

22 But, also, if you look at it from a  
23 franchisee's perspective, if I'm a franchisee,  
24 wouldn't I want to know the terms of my relationship?  
25 I would want to know as well. So I'm not sure that

1 taking away the integration clause protects the  
2 franchisee from that perspective as well.

3 A franchisee is entitled -- two parties are  
4 entitled to know the terms of their relationship. And  
5 without documenting it on a piece of written  
6 agreement, I don't know how anybody would ever be able  
7 to guess their obligations, future obligations during  
8 the relationship, right.

9 And, two, I don't agree that taking away the  
10 integration clause is the way to go so that  
11 franchisees cannot sue franchisors for fraud. There  
12 are many claims that I think franchisees have  
13 successfully brought under state false and deceptive  
14 trade practice acts and where franchisees have  
15 prevailed, right. And we have gone many years now  
16 with integration clauses in most of these contracts  
17 where franchisees have prevailed, where the  
18 circumstances are correct for them to do so.

19 So I'm not sure taking the integration  
20 clause really would -- having the integration clause  
21 would prevent the franchisees from bringing those  
22 lawsuits. I think franchisees will be able to bring  
23 those lawsuits and will continue to be able to prevail  
24 if the circumstances are there.

25 And, third, if you take away from the

1 integration clause and now we don't have the agreement  
2 in writing, right, what happens if a franchisee or a  
3 franchisor transfers the agreement? Franchisees and  
4 franchisors assign franchise agreements all the time.  
5 Franchisees sell their businesses. Some buyers assume  
6 existing contracts while others may sign a new  
7 contract. It takes away the ability, frankly, for a  
8 franchisee to be able to do that and for a franchisor  
9 to be able to assign a contract. Who would spend  
10 money to purchase a contract where they don't  
11 understand and can't rely that the terms of the  
12 contract will continue going forward?

13 MS. LEETS: So can I respond to that, Josh?

14 MR. DOAN: Sure, and then let me go to  
15 Howard and Lee after that.

16 MS. LEETS: Really quickly. Yeah, I agree  
17 with what Amy is saying in that certain integration  
18 clauses are okay. It's that part of the integration  
19 clause that says that the franchisee did not rely on  
20 or have any representations outside the FDD. That's  
21 the problem part, and that's the part that has to be  
22 removed or limited, and that's the part that prevents  
23 franchisees from bringing lawsuits, not the standard  
24 integration clause saying this is the intents of the  
25 parties. Absolutely, that should be in the agreement.

1                   MR. DOAN:   Okay, Howard, do you have  
2 something you would like to add?

3                   MR. BUNDY:   Thank you.   I wanted to take  
4 issue with something that Lee said and that also came  
5 up in the first workshop this morning, and that is the  
6 statement that franchisees, before they invest, should  
7 consult with someone like me before they invest.   The  
8 reality is somewhere different from that.

9                   Prospective franchisees tend to come to the  
10 table with a mixed bag of experience, out of large  
11 corporations, they're retired teachers, they're young  
12 couples, almost never having business experience.  
13 Their first thought is not to talk with lawyers.   They  
14 are talking with the sales rep or the franchise  
15 executive that's trying to sell them the franchise.  
16 And throughout that process, they are being told, both  
17 directly and through more subtle means, that they  
18 should not waste their money on lawyers because this  
19 document's been reviewed and approved by the  
20 Government and it's a safe investment because of that,  
21 and, besides, we don't negotiate anything, we won't  
22 change asking anything.

23                   That results in prospective franchisees  
24 saying, well, if they won't change anything, if they  
25 won't negotiate anything, why should I spend a few

1 thousands dollars having a lawyer look at it? And,  
2 yes, that is a wrong decision, but that is the  
3 decision that's being driven by the sales process.

4 And believe it nor not, even that set of  
5 misrepresentations that leads to those bad decisions  
6 to not hire counsel is wiped out by these clauses that  
7 we're here to talk about today.

8 MR. DOAN: Lee Plave, what would your  
9 response be?

10 MR. PLAVE: Yeah, it will come as virtually  
11 no surprise that I disagree with virtually everything  
12 that Howard just said. But I would -- you know, I'm  
13 not going to refer to him the way that Vincent  
14 Laguardia Gambini might have responded.

15 But the reality is, what you've described,  
16 Howard, and to a degree also what Theresa described,  
17 was an information imbalance. And that's precisely  
18 what disclosure is intended to address. I'm not aware  
19 of the instances that you're talking about -- and I'm  
20 sure that when the rule-making record opens up, you'll  
21 put in copious evidence of that. I'm not aware of  
22 franchisors that discourage prospective franchisees  
23 from talking to lawyers. Precisely the opposite.

24 But to address that imbalance, the easiest  
25 thing to do would be to have the FTC require

1 boilerplate that says, this is a serious investment.  
2 We recommend strongly that you seek out counsel with  
3 experience in this area and an auditor with experience  
4 in this area. I was part of the FTC's team that  
5 regulated used cars and funerals years ago. As  
6 expensive as those are, they pale in comparison to the  
7 cost of buying a franchise.

8           Buying a franchise is an investment that  
9 runs somewhere between \$50,000 on the low end and well  
10 north of \$1 million on the high end. It's just  
11 inconceivable to me that somebody would make a  
12 judgment of that nature and elect not to hire counsel  
13 because it's too expensive. If you're going to spend  
14 that kind of money, you make the choice of hiring  
15 counsel. And if you choose not to, that's not a  
16 choice that's attributable to the other side of the  
17 equation.

18           The FTC, however, can address that imbalance  
19 by adding a disclaimer -- not a disclaimer, a  
20 statement that -- yeah, a disclaimer -- a statement  
21 that would tell the franchisee go out and find a  
22 lawyer, go out and find an accountant. I think that  
23 would be a really useful thing to achieve the public  
24 policy goal of encouraging people to hire folks like  
25 Howard or talking to Brandon or talking to other of

1 their colleagues who know what they're talking about.

2           And even if they don't get changes in the  
3 agreements, get an assessment of what the contract is  
4 that you're signing. It's a critical thing. And the  
5 notion that you can rely on anything that somebody  
6 said is really interesting. We've seen franchisees as  
7 well make statements about their own experience, their  
8 past. It's got to, at some point or another, say,  
9 okay, we're done. That's the parol evidence rule.  
10 Centuries of jurisprudence suggest that that's the way  
11 to go. I don't see how the franchise world is much  
12 different.

13           However, if you do believe that there is an  
14 information imbalance, as Theresa suggests, while I  
15 don't know specifically what information that is or  
16 how you deal with that, I'd suggest that additional  
17 disclosure or additional mandatory boilerplate  
18 language to explain you cannot rely on things that  
19 were told to you before you sign this contract -- read  
20 this contract; this is the entire ball of wax. If you  
21 have statements to that effect, you put somebody on  
22 notice through the regulatory process that what they  
23 might have heard earlier just doesn't have any bearing  
24 on what goes forward from here on out. I think that's  
25 the better way to proceed.



1                   MR. DOAN: Amy, I couldn't tell whether  
2                   there was something you wanted to add. Did Lee cover  
3                   it all?

4                   MS. CHENG: I think Lee covered most of it.  
5                   But I think there is a misconception that franchisors  
6                   don't want franchisees to read the FDD and read the  
7                   agreement. I can tell you that most of my clients not  
8                   only want them to, but they actually spend a lot of  
9                   time walking franchisees through these documents to  
10                  explain. Because as a franchisor, frankly, you don't  
11                  want to get into a relationship with somebody who has  
12                  not read the contract.

13                  I tell my clients all the time, you'd rather  
14                  sell a franchise to somebody who has read the contract  
15                  and understands the terms of the relationship than  
16                  somebody who goes in there with their eyes closed. So  
17                  franchisees also, they do have a responsibility to do  
18                  so. If they're going to spend half a million dollars,  
19                  it's amazing how many people will spend half a million  
20                  dollars and not spend the money to have an advisor to  
21                  advise them regarding the contract, if necessary.

22                  MR. DOAN: Thank you, Amy.

23                  Let's talk about the questionnaires and  
24                  acknowledgments then, if we can move on. My  
25                  understanding is that some franchisors use

1 questionnaires or acknowledgments during the sales  
2 process. How prevalent is the use of those documents  
3 and how and at what stage of the negotiation or  
4 discussion of a potential franchise relationship are  
5 the questionnaires or acknowledgments presented to  
6 franchisees?

7           Brandon Moore, do you have a view on that?

8           MR. MOORE: Yeah. Typically, this  
9 document's presented on the tail end of signing the  
10 agreement as kind of a followup, oh, one last item, we  
11 just need you to sign this. Typically, franchisors  
12 may say, I need you to answer favorably towards the  
13 franchisor for all of these questions or else you  
14 might not be able to get the franchise. I've only  
15 heard of one instance where somebody documented this,  
16 or that they did receive, you know, something -- they  
17 did answer unfavorably towards the franchisor.

18           But also, too, what's curious about this is  
19 that if you have any questions about the definitions  
20 of the things that you're asking to -- about the  
21 question, such as, what is an FPR, you know, in the  
22 same breath that they're asking you to fill out this  
23 form, they're also going to tell you, oh, well, don't  
24 worry about what an FPR is, you've never seen one  
25 because we don't make them. And so there is a little

1 bit of an issue with defining things.

2 And this goes back to what Mr. Plave was  
3 stating. You know, I think an attorney might help in  
4 this scenario, but at the same time, I think it's an  
5 interesting point of debate.

6 MR. DOAN: Thank you, Brandon.

7 Howard, is Brandon's description also your  
8 experience working with these questionnaires and  
9 acknowledgments on behalf of franchisees?

10 MR. BUNDY: Yes, it is, Josh. Very much the  
11 same experience. We've seen hundreds of prospective  
12 franchisees over time and I don't think I have ever  
13 seen a questionnaire -- I'm trying to remember here on  
14 the spot -- but I don't think I have ever seen a  
15 questionnaire filled out by a franchisee where there  
16 was other than the desired answer provided, where the  
17 franchisee actually became a franchisee.

18 I've seen a couple of instances where, under  
19 pressure from certain attorneys, the franchisee told  
20 what I would characterize as the truth. Yes, I did  
21 get FPRs or, yes, I did get these outside statements.  
22 But those people never became franchisees.

23 Can I tell you why that happened? No. But  
24 there's an interesting coincidence that of all of the  
25 franchisees that we've seen over the years, with the

1 almost ubiquitous presence of those questionnaires,  
2 we've never seen one where the franchisee had  
3 answered, yes, I got impermissible information, and  
4 here it is.

5 MR. DOAN: Amy Cheng, let me ask you this.  
6 Is there a benefit to franchisees in having a  
7 franchisor provide them with the questionnaire  
8 acknowledgment document or does it strictly benefit  
9 the franchisor?

10 MS. CHENG: No, I think it absolutely may  
11 benefit the franchisee as well. So contrary to the  
12 way Howard would describe this document would be a  
13 disclaimer, I don't think this document is a  
14 disclaimer in any way. It is a questionnaire. It  
15 literally is a set of questions. So if a franchisee  
16 answers a question -- let me give you an example.

17 One of the many questions probably --  
18 typically, is have you received any financial  
19 information from any franchisor representative other  
20 than what is contained in Item 19 of the FDD? Now, a  
21 franchisee may answer yes, and they write down, so-  
22 and-so told me this information. Well, if the  
23 franchisor receives that document, what I have seen,  
24 actually, is that the "so-and-so" is another existing  
25 franchisee who provided this prospective franchisee

1 with all kinds of financial information.

2 And the franchisor was able to sit down with  
3 the prospective franchisee and explain, you obtained  
4 the information from our existing franchisee, but you  
5 have to understand that this information did not come  
6 from us. There is not information that you should be  
7 relying on or information coming from the franchisor.

8 Another example is a franchisee may  
9 understand that they're buying a business and they're  
10 getting -- a franchisee will fill it out and say,  
11 well, I got information from the seller of an existing  
12 franchise business that I'm buying. Again, as the  
13 franchisor, you can explain -- where they got the  
14 information on and explain that the information is not  
15 from the franchisor. So they have an obligation to do  
16 their own due diligence, right. A franchisor cannot  
17 verify the financial information that they received  
18 and they will tell the prospective franchisee make  
19 sure that you do your due diligence.

20 So as a prospective franchisee, I do think  
21 you may benefit from getting that information. There  
22 have been many circumstances over the years, where  
23 these examples I'm giving have happened and they're  
24 real, live examples where the franchisee did go back  
25 to the person from whom they received the information

1 and was able to verify the information and do their  
2 own due diligence.

3 MR. DOAN: Lee, I think you had something  
4 you'd like to add.

5 MR. PLAVE: I think Amy makes some cogent  
6 points here. And I would simply say this, the  
7 questionnaire that asks did you get any information  
8 about gross revenues, other than what's in the FDD,  
9 there's no disclaimer in that. You're not saying we  
10 don't stand behind our Item 19 or we say that  
11 everything we said in the Item 19 is not true or we  
12 stand back from it. It's asking the simple question,  
13 did you get information that was any different than  
14 what you got in the FDD?

15 I have seen people who answered that yes.  
16 The franchisor then takes it, looks seriously at it,  
17 determines what went on. Amy gave some examples of  
18 that; I've seen others. It actually also serves an  
19 additional point and an additional process. The point  
20 of public policy is to get people to comply with the  
21 law. Whatever the law is, that's the point of public  
22 policy.

23 If you have the accountability of a sales  
24 team that knows it's about to be discovered if it made  
25 some sort of an illegal FPR, because as soon as the

1 franchise agreement is submitted to be signed, and the  
2 questionnaire is there, the information is going to be  
3 laid bare, why then, at that point, the salesperson is  
4 a whole lot less likely to do something for which they  
5 will be held accountable.

6 Now, Howard suggests that franchisors  
7 routinely have their sales team telling people to sign  
8 it, no matter what, whether it's true or not. The  
9 document says -- and usually concludes with -- we're  
10 relying on your answers, please be honest and truthful  
11 and complete. Again, if somebody can't answer  
12 questions on an honest basis, then there's a problem.

13 I could tell you in my own experience I have  
14 seen that questionnaire used. It is quite prevalently  
15 used, and ironically, it was the instigation of the  
16 Maryland Examiner roughly 20 years ago that suggested  
17 it would be a great way to handle things, other than  
18 using disclaimers. And that suggestion seems to have  
19 led to the use of these questionnaires.

20 But I have seen the questionnaire used. I  
21 have seen a franchisee who asked its counsel to call  
22 us up and threaten one of our clients with a lawsuit.  
23 And when we sent the franchisee's questionnaire to his  
24 counsel, it revealed, among other things, the three or  
25 four different things that he had told his counsel

1 that were not true. His counsel didn't take the case.  
2 There were other pieces to it as well.

3 The point is not everybody remembers  
4 everything with clarity in the years to come. If you  
5 have the opportunity to memorialize what took place  
6 just now, did you get any of this information, do you  
7 understand the information that you got? If not,  
8 would you like some more information, some more  
9 explanation. That serves a useful purpose and it's  
10 consistent with public policy.

11 MR. DOAN: Howard, did you want to respond  
12 to that?

13 MR. BUNDY: Yes. I think it needs to be  
14 clear that I do not oppose and I don't think most  
15 franchisees oppose a checklist of facts as to what  
16 they did or did not do in the due diligence process.  
17 I think there can be a benefit to both franchisees and  
18 franchisors in having a formalized checklist. Again,  
19 my problem, as I alluded earlier, is not so much in  
20 what the surface of the document says, but in how it  
21 gets you in the defense of claims by franchisees.  
22 All of a sudden, that sentence that says, I did not  
23 receive any inconsistent information about becomes I  
24 waived any claims made because I received information  
25 that I didn't understand to be inconsistent.



1           It simply gets applied on the defense of  
2   claims in a way that is not consistent with the FTC's  
3   goal in creating a level playing field of information  
4   and of remedies, potential remedies for franchisees  
5   who get misled in the process.

6           MR. PLAVE: Could I just say one thing on  
7   that?

8           MR. DOAN: Sure, briefly, and then I know  
9   Amy wants to add something, too.

10          MR. PLAVE: Oh, sure, I'm sorry. I'll just  
11   be brief on this. Howard raises a fair point, which  
12   is that if you don't understand the question, then the  
13   answer is somewhat more murky than it should be. But  
14   if the question is properly posed and the answer is  
15   honestly given, then, at that point, the only thing  
16   that is foreclosed is lying in the future.

17          But if you ask the wrong question, then  
18   you're going to get a murky answer, and I think that's  
19   why people should be asking the questions the right  
20   way. Forgive me.

21          MR. DOAN: Sure.

22          Amy, did you have anything you wanted to add  
23   to that?

24          MS. CHENG: Yeah, a couple of things. One  
25   is the timing of the document, I don't think it's

1 correct that this document is slipped in at the last  
2 minute to a franchisee when they're about to sign the  
3 franchise agreement. It does come with the execution  
4 of the agreement. However, it is attached as an  
5 exhibit to the FDD, so the franchisee has had the  
6 opportunity to review this document, along with all  
7 the other documents.

8 Under Item 22 of the FTC Rule, you're  
9 required to attach all documents that the franchisee  
10 must execute in connection with the purchase of the  
11 franchise. So if a franchisor is including this  
12 document, it should be attaching it as an exhibit to  
13 the FDD.

14 And, second, I don't think that the answer,  
15 no, I did not receive any financial information,  
16 necessarily precludes, in all instances that kind of  
17 Howard alluded to, a franchisee from bringing a claim.  
18 And, in fact, there have been many lawsuits, I think,  
19 over the years -- if you read some of these decisions  
20 -- where a franchisee has executed a questionnaire,  
21 has answered a question that they did not receive.  
22 However, their attorney was able to bring in  
23 sufficient evidence that that was incorrect, and there  
24 was information provided outside of Item 19 where a  
25 franchisee was able to prevail.

1                   So I don't think that it is just because the  
2 franchisee answers no it immediately precludes them.  
3 And, again, this is not a waiver. This is not a  
4 waiver of claims. It's very different. It's simply a  
5 questionnaire.

6                   MR. DOAN: Theresa, is there something you  
7 would like to add?

8                   MS. LEETS: Yes, I definitely have a  
9 regulatory perspective on this that might be a little  
10 bit different. I question how this questionnaire got  
11 into this document. It definitely didn't go through a  
12 rule-making process and was less vetted than the NASAA  
13 FPR commentary, for instance. But it is, I think,  
14 very helpful for a regulator to see the questionnaire  
15 flags areas that it appears that the franchisees  
16 commonly failed to understand in the franchise  
17 relationship.

18                   And this goes back to the power imbalance.  
19 And it does have the impact of preventing franchisees  
20 from being able to bring lawsuits. And a lot of the  
21 information in that questionnaire is not in the FDD.  
22 And let me give you a quick example. I'll give you  
23 three examples.

24                   One of the things a franchisee is commonly  
25 required to agree is that they read and understood the

1 FDD, right. But the rule doesn't say anything about  
2 whether the franchisee is literate, whether they can  
3 read English, whether the FDD was disclosed in  
4 language that was suitable to their education, reading  
5 comprehension level. So we are making a lot of  
6 assumptions that may not be true, that they understood  
7 a very complex and long document.

8           Second, franchisees are required to do their  
9 due diligence, their independent investigation of  
10 market conditions and competitive factors. Yet, the  
11 franchisor is usually the number one source of that  
12 information and they don't have to disclose that in  
13 Item 1. So if you're going to ask that on the tail  
14 end of a questionnaire that's not expressly  
15 authorized, you'd better be amending the rule to make  
16 sure that they're disclosing in the FDD information  
17 about competition and market conditions.

18           Last example, another one that the  
19 franchisees have to agree to is that their business  
20 abilities and efforts are vital to success. Again,  
21 many people are recruited and told they don't have to  
22 have any business experiences. Yet, in Item 15 of the  
23 FDD, the only thing the franchisor has to disclose is  
24 whether or not the franchisee has to participate in  
25 the business.

1           Item 15 has to be amended if we're going to  
2 include that language in the questionnaire to add a  
3 disclosure about business abilities, skills,  
4 knowledge, and time commitment needed to run the  
5 business being offered. Otherwise, we have a  
6 disconnect between what's in the FDD and what's in the  
7 questionnaire and what people need to know to make an  
8 informed business decision.

9           This is about a relationship and I think you  
10 have to have a better transfer of information if we're  
11 going to have a better outcome in this channel of  
12 commerce.

13           MR. DOAN: Howard, is there something you  
14 would like to add to the discussion on that point?

15           MR. BUNDY: I would second what Theresa  
16 said. The point that I wanted to make -- and I'll try  
17 to make it quickly -- is that I think part of what the  
18 Commission needs to understand is that not all  
19 franchisors out there are McDonald's or the big names  
20 that we hear in franchising all the time that have  
21 very sophisticated, qualified counsel guiding them to  
22 make sure that they do a good job.

23           There are some good franchisors who have  
24 been at it a long time and they've figured out how to  
25 hire Lee or Amy to do a good job for them. The

1 franchisors that I see, the franchisors that Theresa  
2 sees, to a large extent, are much less sophisticated,  
3 much less experienced, and, frankly, much less honest.  
4 They don't care as much about being sure that their  
5 franchisees understand. What they care about is that  
6 the franchisee can fog a mirror and sign a check.

7           And that is not a qualifications that the  
8 franchisors should be looking for, but that's what  
9 they're looking for because they're trying to hit the  
10 bottom line. And that's very true of a lot of young  
11 franchisors. It's also true of some of the larger  
12 ones. I recently had a case involving a franchisor  
13 that has 2- or 3,000 franchises worldwide. And they  
14 were having a fire sale of franchises, selling them in  
15 five-packs. And the tales they were telling about how  
16 well these franchisees were going to do, the  
17 spreadsheets that they were putting up on webinars  
18 like what we're doing today, were very impressive.  
19 I mean, were I not in the role that I am, it would  
20 have been tempting to me to buy a pack of those  
21 franchises.

22           They failed in droves. So I think the --  
23 you know, we create traffic laws for the person who is  
24 careless and runs a stop sign and hits a child. But  
25 that same traffic law also impacts the person who's

1 very, very careful, who has never had an accident.  
2 That doesn't mean we don't need the traffic laws. And  
3 we need them to be strong and firm, and in this case,  
4 to make sure that the franchisee, A, has access to  
5 really solid, reliable information, complete and  
6 truthful information, and that at the end their remedy  
7 is not taken away from them through terms hidden in  
8 contracts and then suddenly become the billboard the  
9 minute a claim is made.

10 MR. DOAN: Thank you, Howard. I did want to  
11 add one point addressing some of the discussion  
12 earlier about the Franchise Rule and recommending that  
13 franchisees have counsel or an accountant to help them  
14 review the franchise disclosure document. And I did  
15 just want to point out that under the Franchise Rule  
16 as currently written, I believe it's 16 CFR  
17 436.3(e)(3), the franchise disclosure document must  
18 state on the first page that the terms of the contract  
19 will govern your franchise relationship. Don't rely  
20 on the disclosure document alone to understand your  
21 contract. Read all of your contract carefully. Show  
22 your contract and this disclosure document to an  
23 adviser, like a lawyer or an accountant.

24 So I did just want to point out that the FTC  
25 already has included language to this effect in the

1 Rule and requires it in the document.

2 I think we only have about -- well, my clock  
3 just actually turned. So I think we're out of time  
4 for better or worse. I know it's been a great  
5 discussion. I want to thank you all for being such  
6 lively panelists and thanks for appearing. And I  
7 believe we have a 10-minute break before the next  
8 panel. Thank you, all.

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First Version

Reviewing the Franchise Rule - Workshop

11/10/2020

1 THE PROS AND CONS OF THE CURRENT FDD FORMAT

2 MR. MAXSON: Good afternoon, everyone, and  
3 welcome to the third and final panel of our workshop  
4 today. This panel is titled, Pros and Cons of the  
5 Current FDD format. We'll be running about 50 minutes  
6 today.

7 Just a housekeeping matter, on behalf of  
8 myself and all of the panelists, I'd like to note that  
9 the views we express today are our own and don't  
10 necessarily reflect the views of the Commission or of  
11 any one particular organization, law firm, or company.  
12 Also, if we have time, I'll try to incorporate  
13 questions that we get from viewers. If you have any  
14 questions, please submit them to franchiserule@  
15 FTC.gov.

16 So we have a great panel today. I would  
17 encourage everyone to go online and read everyone's  
18 full bio. I'm going to give a very quick overview of  
19 everyone that will not do justice to their full bio,  
20 but just so you know who we've got here.

21 So if you've watched the whole day, you have  
22 already seen Dale Cantone. He is an Assistant  
23 Attorney General for the State of Maryland and the  
24 Deputies Securities Commissioner for the Maryland  
25 Securities Division. Mr. Cantone is the Chief of the

1 Franchise and Business Opportunity Unit.

2 Kimberly Crowell, along with her husband,  
3 cofounded a company that owns and operates 33 Jersey  
4 Mike's Subs restaurant franchises, with 13 stores in  
5 development and employs approximately 300 people.

6 Ronald Gardner is a partner at Dady &  
7 Gardner, P.A., who limits his practice to the  
8 representation of franchisees, franchisee  
9 associations, dealers and distributors, and their  
10 relations with their franchisors, manufacturers, and  
11 suppliers.

12 Earsa Jackson is a partner in the Dallas  
13 Office of Clark Hill and the team leader for the  
14 firm's Franchising and Licensing Group.

15 And Carl Zwisler is senior counsel and a  
16 member of the Lathrop GPM Franchise and Distribution  
17 Practice Group in Washington, DC.

18 So today, we're going to talk in this panel  
19 about financial disclosure documents. We've talked  
20 some today already on what should be included in  
21 those, whether there are things that should be added  
22 to them, changes that should be made to FDDs as far as  
23 the substance of what might be in them or whether  
24 they're appropriate the way they are now. What we're  
25 going to talk about some is really the structure, the

1 layout, and the length of FDDs.

2           And so we're going to start out talking  
3 about the length of FDDs. So I'm going to start out  
4 with Carl, and ask him, so financial disclosure  
5 documents are often hundreds of pages, very long  
6 documents in many cases. Does the length of the FDDs  
7 deter prospective franchisees from reading them?

8           MR. ZWISLER: Well, thank you for the  
9 question and for inviting me to participate on this  
10 panel.

11           Let me start by saying that I agree with  
12 Congressman Hern who kicked off this whole afternoon  
13 by saying that, by and large, I think the Rule is  
14 functioning effectively and that the disclosures, as  
15 required in the current formats, work and they work  
16 reasonably well.

17           I'd also like to note that, as much as we  
18 all want the FDD to be readable and understandable by  
19 everybody else, the Rule's mission is to require  
20 franchisors to provide material information to  
21 prospective franchisees. It's not to require  
22 prospective franchise to read the information, as much  
23 as we would like to have them read it, which is not to  
24 say they should not be readable.

25           But I think, first of all, the longer the

1 document, from my personal perspective, the less  
2 likely I am to be interested in reading all of it.  
3 That's just me, and I suppose it's a lot of people.  
4 My wife, who is an English major, she read all kinds  
5 of long books, and I could never put up with all of  
6 that volume.

7           But I don't think that's the only reason  
8 some people don't read FDDs. First of all, many  
9 prospects today are introduced to a franchise or very  
10 early on in their consideration of a franchise, speak  
11 with trusted referral sources. And if they trust the  
12 referral source who shares a success story with their  
13 franchise operation, that may mean a lot more to them  
14 than details about the franchise and the franchise  
15 relationship that are spelled out in an FDD.

16           Other prospects probably feel confident from  
17 the reviews that they've read online about the  
18 franchisor, and they make up their minds about that  
19 without first looking at an FDD. And as any of us  
20 know who have gone online to search for a franchise,  
21 you can find comparisons of franchises, rankings of  
22 franchises, lists of unhappy franchisees of  
23 franchises, if the franchisor has been in problems,  
24 there are stories about what the problems are on the  
25 franchise relationship. So there's a wealth of

1 information that will steer people either to proceed  
2 or back away that may be more important in some  
3 respects than what's in the FDD.

4 Many franchisee prospects already own a  
5 franchise. In fact, the majority of franchisees own  
6 more than one. So it may be less likely that they are  
7 going to read an additional FDD when they make a  
8 second investment.

9 And, finally, for some people, they're just  
10 disinclined to read things, like instruction manuals  
11 and assembly manuals. They'd rather do it themselves  
12 and they just don't want to take the time.

13 So I don't know that we can address those  
14 issues with everybody or with an FDD, but I do think  
15 it's important that when we evaluate the role of FDDs  
16 and whether they are readable and usable right now, we  
17 look at the data. And there is very little data  
18 that's available about franchisees' experience with  
19 FDDs. The only one that I have been able to find is a  
20 2015 survey by franchise grade in which 1,122  
21 franchisees were asked whether they had read and  
22 understood the FDDs they received.

23 Seventy-two percent of them said they had a  
24 clear understanding of the obligations and commitments  
25 within franchise agreements. Eighty-two percent

1 reported having read the FDD in the franchise  
2 agreement, and 76 percent said that they had consulted  
3 with an attorney or an accountant. So despite surveys  
4 of so-called franchise experts and those of us who  
5 only get involved in the process when we have  
6 complaining franchisees come to us, the only research  
7 that seems to be credible out there says that  
8 franchisees do read the research.

9 Now, I think it's also important to put the  
10 FDD and the research in context. The survey that I  
11 just mentioned, as well as a couple of others of  
12 experts, really focus on existing franchisees. What  
13 it doesn't focus on is the franchise sales process.  
14 And according to Fran Connect, which regularly reviews  
15 franchise sales and tries to help its clients find  
16 more efficient ways to sell franchises, only about 1  
17 percent of all franchise leads is converted to an  
18 actual franchise sale. That means 99 out of 100 may  
19 or may not get the FDD and read it, and they're making  
20 their own decisions about whether to buy a franchise.

21 So if we're going to look at the validity  
22 and the helpfulness of an FDD, I think we need to look  
23 at research about what these prospects are who never  
24 concluded a franchise arrangement. So I'll leave it  
25 here at that point. But I think it's important to

1 look at the data and that there should be more data  
2 before any material change is made relating to  
3 readability of a franchise agreement and an FDD.  
4 Thanks, Will.

5 MR. GARDNER: If I might, Will, I don't  
6 think you have to go a lot farther in terms of surveys  
7 -- and I'm not sure what the one survey Carl found on  
8 the internet seems to -- deemed it to be credible,  
9 because I'm not sure we have any idea how they  
10 collected that information. I don't think you have to  
11 go much further, frankly, than looking at the  
12 resources surrounding the litigation that exists with  
13 franchisees and franchisors to get a sense of how many  
14 franchisees feel like they're not getting the  
15 information that they need, and in part because of the  
16 FDD and its sheer breadth.

17 I don't disagree with Carl that people could  
18 have lots of different reasons for not reading it, but  
19 that doesn't mean that you don't attack one that  
20 you're aware of. You know, when you get an FDD that  
21 rolls in at 1,200 pages, I don't care if you're  
22 someone who doesn't like to read or someone who is an  
23 English major, the reality is that is extraordinarily  
24 daunting. And I've seen FDDs at 1,200 pages.

25 So I don't think that there's any legitimate

1     dispute that the sheer breadth of what the FDD is at  
2     now discourages people from reading it, discourages  
3     them from understanding it. You've got to factor into  
4     this the time frame that's being -- and the pressure  
5     that's being put on a lot of these people to hurry up  
6     and purchase. We've got somebody else looking at the  
7     territory or even, frankly, we don't have anybody else  
8     looking at the territory but we need your answer  
9     within the next 14 days. You know, you just can't  
10    digest everything you need to digest in the time  
11    period in which you're expected to digest it and make  
12    a reasonable decision.

13                 So, you know, Carl and I will snipe at each  
14    other, I'm sure, on the next hour, as we've spoken on  
15    other panels together. We're good friends. So don't  
16    take it the wrong way. Neither one of us do, that's  
17    for sure. But the reality is is that my office is in  
18    business, frankly, with hundreds of clients because  
19    people were overwhelmed by the FDD or didn't get it.  
20    And there's certainly a better way to do it than the  
21    one that we have now that goes back to the '70s, when  
22    we needed to know that Kenny Rogers somehow endorsed  
23    Kenny Rogers roast beef. I mean, the fact that Item  
24    18 exists is ridiculous.

25                 So this does deserve a hard look at how you



1 can shorten it, make it more succinct, get the  
2 important information up-front. It all ought to be  
3 done as part of this review.

4 MR. ZWISLER: Ron, if I could respond very  
5 briefly. I don't want to monopolize the time. But  
6 you did mention the number of disputes that arise  
7 because of problems with FDDs. We did some research  
8 with Westlaw, and over the last three years, we've  
9 found that there are 42 franchise cases alleging  
10 disclosure fraud and/or misrepresentation. That's 42  
11 over three years.

12 And we did some further research and we  
13 found that there were -- that's an average of 14 cases  
14 a year. There were 27,000 new franchises opened in  
15 2017; 26,000 opened in 2016. I'm sure there are  
16 disputes, but they don't seem like a tidal wave by any  
17 means.

18 MR. MAXSON: Kimberly, I'd like to turn to  
19 you now. Ron mentioned these 1,200-page FDDs. Do you  
20 have any suggestions for what could be done to  
21 potentially shorten FDDs or make them more readable?

22 MS. CROWELL: Sure. And thanks again for  
23 having me.

24 I think that if we look at the FDD as yet  
25 another tool that prospective franchisees can use to

1 do their due diligence, I don't know that the length  
2 of the FDD would necessarily matter. I think it's  
3 really important that, you know, prospective  
4 franchisees understand that this is a potential  
5 playbook; this is a potential opportunity for you to  
6 learn more about a potential business that you're  
7 going to invest in. And I don't necessarily think  
8 that just saying, oh, it's too long, I don't want to  
9 read it, is a good enough excuse. I think, if  
10 anything, it's providing you with the information to  
11 then go and do additional research.

12 So, for example, if, you know, in the very  
13 beginning of the FDDs it lays out estimated  
14 investments and it provides you with additional  
15 notices of where to go, be it to the FTC website or to  
16 speak with counsel on that, I don't necessarily  
17 believe that the length is necessarily the problem.  
18 It's understanding that there's a plethora of  
19 information in there that you need to seek out and  
20 find and be able to make an educated business decision  
21 on that investment.

22 MR. MAXSON: Earsa, I'd like to turn to you  
23 now. Do you support the use or the addition of a  
24 summary document for FDDs, and if so, why or why not?

25 MS. JACKSON: Thanks, Will. Thanks for

1 having me.

2 Now, I can appreciate Ron's comment about  
3 the length of the FDD, and the fact that they are very  
4 lengthy documents. Having prepared and reviewed many  
5 of those over the years, they are very long documents.  
6 And a summary document might, on its face, seem like  
7 it's a great idea. But I would caution that there are  
8 likely some unintended consequences.

9 If we are encouraging folks to do their due  
10 diligence, do their homework, a summary might actually  
11 discourage people from looking at valuable  
12 information. I think Kim referred to it as a  
13 "playbook." I think that there's valuable information  
14 that the prospect might not get if there is a summary.  
15 They might take the summary as the gospel and not do  
16 full due diligence and make an informed decision.

17 I think that a summary document might turn  
18 into a summary kind of sales pitch-type document.  
19 Now, there is, obviously, some checks and balances if  
20 you're in a franchise registration state where  
21 someone's going to look at that. But for those brands  
22 where no one's going to look at that, I see that as a  
23 huge danger not being policed.

24 And if we are looking at this from a  
25 consumer protection standpoint, I do think that

1    there's a possibility that the most vulnerable folks  
2    might be in further peril with just relying on a  
3    summary document and thinking that that's all the  
4    information they need to make an informed decision.  
5    So I think we might fall short on the consumer  
6    protection side. So I would not be in favor of a  
7    summary document.

8                   MR. GARDNER: I actually am. But I will  
9    tell you, I've been slow to embrace this because of  
10   exactly the point that Earsa has made. I kind of got  
11   drug kicking and screaming to the idea that a summary  
12   is a good idea, for the fear that people might skip  
13   the more important stuff. But, frankly, as I thought  
14   about it and looked at the experiences that we've had  
15   in our office and my franchisee-represented brethren  
16   working with some regulators, the reality is that lots  
17   of people aren't reading the whole thing anyway and  
18   some it's probably better than none.

19                   The other thing I would say is that I don't  
20   think that the FTC should be frightened away from the  
21   idea that Earsa has raised here that there might be  
22   some nefarious people that use this the wrong way.  
23   Again, that would be happening with the FDD as it  
24   exists in nonregulated states as it is and probably  
25   is. So I don't know that the risk is any higher with

1 a summary document than it is with some sort of  
2 shorter -- or longer document or shorter document.

3 The other note that I would make about a  
4 summary is that -- and, again, back to what the FTC  
5 should be thinking about, in my opinion -- is it's not  
6 like this is uncharted territory. When you buy  
7 securities today, you get a document that has lots and  
8 lots and lots of important information, but you get a  
9 summary. It can be crafted in such a way that people  
10 get the most important information, they get it right  
11 up-front, they have a sense of what's going on, and it  
12 prompts them, if you will, to follow up on one of  
13 Kimberly's comments, to do more research and to look  
14 further in.

15 You know, at this point, people open up that  
16 FDD and they get to page, you know, 7 and they give up  
17 because where the information they actually want,  
18 there's no way to know where it is. There's no  
19 directory. There's nothing that says, you know what  
20 you really ought to start with is Item 19. You got to  
21 get three-quarters of the way through the document  
22 and, oh, by the way, all the people you need to call,  
23 they're in the back. I mean, a summary document would  
24 do so much to bring front and center the stuff that  
25 needs to be done, that needs to be used for consumer

1 protection, the same way it works in our sister  
2 industry with respect to securities.

3 And so, again, I've been slow to get there.  
4 But I do embrace the idea of a summary document at  
5 this point.

6 MR. MAXSON: Ron, are there any specific  
7 things you would suggest putting in a summary  
8 document?

9 MR. GARDNER: You know, I think we'd have to  
10 think hard about that. I think that the key  
11 information from Items 5, 6 and 7, you know, what's  
12 your up-front and how is it going to run, the key  
13 information from Item 19, what do people, when they  
14 spend this money, what kind of return are they seeing  
15 as a generalized statement.

16 I certainly think you'd want to know the  
17 description of the business, the key sort of passage,  
18 if you will, out of Item Number 1, so people know what  
19 it is they're buying. You know, I don't have a  
20 specific this is for sure. I've never mapped it out.  
21 But those of us that work in the regulatory area, the  
22 NASAA folks are well equipped to, I think, take this  
23 up, or some group that the FTC appoints -- and, Dale,  
24 I'm sorry that I might be volunteering you for  
25 something -- that take things up to craft something

1 that I think the industry would probably widely accept  
2 if they could actually see what it is.

3 Part, I think, of the hesitation that people  
4 have is we don't know what we don't know about what  
5 that might look like. I do think we could get to  
6 something that we would all likely embrace as, yeah,  
7 this is a pretty good idea.

8 MS. CROWELL: Will, if I could jump in, too,  
9 and add a couple points from the franchisee's  
10 perspective. And I've gone back and forth with the  
11 idea of the summary document. And I agree with Earsa  
12 that I don't necessarily agree that the summary  
13 document would be the way to go for the reasons that  
14 she stated, that, you know, it might deter prospective  
15 franchisees from actually diving down deeper.

16 However, if there was some sort of way to  
17 direct some of the high-level areas that a prospective  
18 franchisee would want to know about, some of the ones  
19 that Ron mentioned -- other things come to mind, you  
20 know, like retrofit requirements, terminations,  
21 defaults, transfer -- you know, I think if there was a  
22 way to pull not just some of the legalese, but also,  
23 from a practical standpoint, what would a brand new  
24 franchisee or someone looking at investing in a  
25 franchise, what are the 25 top items that they mostly

1 care about, and finding a way to incorporate that, or  
2 at least making sure that they have access to it  
3 fairly quickly so that they can get the answers that  
4 they need and then be able to make a choice on whether  
5 they want to invest.

6 MR. ZWISLER: Will, if I could comment?

7 MR. MAXSON: Sure.

8 MR. ZWISLER: First of all, I think Dale and  
9 his NASAA Committee should be commended for the new  
10 state cover page requirement that went into effect  
11 last year. And it does exactly, I think, what Ron was  
12 suggesting, which is explaining frequent questions and  
13 where to find the information in an FDD and why it's  
14 important. And I think that is a much better  
15 approach, frankly, than a summary.

16 And the principal reason for a summary --  
17 and there are different ways to do it, and I have  
18 criticized some of them in a "law review" article  
19 where there was a summary FDD proposal by another  
20 lawyer -- but I think it's deciding which thing is  
21 most important. And we've heard Ron describe a series  
22 of things that he thought should be in a summary.  
23 We've heard Kimberly describe a series of things that  
24 she thought should be in the summary. And they don't  
25 overlap, as far as I could tell. And pretty soon



1 you're getting into the full-blown 23 items of the  
2 FDD.

3           So in my opinion -- and it is my opinion and  
4 I share Earsa's and Kim's perspective -- if you have a  
5 summary, an executive summary, this is the important  
6 stuff. If these are the risk factors, well, that's  
7 what I need to focus on. God forbid I have to read  
8 the other 400 pages in this thing. That doesn't make  
9 any sense. Nobody is going to do it. They don't have  
10 the patience. So I think a summary, as good as it  
11 sounds, probably isn't going to get everybody where we  
12 want to be in this disclosure process.

13           MR. CANTONE: I think the fact that we're  
14 talking about a summary document illustrates the fact  
15 that there's a real concern about prospective  
16 franchisees reading the entire franchise disclosure  
17 document. I think that is a real concern. The length  
18 of them have increased a lot since I started doing  
19 this 30 years ago.

20           Carl, you have been around longer than I  
21 have. Probably Ron, you and I are about the same.

22           They've gotten bigger over the years for all  
23 sorts of reasons. Having said that, I'm not quite  
24 there with the summary document. I also have  
25 concerns. This might be one of the few times I agree

1 with Carl over Ron, although I understand exactly  
2 where Ron is coming from in some ways. Yet, if we  
3 could identify -- if we're ready to say clearly  
4 they're not going to review the entire disclosure  
5 document, certainly a summary document is better than  
6 nothing. I'm not ready to give up on the entire  
7 disclosure document or some variation on the  
8 disclosure document that I suspect could be improved.

9           And the reason for that is because in our  
10 law enforcement experience, you can never tell what  
11 part of the disclosures, you know, are a material  
12 piece of information that affect the franchisee's  
13 decision or prospective franchisee's decision. What  
14 part of the disclosure document would you want to cut  
15 out?

16           I mean, we've had people say that they  
17 really relied on the territory disclosures or the  
18 trademark disclosures or, you know, the required  
19 purchases or complain about the fact that they didn't  
20 read the disclosure document but it was clear about  
21 the amount of rebates and kickbacks, they call them,  
22 that the franchisor was getting. So I don't know that  
23 it would be possible to distill all the information  
24 that's in that franchise disclosure document into a  
25 summary document.

1           Although, I have to also say, as much as I  
2 appreciate Carl's shout-out to the state cover pages,  
3 the state cover pages really are not a replacement for  
4 the type of summary disclosure document that I think  
5 Ron was referring to. I think the fact that we  
6 adopted these new state cover pages is a reflection of  
7 the state regulator's concern that people are not  
8 reading the disclosure document and that many  
9 prospective franchisees find that document  
10 intimidating.

11           So the state cover sheets are kind of a way  
12 to assist a prospective franchise to maneuver through  
13 the document by including a page "how to use the  
14 disclosure document" and a page that has, you know,  
15 realistic, practical information about the one-sided  
16 nature of the franchise relationship that a lot of  
17 franchisees don't understand until it's too late. And  
18 then there's a page on risk factors that, of course,  
19 are imposed by state regulators.

20           But I don't think that anybody should  
21 conclude that that is a replacement for the type of  
22 summary disclosure document that I think we're talking  
23 about. Again, I'm not quite there. I see the  
24 utility, but I think that if we can get franchisees to  
25 read the entire disclosure document, that would be the

1 ideal. It doesn't happen currently.

2 MR. GARDNER: Well, I just --

3 MS. JACKSON: I'm a little concerned -- I  
4 think the real concern is how we kind of demystify  
5 that document. There's a resource that's been around  
6 for quite some time, and that's "The Consumer's Guide  
7 to Buying a Franchise." It's referenced in the cover  
8 of the FDD. Most people don't know that -- prospects  
9 don't know they can easily get a PDF of that document.  
10 That is, by far, kind of the most kind of detailed  
11 road map as to what is in that FDD. It's not specific  
12 to a system, but that's a resource that's out there,  
13 and we might consider whether there are some tweaks to  
14 that that might be more beneficial to address this,  
15 because I think the real issue is how to kind of  
16 demystify that document.

17 Ron referred to 1,200 pages. It is a lot of  
18 information. But giving the prospect the resources to  
19 digest it might be the way to focus here, because I  
20 think, as we've pointed out, you know, once you start  
21 trying to figure out what are the most important  
22 things for the summary, some things are going to be  
23 more important for prospects than others, depending on  
24 the system or depending on the region. So giving them  
25 the resource and equipping them with how to dissect

1 that document may be a better focus.

2 MR. GARDNER: Well, and I want to make one  
3 thing clear, I'm not actually advocating for a  
4 jettison of any parts of the FDD. What I was really  
5 talking about is the type of executive summary that  
6 you get in a securities prospectus. You know, you  
7 still get the whole prospectus. You just get a  
8 summary up front of what they see is the key  
9 information. So I didn't mean to suggest that -- and  
10 I kind of heard Dale answering like that was what I  
11 was suggesting.

12 I don't mean to suggest that we get rid of  
13 the FDD and all of the information that's in there. I  
14 am suggesting we might consider an executive-type  
15 summary up front with the most key information so  
16 people can get that quickly.

17 MR. CANTONE: And, I guess, Ron, my concern  
18 is it's hard enough for us to get prospective  
19 franchisees to read the disclosure document now. And  
20 I'm sure if we had a summary document, it would be  
21 that much more difficult to get them to focus on the  
22 entire disclosure document, if they did have an  
23 executive summary.

24 MR. GARDNER: Exactly why I told you I was  
25 very slow to come to this opinion. I don't disagree

1 that that's a risk.

2 MR. MAXSON: So we've heard both sides of  
3 this summary debate, and, obviously, different mind  
4 can have different opinions on this issue. But, Ron,  
5 let's say you don't have a summary document. Would  
6 there be any utility in reorganizing the FDD to put  
7 the most important items up front so that if someone  
8 wasn't going to read all the way through a 1,200-page  
9 document, if they read at least a certain portion at  
10 the beginning, the things that they hit first maybe  
11 are going to have the most utility to them in making  
12 their decision about buying a franchise?

13 MR. GARDNER: I think so. And, frankly, my  
14 view -- or my belief here is it could be reorganized  
15 in such a way that not only will they get the  
16 information they're probably looking for up front, but  
17 it would encourage them to keep going, because then  
18 the other issues come to bear.

19 I mean, right now, you get to Item 3, and  
20 suddenly, depending on what system you're in, you have  
21 nothing there or literally 100 pages in one system  
22 that I'm thinking of, of lists of their litigation. I  
23 mean, you're into Item 3 and you're already 100 pages  
24 in and you're reading stuff that has really nothing to  
25 do with the things that you are wondering about.

1                   So to me, I think I would reorder. I think  
2 I'd go, just off the top of my head, 1, 2, 5, 6, 7,  
3 because people want to know how much it's going to  
4 cost them to get in. 19, how much am I going to make?  
5 I then would, I think, spring board from there, what  
6 do I get. I would talk about territory. I would put  
7 in 12. How does purchasing work, 8. I mean, I think  
8 you could come up with a logical flow about the way  
9 people think about getting in the business. You know,  
10 you get interest in how much it costs and then how  
11 much could I make, but how does it really work.

12                   I think you can take the items that we have  
13 now and organize them in a fashion that not only gives  
14 people who aren't going to read as much, the more  
15 critical information up front. But like I say, if you  
16 model it about the way people approach buying a  
17 business would logically lend itself to, okay, now  
18 I'll read the next section because I'm now wondering  
19 about that. I could see how much it costs. I'm still  
20 interested. I could see how much I can make. Okay,  
21 now I'm interested in that. But how about what does  
22 the business look like? What kind of territory do I  
23 have? Who do I have to buy products from?

24                   I mean, there's lots of great information,  
25 but it's like someone took a shotgun and threw it up

1 on the wall and you have to go pick it out. And  
2 particularly when you get into the longer documents,  
3 finding it is just -- it's brutal. So I do think a  
4 reorganization, at a minimum, is in order here.

5 MR. MAXSON: So you mentioned getting 100  
6 pages in and maybe some of the stuff you read in the  
7 first few items maybe isn't as useful to you or isn't  
8 all that useful to a prospective franchisee. I guess  
9 the followup question would be then, are there things  
10 that should be cut that just aren't useful and are  
11 just adding pages and make it less likely that a  
12 prospective franchisee is going to read the whole  
13 document because it's just too long?

14 MR. GARDNER: You know, my struggle in this  
15 one is -- you know, I've already said I think Item 18  
16 ought to go away. But, right now, if there's stuff  
17 that doesn't need to be said or is minimal, it doesn't  
18 take up a lot of space. I think the challenge here is  
19 the ancillary documents. I mean, people do need to --  
20 when you get into a system where they have three  
21 different versions of their lease rider and five  
22 different versions of their asset, what do the  
23 building plans look like, and then they just append  
24 all of them, I mean, not all of them are relevant to  
25 every franchisee, but every franchisee gets a copy of



1 every one of those. That's, to me, where the real  
2 problem is.

3 In the current regime of saying convenience  
4 for the franchisors, just append anything they might  
5 ever sign compared to what is it this franchisee is  
6 likely to have to sign, there's an enormous imbalance.  
7 And I think some examination of how do you fix that  
8 fixes -- gets to some of the issue, taking care of  
9 this issue in a way. Because it's those agreements  
10 that have three different unit types and they have  
11 their area development agreement as part of their FDD,  
12 and they have their multi-unit agreement, as well as  
13 their single-unit agreement, and all -- you know, the  
14 lease arrangements that are different for each one of  
15 those sections. And, suddenly, you get this behemoth  
16 of a document. That's where the real challenge with  
17 the breadth of the document comes in terms of sheer  
18 page numbers, from where I sit.

19 MR. CANTONE: Well, I agree with Ron that --

20 MR. ZWISLER: One of -- go ahead, Dale.

21 MR. CANTONE: I was going to say, just  
22 quickly, I totally agree with Ron that for those  
23 1,200-page documents -- and there are quite a few of  
24 them -- the bulk of that text is not the 23 items of  
25 the FDD, the bulk of those are the ancillary

1 documents.

2           So one idea is to separate those 23 items,  
3 some of which are pretty lengthy. But, really, when  
4 you see these intimidating thick documents, most of it  
5 is the ancillary documents. Ron is absolutely right.

6           MR. ZWISLER: But, Dale, let me ask you this  
7 question. I prepare FDDs. And so we have clients who  
8 want to register in Maryland or have one universal FDD  
9 that they could use to disclose any prospect. When  
10 we're preparing those, we don't know who the  
11 prospect's going to be usually. We don't know which  
12 of those contracts they're going to sign.

13           MR. CANTONE: I'm not saying you don't give  
14 them to them, but maybe not, you know, separate from  
15 the rest of the disclosures.

16           MR. MAXSON: Kimberly, we've talked about  
17 these sometimes very long, sometimes complicated and  
18 hard-to-follow FDDs. In your real-world experience as  
19 a franchisee, do most prospective franchisees hire an  
20 attorney or an accountant to help them understand  
21 these documents?

22           MS. CROWELL: Well, in my experience, the  
23 first-time franchisee, prospective franchisee, more  
24 than likely is probably very apprehensive about hiring  
25 an attorney because they're worried about the cost.

1 And so what I have found is they will reach out to  
2 another franchisee or some business associate to try  
3 to get some initial help on just understanding the  
4 operational side of the business. And then, you know,  
5 if I'm speaking to them as a multi-unit operator now,  
6 I would say, you know, go and speak to an attorney  
7 about more of the legal issues that you might face,  
8 but really understand how the business operates first.  
9 If cost is an issue, get a handle on how to operate  
10 the business, and then go to the attorney for  
11 additional consultation.

12 MR. MAXSON: So, obviously, this workshop is  
13 in English and most FDDs are in English. Dale, I'm  
14 curious if, in your experience, franchisors are  
15 marketing their franchises in languages other than  
16 English?

17 MR. CANTONE: There are franchisors that  
18 market their -- well, they market their franchise to  
19 predominantly or, you know, a significant percentage  
20 of people who do not have English as their primary  
21 language. And I think part of that is reflecting a  
22 reality of franchising that we're kind of glossing  
23 over, which is franchising covers such a huge variety  
24 of businesses from the multi-unit operators, you know  
25 the big conglomerate franchise systems to, you know,

1 very low-cost franchise systems, where, by the way, no  
2 one ever has an attorney help them. So there are  
3 systems that market directly to people who may not  
4 have English as their first language, and I can give  
5 you several examples.

6 We have seen that happen in nail salon  
7 franchises. Bubble Tea, which is -- there are not  
8 that many of them, but often they are targeted towards  
9 the Asian community franchisee. As a matter of fact,  
10 on my desk today that I was looking at, a Bubble Tea  
11 agreement that was written in Chinese. And then  
12 probably, maybe the largest segment of this industry  
13 that targets to a lot of non-English-speaking people  
14 is the janitorial cleaning franchise system. And if  
15 you look at the list of franchisees in those systems,  
16 there are a lot of recent immigrants, people who do  
17 not have English as their first language.

18 And so I do not believe -- I don't know.  
19 I've never seen a disclosure document in anything  
20 other than English. So I do not know how those are  
21 being disclosed and how the disclosures are getting to  
22 the prospects. And I fear, based on some of my  
23 experience, that a lot of the people who buy into  
24 those systems simply do not read the disclosure  
25 document at all.

1           MR. MAXSON: So do you think if franchisors  
2 are required to produce their FDD in the language in  
3 which they marketed their franchises, that would incur  
4 much additional cost for those franchisors?

5           MR. CANTONE: I'm afraid it would. It would  
6 incur some additional cost. And, you know, just the  
7 cost to translate a document -- you know, many years  
8 ago my office and yours worked together on a consumer  
9 publication about the janitorial cleaning franchise  
10 industry, and it was costly to translate that into  
11 Spanish. And we had hoped, at that point, to  
12 translate it into other languages, but it never went  
13 forward for all sorts of reasons, one of which was the  
14 cost to translate it into different languages. So  
15 there's clearly a cost.

16           But I don't know what you do if you are  
17 primarily targeting or selling to people who don't  
18 speak English. The disclosure document doesn't work  
19 for a lot of those and so I don't know what you do.  
20 But it definitely is a cost. And part of our concern  
21 is that cost might be passed on to franchisees in the  
22 system anyway.

23           MR. ZWISLER: Dale, I can also foresee  
24 problems -- I don't know how many people in your  
25 office or your examiners speak multiple languages, and

1 I know we have very few, relatively speaking, within  
2 our office. If we had to preparer franchise  
3 agreements in Spanish, the most common additional  
4 language, who is going to review them?

5 MR. CANTONE: I'll read that one for you.

6 MR. ZWISLER: You'll do that one?

7 MR. CANTONE: Actually, I think the other  
8 way to work it is to have maybe some type of  
9 certification that a professional translation service  
10 translated the document from English. Because you're  
11 right, we wouldn't be able to do that. That's the  
12 only way I would see that would be workable, but, of  
13 course, that comes at a cost.

14 MR. ZWISLER: Yeah. I can share an  
15 experience. I do quite a bit of international  
16 franchising work. And I remember particularly in  
17 South Korea, which does have a franchise disclosure  
18 and registration requirement, but their FDD is not  
19 nearly as complicated as ours -- although they keep  
20 moving in that direction -- the translation cost there  
21 exceed all of our legal costs every time we prepare a  
22 filing. And that may be a very substantial additional  
23 expense that might deprive a lot of these non-native  
24 English speakers of a franchise opportunity.

25 MR. MAXSON: If there were a requirement

1 that they produce the FDD in the language in which  
2 they market these franchises, would that have any  
3 impact on state franchise registration requirements?

4 MR. CANTONE: I think that they certainly  
5 would because we have to review a document, and as  
6 Carl pointed out, most of us only speak one language.  
7 And so the only way I can see that happening is if we  
8 get a certification that a Spanish or some other  
9 language is being -- if the disclosure document is in  
10 a different language, we have the comfort to know that  
11 it is actually an accurate representation of what was  
12 registered in English in the States.

13 MR. MAXSON: Kimberly, are there  
14 technological features that might make the FDD more  
15 readable or more accessible to franchisees?

16 MS. CROWELL: Sure. I mean, I think it's  
17 important that we, you know, adopt newer technologies  
18 in terms of having the ability to look at it on your  
19 mobile device. I think having a search feature with  
20 either potentially, you know, having the ability to  
21 write specific questions that will lead you directly  
22 to different items within the FDD, I think would be  
23 helpful as well. For the FDDs that I've looked at, I  
24 haven't seen any -- even something as simple as a  
25 hyperlink from the table of contents, to be able to go

1 directly to that particular area. You know, as Ron  
2 mentioned, the 1,200-page FDD, certainly you don't  
3 want to have to scroll and try to figure out what page  
4 that is at.

5 So I think those would be some very simple  
6 adjustments to allow for better readability of the  
7 document from a technology standpoint.

8 MR. GARDNER: If I could link that back to  
9 something you asked about early, Will, and that's the  
10 review by attorneys or why people don't go to  
11 attorneys. I do think what Kimberly is suggesting is  
12 absolutely, I think, the next step in the evolution of  
13 how the FDD should be delivered. I mean, there's no  
14 question that it should come electronically. There's  
15 no question that it should have hyperlinks. All of  
16 that should exist because that's the way people digest  
17 their information these days.

18 I will say that I do think one of the  
19 reasons that people don't go to lawyers is because  
20 they get that document that is this big. They're  
21 terrified of the cost, which is ironic in a way  
22 because most franchisee lawyers do that on a very low-  
23 cost basis, relative to what these people are looking  
24 at potentially investing in their franchise. But that  
25 is what it is.



1           I do think that having it more  
2   technologically navigable will -- I think it would  
3   have two benefits. One is the obvious one, which is  
4   people can maybe find what they're looking for. And I  
5   think the other one is that it would cause them to ask  
6   more questions. You know, the other thing Kim talked  
7   about earlier was getting people to do more due  
8   diligence, to dig in. And being able to find stuff,  
9   whether it's because you have an attorney that's  
10   pointing you to it or because you stumble on it by  
11   yourself, is something I think that is probably in  
12   everybody's best interest.

13           This might be something we can all agree on.  
14   To get people to digest more information is a good  
15   thing.

16           MR. ZWISLER: I agree with Ron.

17           MR. GARDNER: I knew it would happen.

18           MS. JACKSON: I second that, Carl.

19           MR. MAXSON: So in your experience, are  
20   franchisors not doing these things, hyperlinks and  
21   things like that, because they think that they're not  
22   permitted to do it by the regulations or because  
23   they're intentionally trying to make it difficult to  
24   manage the document and to increase time or cost or  
25   whatever it is to review an FDD?

1           MR. GARDNER: I'll let Carl and Earsa who  
2 worked for the franchisors answer. I would say my  
3 guess is because you've heard them say it a couple of  
4 times already, things that increase costs. Increasing  
5 the technological application to your FDD does  
6 increase costs, at least on the front end in the short  
7 term.

8           I don't think anybody -- I shouldn't say  
9 "anybody." I don't think most franchisors are trying  
10 to discourage people from reading. I don't. But I do  
11 think the structure and the breadth does discourage  
12 it, and we ought to work on fixing that. I'll let  
13 Carl and Earsa speak from the real franchisor  
14 perspective on this one.

15           MR. ZWISLER: And I would consult with Dale,  
16 but my understanding of the Rule is that you're not  
17 allowed to have hyperlinks inside the FDD.

18           MR. CANTONE: I think the FTC Rule in 2007  
19 prohibited external hyperlinks. When I review these  
20 documents, I like to see certainly a hyperlink from  
21 the item numbers. I think there's nothing more  
22 helpful than that to have on the side of the document  
23 where each item number is to be able to go to it.  
24 That's a simple -- I don't think that type of  
25 hyperlink is prohibited by the Rule. But I don't see

1 that a lot.

2 MR. GARDNER: Like an internal hyperlink.

3 MR. CANTONE: Internal, yeah. It's the  
4 external hyperlink that isn't allowed.

5 MR. MAXSON: That leads me to a question  
6 that we got from the audience. Do locked PDFs inhibit  
7 the review of FDDs?

8 MR. CANTONE: Oh, I think that's a good  
9 question. Frequently, when I review a -- I mean,  
10 talking about searching terms, I mean, I've had FDDs  
11 where I'm trying to search on terms to find something,  
12 and you cannot do that. And I find that really a  
13 problem. I think it's certainly easier if you're  
14 searching particular terms to be able to find it in  
15 the FDD. That's interesting. In my experience, you  
16 know, about half of them are locked. But, you know, I  
17 don't know why.

18 MR. MAXSON: Carl, do you have any  
19 suggestions for how an FDD might be accessed more  
20 easily through less-traditional formats? There was  
21 mention earlier today about on iPhones or cellular  
22 phones or iPads or different documents like that. Are  
23 there any changes we can do as we're thinking about  
24 updating this Rule that was drafted a while ago, as  
25 the technology improves, that would make it easier for

1 people to navigate an FDD?

2 MR. ZWISLER: Well, I think mostly the  
3 things that we've already talked about, using  
4 hyperlinks, allowing or encouraging franchisors to  
5 post their FDDs online and make them accessible to  
6 franchisees early on, if they want to do that.

7 I don't know of any particular thing that  
8 makes reading an FDD on a phone any easier. I know I  
9 can't do it, but if that's what people choose to do.  
10 So I don't know the answer to that.

11 But I think I do have an answer to Dale's  
12 question about why we have locked PDFs, and I think  
13 that's really a protection that the franchisor wants.  
14 It doesn't want to have the document manipulated once  
15 it's been delivered. I mean, that would be the case  
16 when it's delivered to a prospective franchisee. They  
17 don't want to show up in somebody's office and have a  
18 version of a document that's not what they authorized.  
19 And that may be the reason that you're seeing them  
20 that way, too, Dale.

21 MR. CANTONE: Well, I certainly appreciate  
22 that. That's a legitimate concern. I just didn't  
23 realize that that prevented it from being searchable.

24 MR. ZWISLER: I think that's what we really  
25 need. It's not whether it's locked; it's whether it's

1 searchable. Yeah, I suffer from that, too.

2 MR. GARDNER: I think the idea of a  
3 hyperlink could really address not only navigation of  
4 the FDD itself, but it may help with the issue that I  
5 raised earlier about finding the relevant and  
6 appropriate ancillary documents in this 1,200-page  
7 morass that showed up.

8 I mean, one of the things that, you know,  
9 Earsa -- I think it was Earsa that said, we don't know  
10 which prospect is going to get our FDD -- if it was  
11 Carl that said, I apologize, but I think it was Earsa  
12 -- and to which I say, well, it seems to me you can do  
13 one of two things. You could break the process into  
14 two steps. Here is the FDD. If you're interested in  
15 going forward, here are the documents you're going to  
16 need to sign, this is a copy of your lease and your  
17 lease rider and all of the other things.

18 Alternatively, if you want to avoid that  
19 second step, then you give them a cover letter that  
20 says, okay, here's the whole document; it's all  
21 together; we're not breaking it up for cost reasons.  
22 But given your situation, if you're going to be a  
23 single-unit operator, you should go to these links.  
24 If you're thinking about a multi-unit, go to these  
25 links. If you're going to rent, you need these links.

1 If you're going to own, you need these links. And you  
2 could use that hyperlink technology as a way to direct  
3 people to the stuff that they actually need to read,  
4 rather than, again, wading through this 1,200-page,  
5 unsearchable monster.

6 MR. ZWISLER: Sure. I think we could think  
7 about how that might work and, particularly, if the  
8 FDD is delivered online or accessible online. You  
9 know, it's there if anybody wants to read it. But  
10 only as you get closer, whether it's the seven days  
11 before signing or at some earlier time, the parties  
12 could agree on which documents would have to be  
13 signed, and they would certainly be made available to  
14 the prospect.

15 MR. MAXSON: And so what you were talking  
16 about, Ron, I think you were talking about internal  
17 hyperlinks, right?

18 MR. GARDNER: Yeah. Well, probably. I  
19 mean, the question is if you still include all those  
20 documents in this single document then, yes, they're  
21 internal. But you could do it -- I'm not sure I'm  
22 there on Carl's idea that you just post it somewhere  
23 on the internet. But if you do, then they don't  
24 necessarily have to be internal. You can direct from  
25 the FDD itself to somewhere else on the franchise

1 owner's website where they have the relevant leases or  
2 documents for single-unit operators or for multi-unit  
3 operators. So that really sort of depends on how it  
4 gets structured.

5 But I'm not talking about linking to  
6 anything that's outside of what would normally be in  
7 these 1,200 pages. So I think, Will, yes, internal in  
8 terms of what they're getting now, not extraneous  
9 information beyond that.

10 MR. ZWISLER: Will, I know you want to  
11 conclude this, but I would just like to bring up one  
12 point to kind of refute something that Theresa Leets  
13 was suggesting earlier, which is that the franchisors  
14 are all-powerful, they drive the bargains, et cetera.  
15 Last time I looked at the statistics, most franchisors  
16 had 50 or fewer units. I saw a recent survey that  
17 said most franchises started over the last four years  
18 had one or zero units.

19 We're talking about -- most of the people  
20 who are going to be subject to these rules and any  
21 changes we're talking about are truly small businesses  
22 that are trying to comply with the Rule in good faith,  
23 and we better be very careful about any changes that  
24 we make that might unnecessarily add costs to doing  
25 business and their ability to create jobs for

1 prospective franchisees and their employees.

2 MR. CANTONE: But by the same token you  
3 can't refute that most franchise agreements are very  
4 one-sided in favor of the franchisor.

5 MR. MAXSON: With that, I am going to end it  
6 because we have reached our time at 4:30.

7 MR. CANTONE: Thank you.

8 MR. MAXSON: And we're not going to have  
9 cross-panel debating. That would get a little tricky.  
10 But thank you all very much for being here and for  
11 helping educate everyone about these franchise issues.  
12 We really appreciate it and appreciate your time.  
13 This has been very useful. I hope everyone sitting at  
14 home or in their offices will be quietly clapping for  
15 you right now. I know you won't hear it, but  
16 cosmically, maybe you'll feel the good vibes.

17 So with that, we're going to turn it over to  
18 Lois Greisman, who's the Associate Director of the  
19 FTC's Division of Marketing Practices, and in just a  
20 moment, she will be delivering the closing wrap-up for  
21 this workshop. Thanks very much.

22

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1 CLOSING REMARKS

2 MS. GREISMAN: Good afternoon, everybody.  
3 My name is Lois Greisman. As Will said, I head the  
4 Division of Marketing Practices at the FTC. That  
5 division has the primary responsibility for enforcing  
6 and promulgating the Franchise Rule.

7 And it's my honor to close out today's  
8 workshop, and I'm going to begin to do that by  
9 extending thanks, of course, to the speakers and my  
10 FTC colleagues who made this possible. Many of them  
11 you have seen but not all. So I want to give a shout-  
12 out to Crystal Peters, Larissa Henderson, James  
13 Murray, Bruce Jennings from the FTC's event planning  
14 and media team; paralegals Leah Hebron and Kate Moody;  
15 Collin Hansen from our Bureau of Economics; Kenny  
16 Wright from our General Counsel's Office; June Chang  
17 and Lesley Fair from our Division of Consumer and  
18 Business Education; and both Nicole Drayton and  
19 Juliana Gruenwald in our Office of Public Affairs.

20 So this is not really a close-out since, of  
21 course, the record stays open. I just want to make a  
22 couple of comments on the engaging panels that we've  
23 had today and what I will refer to as very diplomatic  
24 disagreement on some of the issues. And as  
25 Representative Hern opened with, no FDD is perfect.

1           So whether or not to mandate financial  
2 performance representations has been an issue since  
3 the get-go. Interesting change since 2007, when about  
4 20 percent were providing FPRs to some 66 percent  
5 these days. Discussion that the FPR is the most  
6 important item and, also, a slightly different view  
7 expressing concern about whether or not the FPR really  
8 is a breaking point; and some agreement that shifts in  
9 cost-benefit analysis have changed given changes in  
10 technology.

11           But then we moved over to discuss  
12 disclaimers, waivers, integration clause, questions  
13 about is there a bright line, is there a way to  
14 distinguish between explanations and disclaimers; and  
15 what is that line; who do integration clauses favor;  
16 who do the questionnaires benefit; is the main purpose  
17 of these kinds of provisions for the franchisors to  
18 defend against a lawsuit; and at what point do they  
19 become problematic?

20           Then finally, the last panel, Pros and Cons  
21 of the FDD Format. A good discussion of a summary  
22 document that arises out of concerns about whether the  
23 FDD is a playbook or is it a 1,200-page monster that  
24 perhaps may or may not be tamable by using hyperlinks.

25           So to sum up, there's absolutely no shortage

1 of challenging, interesting issues and ongoing  
2 provocative discussion.

3 Please keep in mind that the record is open  
4 until December 17.

5 So again, thank you all for joining us this  
6 afternoon. We look forward to hearing more from you  
7 and please stay safe and healthy. Thank you very  
8 much. And take good care. We are adjourned.

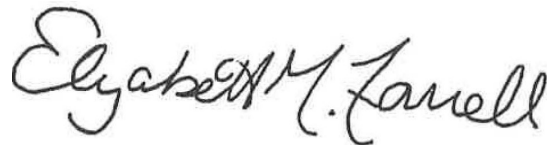
9 (Hearing concluded at 4:40 p.m.)

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