

KnowledgeVision | Open-Welcome-Financial Performance Representations- What Should be Disclosed- And Why-

CHRISTINE

TODARO:

Good morning, and welcome to Reviewing the Franchise Rule, an FTC virtual workshop. My name is Christine Todaro, and I'm the FTC's Franchise Rule Program Coordinator. On behalf of the entire FTC Workshop Team, we are delighted that you are joining us here today via our live webcast.

Before we begin, I have a few administrative details to cover. First, a video recording and transcript of these proceedings will be available on our workshop event page soon. Second, as with any virtual event, we may experience technical issues. If these occur, we ask for your patience as we work through them.

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

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

ANDREW

SMITH:

Thank you, Christine. Welcome to Reviewing the Franchise Rule, an FTC virtual workshop. My name is Andrew Smith. I'm the director of the FTC's Bureau of Consumer Protection.

Today's workshop features three panels presenting franchisor, franchisee, and regulator perspective on key franchise rule issues, as well as opening remarks from congressmen and McDonald's franchisee, Kevin Hern. I'd like to thank Congressman Hern and each of the panelists for helping to make this virtual workshop possible.

Let me start today's discussion by giving some background on why we're here. The franchising business model is an important one. It enables individuals to develop small businesses without having to start from scratch and franchisors to expand their reach and serve new customers.

In fact, the International Franchise Association estimates that there are more than 733,000 franchise establishments that employ more than 7.5 million individuals. Nevertheless, joining a franchise system isn't without risk. The primary purpose of our franchise rule, which was adopted by the commission in 1978 and last amended

in 2007, is to provide prospective franchise purchasers the material information they need in order to weigh the risks and benefits of such an investment.

Accordingly, the rule requires franchise owners to provide prospective purchasers with 23 items of key information about the franchise in the form of a Franchise Disclosure Document, also known as an FDD. The FTC's franchise rule is thus a pre-sale disclosure rule, which was designed to address deception in the offer and sale of franchises. The rule does not regulate the substantive terms of the franchisor-franchisee relationship, nor does it require the franchisor to register or file any documents with the commission.

The FTC routinely reviews its rules to seek information about their costs and benefits, as well as their regulatory and economic impact. We are here today because of the FTC's ongoing review of the franchise rule. Last year we requested public comment on the franchise rule and received 39 comments in response. I'd like to thank those who took time to comment. Your input is critical to the review process.

While all commenters suggested that there is a continuing need for the rule, some commenters proposed modifications they believed would make the rule more effective. And now, after considering those comments, we are hosting this workshop and seeking additional public comment until December 17 on the issues discussed today. The goal of today's workshop is to dive more deeply into three topics that were raised by several commenters.

The first panel, Financial Performance Representations, What Should Be Disclosed and Why, will focus on whether the current Item 19 disclosures are effective, or whether additional or modified disclosures are necessary to prevent deception in the marketplace. The second panel, A Discussion of Disclaimers, Waivers, and Questionnaires, will address their use by franchisors and whether such use undermines any of the rules protections. The final panel, The Pros and Cons of the Current FDD Format, will explore whether the format of the FDD can be improved to take into account technological advances or otherwise make the FDD more readable.

I anticipate a lively and informative discussion. Each panel includes relevant

stakeholders' perspectives, and I look forward to hearing what each of them has to say.

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

In addition, Congressman Hern serves on the House Small Business Committee where he is the ranking member on the economic growth, tax, and capital access subcommittee. This subcommittee deals directly with franchisees and franchisors as they seek to obtain capital. Please join me in welcoming Congressman Hern.

KEVIN HERN: Thank you, Andrew. And thank you, Andrea. And as it was mentioned, I'm the US Congress from Oklahoma's 1st congressional district here in the Tulsa area. And for over 30 years, I've been involved in the McDonald's franchisee program.

After spending a year as an aerospace engineer, a job that was cut short by the space shuttle Challenger disaster, I had the opportunity to get into the program by working for a long-time franchisee who owns 6 restaurants in the Little Rock, Arkansas area. At the time, he was the chairman of the owner-operator leadership group that was for all the 4,000 US franchisees at that time.

His role, early on for me in my career in McDonald's at that time, his role allowed me to see how the relationship-- having a good relationship between the franchisors and the franchisees is extraordinarily important to the overall success of any franchise brand. For 10 years I worked in the various management roles, coming through all the different-- from entry level management all the way to the director of operations for a multi-unit organization.

And worked 10 years to save \$100,000 to get my first McDonald's restaurant and I became a McDonald's franchisee in 1997. And since that time, in almost 24 years, I've owned 24 McDonald's restaurants.

So now, then, I have 5 left, and my family runs those here in the Tulsa area. And prior to running for Congress in 2017, I served for 13 years on the McDonald's National Leadership Council. The first eight years of that, I was the chairman of the

Franchise Relationship Team and five as the Chief Financial Officer for the McDonald's Franchisee Organization.

As the chairman of the Franchise Relations Team, I saw firsthand how a firm but fair franchise agreement not only protected the intellectual property of the franchisor, but also the equity of the franchisees. My corporate counterparts were the chief financial officer and the senior vice president of franchising for McDonald's in the USA. For a period of almost 13 years, I was involved in almost every franchise agreement issue that developed across the United States among the almost 4,000 franchisees.

In fact, I've often said that franchising relationships are much like the interactions of the states with the federal government. The people are best represented by our public when each entity, the state and federal and the franchisor or franchisee, stays in their appropriate lanes of responsibilities of oversight and acts within its limitations of good governance.

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

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

I've spoken a lot over the past three years about the similarities of the franchising model as compared to the US government. The relationship between states and the federal government is bound together by the framework of the US Constitution. We have elected politicians that debate the very merits of these ideas contained in our great doctrine. I see that firsthand today.

Also, the relationship between the franchisees and the franchisor is bound together by initially the FDD and ultimately the franchise agreement. Most of the brands

have elected representatives that debate the merits of the ideas contained in their franchise agreement. So as you go about your work in reviewing possible updates to the FDD, I would ask that you keep the thought in mind that there must be a balance in the responsibility as to each party in the relationship.

Each franchisor needs to represent or sell its brand to the prospective buyer without over promising or misleading the potential franchisee. The franchisee needs to take necessary steps to do the proper due diligence in making what will be most likely the greatest career change they will ever experience. There is a natural tendency for those with very little franchising experience to pick sides, and I will tell you from years of experience, only the brands that work together will see long term sustainable success.

As with life, there will never be a relationship that doesn't experience disagreements. There are remedies for the franchisees and the franchisors when those disputes develop. As both sides seek protections of their assets, the franchisor in trying to select the top notch franchisees to grow their brands and increase overall system value for stakeholders and the franchisee, who is looking for incredible rewards in return for their investment of cash, hard work, and risk taking.

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

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

Finally, I would say franchising has been a life changer for so many, including myself. It allowed a person like me, who grew up very poor, to work hard, take risks, and become extraordinarily successful. I want to thank you for allowing me to share

my thoughts on the importance of franchising and the franchising model. It's given thousands of aspiring business people the opportunity to realize the American dream. Thank you. And Andrew, thanks again for allowing me to be on here today.

**CHRISTINE
TODARO:**

Thank you very much, Congressman Hern, and thank you to everyone joining us for our first panel of the day, Financial Performance Representations, What Should Be Disclosed and Why. My name is Christine Todaro, and I'm an attorney in the FTC's division of marketing practices and also the FTC's franchise rule program Coordinator.

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

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

First, Dale Cantone is an assistant attorney general for the state of Maryland and the deputy securities commissioner, as well as the chief of the franchise and business opportunity unit for the Maryland securities division. Mr. Cantone also serves as the chair of the Franchise and Business Opportunity Committee and Project Group of the North American Securities Administrators Association.

Susan Grueneberg is a partner at the law firm of Cozen O'Connor and is a certified specialist in franchise and distribution law by the state bar of California. Justin Klein is a partner at the law firm of Marks and Klein where he represents both franchisees and franchisors. Keith Miller is the founder of the franchise advocacy consulting, and he also serves as the director of Public Affairs and Engagements for the American Association of Franchisee Dealers. And he is also the director of Legislative Affairs for the fair franchising initiative. In addition, he's a Subway franchisee.

Sandy Wall is of council at DLA Piper. She previously served as in-house counsel for McDonald's and Sears Roebuck. Thank you, panelists, for joining us.

On behalf of myself and the panelists, I'd like to note that the views we express

today are our own and do not necessarily reflect the views of the Commission or any one particular organization, law firm, or company.

I'd like to start today's discussion by talking about the issue of mandatory Financial Performance Representations, also known as FPRs. Many of you may recall that the FTC previously considered whether to mandate FPRs, and ultimately decided not to when it amended the rule in 2007. In reaching this decision, the commission considered several different arguments in favor of and against mandatory FPRs. I'd like to frame today's discussion on mandatory FPRs by going through some of those arguments and asking the panelists what, if anything, has changed since the commission chose not to mandate FPRs several years ago.

First, we often hear that FPR data is the single most important piece of information to prospective franchisees. During the last franchise rule review, an estimated 20% of franchisors provided FPRs in their FDDs. That's a Franchise Disclosure Document. The commission noted that prospects could thus find a franchise that made FPRs if they wanted to.

The FTC also noted that ordinary market forces might compel more franchisors to disclose without government regulation. Now, IFA estimates that 66% of franchisors make FPRs in their FDDs. My first question to the panel is, does the fact that 66% of franchisors, if we assume those numbers are correct, now disclose FPRs affirm the commission's thinking and weigh against the commission mandating FPRs? Dale, I'll ask you to respond first.

DALE

Thanks, Christine, and thanks for the opportunity to participate in this workshop.

CANTONE:

There's no question that 60%-- by the way, 60% is closer along the statistics that my state of Maryland and other registration states are experiencing. 60% is certainly better than the 20% or the 10% that we'd seen prior to 2000, so that's definitely a positive trend.

But that still leaves around 40% or somewhere close to 40% of prospective franchisees that are left without the disclosure item that is certainly what most prospective franchisees desire most and is arguably one of the most important parts of the disclosure document. So we're currently left in a regulatory scheme that allows a franchisor who, with a failing system, franchisees are losing a lot of

money, to simply choose not to disclose financial performance representations.

And the FTC did go through an analysis in 2007, and there are reasons why they chose not to mandate FPRs at that time. Some of those reasons exist in this day. There is an additional cost to a franchise system for a compiling of financial performance data. However, 60% of franchisors have managed to figure out a way to absorb those costs.

And that also doesn't really take into account cost to prospective franchisees who have to put together a business plan of their own. And there's got to be increased costs for coming up with a business plan without that most important data.

There's also-- one of the reasons the FTC decided not to mandate this disclosure is the perceived availability of getting financial performance data elsewhere. And while there are different avenues for obtaining financial performance information, nothing could compare to having an item 19.

One of the methods is to contact existing and former franchisees. Well, that's easier said than done in many cases. It sometimes works in some systems, but there are other systems where it's very difficult for prospective franchisees to get financial information from existing franchisees who may simply choose not to disclose that information.

So the costs are there. But if you do a cost benefit analysis, the benefits of requiring this disclosure, which, again, everybody agrees is the single most important piece of information that prospective franchisees want the most, far outweighs the benefits far outweigh the costs that there might be to franchise systems. And some of those costs are, quite frankly, a little overstated.

A lot of franchisors collect data directly from their franchisees, and probably even more so now than they did in 2007. And they could be doing that directly through POS systems. So for the vast majority of franchise systems, they already have the data. And, in fact, some of them who choose not to make an FPR to prospective franchisees end up making FPR-type disclosure to banks to facilitate loans.

So it's a really important disclosure. And on a cost-benefit analysis, in my own personal opinion, it's the disclosure that really should be made to prospective

franchisees. And not requiring it is bad for prospective franchisees, and it's bad for franchising in general.

**CHRISTINE
TODARO:**

Thank you, Dale. And we're going to go through some of the other considerations, like the costs, liability, and other issues that you raised. But right now I want to stick to this 66% disclosing FPRs.

And I want to follow up with Susan. In your opinion, does the fact that 66% currently disclose weigh against the commission mandating FPRs?

**SUSAN
GRUENEBERG:**

Well, thanks, Christine. And, again, thank you for inviting me to be a panelist today. I agree with what both you and Dale said about this information, Financial Performance Representation, probably being the most important information that a prospective franchisee wants and a franchisor wants them to have.

I disagree with the conclusion that if a franchisor is not disclosing a financial performance representation, it's probably hiding something. And it's probably hiding the fact that the system isn't making money.

I think the anecdotal reasons you see for franchisors deciding not to make FPRs, in my experience, is, number 1, their brand may be so strong they don't need to. Number 2, there may be sufficient information out there in the marketplace through existing franchisees and other sources. Or, in many, many cases, it may be an emerging franchise system and they feel they don't have enough data or reliable enough data to make an FPR going into franchising or in the early stages.

If you think about it, it makes no sense to maintain a system of franchises that are not making money and make the argument that the initial fee is what you're after. Because a franchisor is not making its revenues based on the initial fee. That initial fee goes to providing the pre-opening obligations that the franchisor has. It may go to a broker in large part.

And it's the ongoing revenue. It's the ongoing stream of royalties or other payments and that makes a healthy franchise system. And for that you need healthy franchisees as well.

Now, again, I realize I view all of this through the prism of a lawyer who primarily represents franchisors, but we all have our own prisms and that's why we're here

today. For me, I would not look at it as an argument of market forces, but rather, is this information important to mandate? Of course, your initial reaction is, yes.

But then you have to ask yourself, can you do that without resulting in some FPRs that are misleading or that don't have a reasonable basis? And after you start thinking about it, the exception sometimes tend to be overwhelming. And are we even thinking of everything we should be thinking of?

Of course, we're talking about ramp up and all of that. But I'm more of a mind that if you're going to encourage FPRs, market forces comes in very-- on a very important basis when you look at what's being disclosed. Because that's going to vary. What's reasonable in different industries is going to be different.

And so it's very difficult to go into that and think, oh, we can just mandate gross revenues. Or, we can tell everybody to do a break even in Item 19. That's just not going to work in my opinion.

CHRISTINE

TODARO:

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

SANDY WALL:

Well, again, thank you for having me again here today, Christine. And I-- it's a little of both. I think, again, we're all in agreement that providing an FPR in an FDD is good for the franchisor and good for the franchisee. But there are clear reasons, as Susan pointed out, why a franchisor may be unable to do this.

Another example is you've got an international company that has been doing business outside the United States and coming into the US, has no US operating history. If you mandated an FPR, you'd basically be saying that they can't franchise in the US without having US operations here. Clearly mandating this would be a barrier to entry of certain franchise systems.

And as Susan pointed out, the exceptions would-- there would have to be vast list of exceptions. In addition, since exceptions won't cover every circumstance, the FTC would have to be prepared to issue opinions on certain circumstances so that certain companies could be exempted out of the FPR requirement. Again,

something that's going to take valuable time and resources while, again, most franchisors choose to do this in their-- for many, many reasons.

And, again, one thing I-- and I understand, Dale, your position on that it's because people-- our franchisors may be hiding information. And there are bad actors everywhere in the world from time to time, and there may be a small percentage of franchisors that don't provide information for that reason.

The franchisees have choice. A franchisee who does not get an FPR, does not get the information from a prospective franchise-- from a franchisor, can always elect not to buy the franchise. This is important information, and if they can't-- they don't feel comfortable that they can get this information through other sources, or they're not comfortable with the reason why the franchisor says they cannot provide this information, they don't need to proceed.

CHRISTINE

OK. Well, that's actually a great segue into the next topic that I'd like to talk about.

TODARO:

Another factor that was considered was whether mandatory FPRs would reduce the level of false earnings claims made to prospective franchisees.

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

KEITH MILLER:

Well, again, thanks, Christine and thanks for all the staff at the FTC for putting this together. When looking at false or unsubstantiated claims outside of the FDD, I think we first have to understand that no prospective franchisee is going to buy a franchise without some understanding of revenue and cost information. Knowing that about 34% or 40% of franchises put nothing in the Item 19 makes me assume that those franchisees of these brands are getting information outside of the FDD.

Of course, that doesn't make that information false, but it also doesn't mean that a franchise giving Item 19 data isn't giving information beyond what's in the FDD. And the information isn't always direct information.

For example, one brand I worked with in this last year that captured a lot of news stories seemed to float \$1.5 million as a revenue number. Every franchisee I talked to gave that number. Some of them got it direct, but for most it was actually more

subtle as they were talking about how they would build out the store and what would be in the restaurant.

They were told, well, you have to put it in a Coke Freestyle machine, because that was what was required for a \$1.5 million operation. Same with other build out and equipment requirements that they were told, well, we have to do this to build for a \$1.5 million operation. Yet not a single unit ever reached that number.

I try to tell people that the only financial information you should trust and believe is what is in the FDD. Everything outside of it can be suspect, especially if it's verbal or implied. And I would also argue that franchisors who avoid giving even basic revenue and cost data-- look.

When we talk about the fear of giving these numbers, I think people get more into the weeds and want to talk about EBITDA, EBITDA-type numbers, which would be great. But I think that's a big step. And I think even some even basic revenue data and cost data probably needs to be required.

And the reason someone buys a franchise is because that brand has supposedly been tested and proven as a business model. Now that doesn't mean or guarantee any success. But for franchisors who can't show the data that the model is proven, I would ask why they're franchising.

The intent of the franchise rule is to protect the consumer, the prospective franchisee. Yet often discussions on the rule seemed to get steered towards protecting the franchisor from liability. The franchisor is the one with all the resources and leverage.

And I would end this part of how prevalent it is. Look, most franchise owners are good. I agree with that. But we do rules and oversight not to damage the good franchisors. We do it to protect from the bad franchisors.

But with all these concerns, can someone tell me the last time the FTC took action against a franchisor for a financial representation made in the disclosure document? I think most of the people would answer it's been a long time.

**CHRISTINE
TODARO:**

Thanks, Keith. I want to follow up on something that you said earlier. I mean, in terms of the number of representations that you're seeing being made outside of

the FDD, or inconsistent information that's being provided to prospective franchisees outside of the FDD, have you seen a decrease in the number of times that's happening, or the number of complaints or stories you hear from your members and other franchisees now that more franchisors are disclosing?

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

Look, I have to understand that the people who call me are calling me because they have problems and issues. Not everyone who's happy isn't calling me. So I guess as I become more well known, I've probably seen an increase in it.

But I wouldn't say that's because there is an increase in false representations. And I know we'll talk about later the sources, but that's what's gets to be interesting is the sources that the representation is coming from. The false representations tend to be more at an arm's length and not from inside the franchise company, whether it's brokers or consultants or loan brokers, for that matter. And I think we'll touch on that a little later.

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

CHRISTINE TODARO: OK. I'd like to turn to Justin. Have you seen much litigation over false FPR data or FPRs that are given to prospects outside of the FDD?

JUSTIN KLEIN: Yes. I think we're all using interesting adjectives, namely the word false. I think there's a very big distinction between false and impermissible.

I think one of the bigger concerns that I have is about-- the larger concern is false data. Impermissible data or impermissible disclosures outside of the realm of the document is something that I think is going to be really hard to ever regulate around. I mean, sales people are going to be sales people. They're going to say what they're going to say.

Presumably franchisors are doing the right thing by training their staff the right way,

by training their sales people. Presumably they're talking to their brokers and the folks who they are engaging to bring into their universe what is permissible and what is not permissible. Obviously, nobody on this panel, I would presume-- and by the way, thank you for having me on the panel and honored to be amongst all these esteemed colleagues-- but nobody wants false data.

And I think when you look at-- and I will answer your question directly-- but when you look at the concept of mandatory FPRs, my bigger concern, as somebody who represents more franchisees like Keith, is garbage in, garbage out. And if there is no way to properly check and balance the information that's being provided, and we've heard reasonable basis and we know everybody is familiar with the concept around the FPR.

Our folks, who range from John Q and Mary Q franchisee up to sophisticated private equity groups who are all reading the same FDD, are all looking at and analyzing the same information. So my bigger concern is, what is the relevance of the data that's being provided and the form with which it's being provided in to ensure that the prospective investor, the consumer, if that's what we want to call them, is giving the information that is going to be most relevant to the decision to make the investment.

From a law firm perspective, we have not seen an uptick in what I would call impermissible FPR claims. The claims of, I was promised I was going to make \$1 million and I didn't make a \$1 million over the last decade or so have significantly declined from our perspective. I don't know that that's directly FPR related.

Quite frankly, I think that's more probably related to some of the other barriers to litigation that exist out there, be it the franchise agreement, be it the cost, be it the time, be it the nature of the type of claim that's being brought and where either the franchisor or the franchisee stands at the time that claim is being brought in connection with those factors. So I don't know that-- just to round it all back to the topic in the theme, I don't know that there's been an uptick. But I also don't know that mandatory FPR positively or negatively impacts the amount of those types of lawsuits that ultimately come out of that information.

What I can say is I fear that if 40% of franchise owners are not providing the

information for one or more of the reasons that any of the folks on this panel have already addressed, my bigger concern is that the lack of accuracy and the lack of professionalism that is required in the disclosure process isn't going to be met. And that's a negative impact to prospective investors in terms of my concept of garbage in, garbage out.

CHRISTINE Keith, do you have anything in response to that?

TODARO:

KEITH MILLER: No. And I think we have to remember who's looking at these FDDs. And I think Justin brings up a really good point in that you have the range of big private equity franchisees to a person who has very little knowledge.

The industry always sells itself as, be your own boss, proven business model, no experience necessary. Yet then it bashes those people with no experience necessary when they make a mistake.

And I think we have to really look at-- and I know one of the other panels is actually more talking about the structure. I think you also have to look at, when he talked about uptick or lack of uptick in lawsuits on it, I think it's almost impossible for a franchisee to have the resources to do that fight.

I mean, that's what I think franchisees depend on the FTC to do. And especially when there's no private right of action on the franchise rule. The average franchisee, when they fail-- and it may have been falsely disclosed, has been wiped out.

All their assets are at risk, so what resources do they have to fight what's happened to them, whether it's false or unsubstantiated claims. It's very difficult for them to fight it. They just don't have the resources.

CHRISTINE Sandy, do you want to follow up on that?

TODARO:

SANDY WALL: Well, Christine, from the FTC's perspective, have you seen in the last 10 years a lot of complaints from franchisees, alleging that unlawful FPR information has been provided? Or information outside of an FDD?

CHRISTINE I mean, I have to say that this is something that I haven't looked at recently. The last time that I looked at complaint data, I can tell you we get far fewer franchise complaints than we do for other types of business opportunities at least from the data set that I had looked at. And then--

SANDY WALL: And just-- OK. Go ahead.

CHRISTINE Oh, no. Go ahead.

TODARO:

SANDY WALL: I'm sorry. And just to the point about litigation, franchisee litigation continues. And it may be on other issues. But my experience is from a franchisor's perspective, you're not seeing a huge amount of litigation specifically related to FPRs.

I don't agree with the fact that franchisees are not suing franchisors. It's just not based on these types of claims, for the most part.

CHRISTINE Dale, is there something you want to add?

TODARO:

DALE Yeah. I think when you talk about both complaints and litigation, I just don't think
CANTONE: litigation is a good indicator of what's going on in the franchise world. Because there are some systems-- I mean, it depends.

We've got-- franchising covers a huge realm of, like, McDonald's and the Hiltons. And it also covers the smaller investments that the people that we hear most from that maybe Sandy and Susan don't represent. And a lot of those franchisees simply do not have either the resources to pursue litigation.

There are barriers to filing suit that franchisors have been brilliant at putting in the disclosure document. And I know you're having a panel on disclaimers and these certifications, which I think is a good topic to go by. But even a mandatory arbitration provision in a franchise agreement-- and they're ubiquitous-- really does put a barrier in place of to bringing a lawsuit.

But I will tell you that we also don't get that many complaints generally from franchisees. I'm not quite sure. It's funny when I read some of the message boards or when I hear from Keith. There are lots of complaints out there, but for all sorts of

reasons they're not necessarily getting to my office and probably not getting to your office.

I don't think that's an indicator that there aren't problems out there. We're just not necessarily hearing about them.

CHRISTINE Justin, was there a follow-up?

TODARO:

JUSTIN KLEIN: Yeah. I just think as a follow-up, I just think that's a fair statement. I will tell you as somebody who reviews these documents on behalf of folks who are looking to make the investment, one of the initial things that we look at is, first of all, is there an FPR? That's number 1.

And then, I mean, look, lawyers are notoriously bad at math, so I can't really provide much insight into what the FPR does or says or what it means. But the FDD, from our perspective, is step 1 of the process, right? That's the beginning of the due diligence. It's a tool to prospective franchisees to use in connection with the rest of the due diligence that they're going to do.

If the FDD has been approved by Dale's great state of Maryland, if it's been approved by other states that have registration requirements, then we look at it through, to use Susan's word or Sandy's word, a different prism, if some state regulator has reviewed it. So I think, again, it's a positive step if franchisors are going to make those FPRs.

But I don't know that FPRs are the point of the breakdown of the relationship, or why even a franchisee ultimately makes the decision to move forward with a particular brand.

CHRISTINE OK. Thank you. I think Keith wants to add something, and then I'd like to move on to

TODARO: the next topic to make sure we have enough time--

KEITH MILLER: Yeah. One--

CHRISTINE --to cover everything.

TODARO:

KEITH MILLER: --quick comment. One of the reasons the FTC doesn't see a lot of complaints is if a franchisee-- and I've heard this from multiple lawyers that represent franchisees. If they're considering litigation, they don't want their client to file an FTC complaint.

Because the reality is the FTC is probably not going to act on that complaint, and then that gets used against them in their lawsuit that they're told, well. You filed a complaint with the FTC. They didn't act, so, therefore, nothing must have happened.

Wrong. So literally I've heard from multiple franchisee lawyers, telling their clients not to file an FTC complaint. So that reduces complaints.

And, of course, people really don't know how to file them. And if they're still in that system, they are afraid of retaliation from their franchisor if they're still in the system.

**CHRISTINE
TODARO:** OK. We'll just-- I would just like to add that we always encourage anyone to file a complaint with the FTC. You can do that on our website.

We have information to walk you through specifically how to file a complaint. There's also a phone number on our website that you can call in order to speak with someone live to file that complaint. So I just want to add that the FTC's position is people should be filing complaints with us if they feel like they've been wronged for unfair or deceptive practices.

KEITH MILLER: And I would agree with that.

**CHRISTINE
TODARO:** That being said, I'd like to move to another consideration, which some of you have talked about, which is the potential cost to franchisors or franchisees if FPRs were to be made mandatory. In 2007, the commission noted that mandating FPRs would impose substantial new accounting, data collection, and review costs in all franchise systems.

As Dale mentioned earlier, most franchisors now collect financial information through a POS system. That might have not been the case when the commission amended the rule. Sandy, to that end, what's your position on whether mandating FPRs would impose substantial costs on franchise systems today, and what would those costs be?

SANDY WALL: Well, you know, I think you're right, Christine and Dale. You're correct. There is, due to the emergence of technology over the last 10, 15 years, more of that information is provided to many franchisors. But it is not all franchisors. There are some franchise systems that are not based on a percentage of sales, in terms of royalty, and they don't collect that information from their franchisees.

In addition, franchise agreements have a term to them. And depending on when the franchise agreement was entered into, there may or may not be sufficient language in a franchise agreement to allow the franchisor to collect this data from the franchisee. So for systems that don't get this data through a POS system, it would not be-- it would be expensive.

You would have to go to the franchisees and ask them to provide this information. You couldn't mandate it. You would have-- the franchisor would be required to devote the resources to collect the data and then evaluate and analyze the data to make sure it is accurate.

And, again, I think when you look today, if you have that type of system, those are the types of systems that aren't providing FPRs because they have-- they don't feel comfortable that-- and this is something we'll talk about later-- that they have the reasonable basis to stand behind the information in the FPR.

And I think this is, again, it's not all franchisors, but there are a number of franchisors that fall into that category. And, again, we're going to talk about this later, but if-- I'll leave it at that point. I'll leave it at this point right now. You can move on from this.

**CHRISTINE
TODARO:** Susan, do you see other costs that franchisors would incur beyond those that Sandy mentioned? Susan, we can't hear you right now.

**SUSAN
GRUENEBERG:** Sorry. I've been having trouble with my audio today. I was going to say in terms of pure out-of-pocket costs, of course you're going to have more costs to prepare an FPR. You're going to have additional legal fees, accounting fees. But I agree with Dale on the cost benefit analysis.

I don't think this is the factor that should really weigh in favor of not mandating FPRs. I think more-- it's more of what Sandy is talking about, the practical difficulties

in systems that weren't born yesterday and don't have these POS systems in place, or don't have the contractual provisions to mandate use of them.

If you look back at the original statement of basis and purpose when the rule was first enacted, the purpose was to level the playing fields of information. Prospective franchisees were found not to have the same level of information the franchisors had. And so this seems to me, this particular factor cost, is something where it shouldn't mandate in favor of not mandating FPR.

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

CHRISTINE

Dale, did you have a follow up on what Susan just said?

TODARO:

DALE

CANTONE:

Well, this discussion about the difficulties in developing a mandate for FPR is that, in fact, there are some systems that everybody would recognize probably couldn't and shouldn't make an FPR. But that doesn't mean you don't try. Because what we're left with now is a system where a franchise owner can choose purely for whatever reason it wants not to provide the data.

And there are some franchise owners that probably should not and could not provide an FPR, new and emerging systems, what have you. But it doesn't mean you don't come up with an idea where you can move the ball forwards, because it is such an important disclosure. I mean, the one thing that the rule has consistently agreed upon is that this is the number 1 thing that franchisees want, and they really deserve it.

So leaving it entirely up to franchisors, some of whom are absolutely doing the right thing, but not all of them may. And if you do mandate-- if you do provide a mandate

that is a common sense mandate that takes into account the practicalities and the realities of the situation, I think it would benefit everybody. And it's just something that we could trial.

CHRISTINE Sandy, do you have a follow-up to Dale's comment?

TODARO:

SANDY WALL: And look, Dale. Again, franchisees, prospective franchisees, have the choice. If they ask for the information and they do not get a legitimate reason as to why that information can't be provided, they don't proceed with the franchise purchase. It's like everything-- every decision that a consumer makes day to day. And I think trying to craft the rules, as we've discussed and come up with the exceptions about who wouldn't have to produce it, is going to make a lot more-- create more impediments to franchising than it's going to help prospective franchisees.

CHRISTINE OK, and Justin, is there something you want to add? And as a follow up to whatever **TODARO:** you're going to say, I was wondering if you could address whether you think that there will be increased cost to franchisees if FPRs were mandated.

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

I guess my bigger concern, as somebody who reviews these on behalf of somebody else, as an advisor, is I'm more concerned about bad info than mandated info. And, again, if it's mandated, I'd be more concerned about the cost associated with what folks have-- and listen, we've seen some really bad FDDs. We've seen FDDs with other brand's names in them.

We've seen FDDs written on spiral notebooks. We've seen FDDs that don't comply with any regulations that are out there whatsoever and they're just is a cover sheet that says FDD on it. And that doesn't stop our clients from necessarily wanting to invest in the franchise and/or quite frankly even being successful with that brand. It just means that they're not necessarily getting the best guidance from their professionals.

So my bigger concern is, who's preparing the information? And the reliability is critical. And if it's mandated, unless there is some regulatory component to figuring out how reliable that information is for a prospective franchisee, that's my bigger-- that's my bigger concern.

From a cost perspective for franchisees, I mean, most franchisees, no matter how sophisticated they are that come to us, whether they own 1 unit or they're involved in many, many businesses, they ask basically two questions of the franchisor. How much does it cost, and how much can I make? That's all they care about.

I don't know that the FPR, again, is the be all, end all of the mindset of a prospective investor in terms of how much they can make. I think, again, the FDD, at least the way we counsel our clients, is that is only a piece of the puzzle to gather that information and determine its reliability to use it in terms of talking to other franchisees, to talking to competitors, to talking to figure out whether or not it's relevant to your particular market. So I think reliability is the big question.

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

CHRISTINE Justin, do you--

TODARO:

JUSTIN KLEIN: And just to caveat that. I don't think that's necessarily a negative thing. I think that's probably a positive thing that they should be doing in any event, but I do think it's an added cost.

CHRISTINE Do you have a sense whether prospective franchisees compare offerings based on
TODARO: FPRs?

JUSTIN KLEIN: 100%. A lot of folks go on and look at-- go on the internet, and they say, what does this FPR say versus what does this FPR say? And they make their initial decision to

pursue a prospective investment based on the information that the franchisor is providing in the document.

Again, from our perspective, the FDD and the FPR is step 1 or step negative 1 of the process. But I do think that's information that prospective franchisees are looking at. And oftentimes, they're looking at the quality of the product or the service that's being provided.

And sometimes they mistake the quality of the product for the ability to be successful selling that product or service. And I think a component of that is the information that's being provided in the FDD creates an initial mindset as to whether or not they think it's an appropriate investment for them. How much does it cost and how much can I make? Line up 5 FDDs across the board because this is the industry that I'm interested in, and let me see what the information says.

CHRISTINE

Dale, is there something you want to respond to on that?

TODARO:

DALE

CANTONE:

I just wanted to point out that Justin is talking about a category of prospective franchisee that is coming to somebody like Justin to help them review the disclosure document. I can tell you the people that-- a lot of the people that we hear from at the state level who have had issues do not go to a lawyer. They can't afford to go to a lawyer, or they choose not to go to a lawyer.

And from the number of filings that we see, we can tell that there's a significant number of franchise systems out there that are targeting people that probably are not going to a lawyer, much less an accountant, much less fully reviewing disclosure document to make this choice, this determined choice whether or not to buy something based on the disclosure.

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

CHRISTINE

TODARO:

OK, Susan. I think you have a follow up, and then I'd like to go on to the next topic, just being cognizant of time.

SUSAN Yeah. I just wanted to add that in terms of market forces, franchisors will look and

GRUENEBERG: compare different FPRs with their competitors in their industry. And they know they're being compared. So they're going to logically try to get a better representation in their FDD in terms of what they're disclosing. So it does encourage the use of FPRs when you have this comparison going on, so I think it's very healthy.

CHRISTINE OK. Thank you. I'd like to move to next consideration, which was potential liability.

TODARO: Another factor that the FTC considered was whether mandatory FPRs might subject franchisees to potential liability for providing inaccurate data to franchisors who then use that information in their FPR.

I'd like to direct this question to Sandy. Since 2007, have you seen an increase in litigation between franchisees and franchisors on this issue?

SANDY WALL: Not at all. I mean, I think you could ask really any litigator, and they will tell you that up to this point, I'm not aware of any franchisor that has ever tried to bring an action against a franchisee on the basis of information provided that became the basis for an FPR. However, I think that a big part of the reason for that is that FPRs are not mandated, and franchisors that provide FPRs need to have a reasonable basis for putting this information together. And if the information they get from prospective franchisees is, in their judgment, not reliable, they are not going to put an FPR together.

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

In addition, most franchise agreements have indemnification provisions that state that the franchisee has to indemnify the franchisor for issues related to the operation in the business. And again, you could see that those types of provisions could be used. Again, it's unprecedented. You haven't seen it today, because if the

franchisor is not comfortable with the information, they don't prepare the FPR.

CHRISTINE Susan, do you have a follow up on that?

TODARO:

SUSAN Well, I'll just say that my experience has been anecdotally the same as Sandy's. I

GRUENEBERG: haven't seen those kind of claims. To protect against being in that situation to begin with, however, what I think you're seeing more of in FPRs is an explanation of where this data came from, why it could be different from a franchisee's experience, a prospective franchisee's experience. And those explanations are really crucial to explaining how there is a reasonable basis for the information being presented.

I know that later on in this workshop you're going to be talking about disclaimers, and I assume a lot of that discussion is going to center around disclaimers in Item 19. But what you have to be very careful about is not wiping out these explanations along with disclaimers. Because if it's crucial for a prospective franchisee to understand that their experience is not necessarily going to be the same as the franchisee on his data that this FPR was based.

CHRISTINE Dale, from a regulator's perspective, do you have any thoughts on this
TODARO: consideration?

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

CHRISTINE OK. I'd like to move now to the final consideration that we're going to discuss today,
TODARO: which is-- which was the commission's view that the FDD was not the only way or is not the only way for prospective franchisees to get financial performance information. And some of you have touched on that already, that FPRs are one piece of the puzzle when a prospective franchisee is deciding what business they want to participate in.

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

JUSTIN KLEIN: Yeah. And I'm sensitive to Dale's comment that most, if not many, if not the majority of franchisees don't hire lawyers or business advisors or counselors to help

them with this very important decision. As a lawyer, I highly recommend that to the extent you're going to make a large investment like that, you get the right people around you to help you make that investment decision.

One of things that we suggest to folks who are looking to get into franchising who are-- have never done it before is to also look at market conditions. What-- is the business that you're looking to buy? Is it appropriate for the area that you're looking to operate in? And have you spoken to people in the area?

Have you spoken to competitors? Have you spoken to the extent that the franchisor has multiple brands, have you spoken to franchisees of other brands that they operate in? How are the training programs, talking about what the franchisor has to offer separate and apart from what is actually in the document?

Christine, I'm big on trust but verify as a lawyer, I guess. So I presume that everybody is good at heart and the information that's being included in the FDD is accurate. But when I say the FDD is really step 1, the FDD is really step 1 because it's giving you information to then go out and verify. Whether it's with other franchisees, whether it's with competitors in the market, whether it's with other systems that they have, whether it's with folks who may be in independent businesses that are not necessarily operating under a franchise system but are in a similar type of a business.

Again, I'm-- guess because I'm a lawyer, I'm way risk averse. So I'm not a prime candidate to buy a franchise anyway. But there is never enough information that you could gather from an investment perspective, and I think the real value of the FDD is it gives you a starting point to start from to use that information to begin the journey of your due diligence.

CHRISTINE OK. And I want to now turn to Keith and say, what are your thoughts on these other
TODARO: sources

KEITH MILLER: Well--

CHRISTINE --for a prospective franchisee to use.
TODARO:

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

One of the things I'm often quoted in saying is one of the problems in the industry is far too many people profit from the sale of a franchise. Far too few are held accountable for the success of that sale.

Another one that I found quite often is loan brokers. When people start working on their financing, even in advance of signing the franchise agreement, these loan brokers often know what needs to be put on the loan applications to qualify for loans, especially the government guaranteed SBA 7(a) loans. And they know how to fill out those forms to get someone qualified to buy that business, and they're reverse engineering the numbers to get up to revenue.

Again, they have no accountability of that person. So I worry that there is these people outside of the franchise company that are throwing around numbers that people too often take as being gospel and they're not. And people always say, well, do your due diligence by contacting franchisees.

And I would say to that, well, if the franchisor gives you that-- obviously, the list is in the disclosure document of existing franchisees. But often a franchise owner will give people a list that's basically the top performers, which is skewing the information. And then if you try to go out and look for past franchisees, if you look within the disclosure documents, often the contact information is wrong and you can't get a hold of that franchisee.

And then if there was a bad exit by a franchisee, there's often a non-disclosure agreement that's been signed. So you won't hear the downside of the stories. You tend to be-- when you try to contact franchisees, current or past, tend to get skewed to the better franchisees.

And if you're-- even with existing franchisees, if it's a troubled franchisee, there's cases right now where existing franchisees are being sued in violation of the non

disparagement agreements that are within the franchise agreement. So I really don't see franchisees often as being a reliable source.

And that's why, of course, I push hard for more data in the disclosure document. Because there is some liability and responsibility in that, and I believe that information in general can be trusted.

**CHRISTINE
TODARO:** Sandy, do you have a follow up to what Keith just said?

SANDY WALL: I mean, Keith, again, I think we're-- you're focused on the bad actor here. I mean, what you're talking about here is if a franchisor and gives a prospective franchisee-- steers them to specific existing franchisees, that's a violation of the disclosure requirements. And, again, there is a list of franchisees given. There is a list of franchisees who have left the system in the last 12 months. And the franchisee, perspective franchisee, needs to do their homework and make the calls.

What you're referring to about the confidentiality agreements is addressed in Item 20 the of the FDD. If the franchisor restricts the ability of franchisees to talk about their experience with the system, that has to be disclosed in Item 20 of the FDD also.

Again, this is the purpose of disclosure is to help prospective franchisees make informed decision making. The information is there. And if you see all these things in there, if you're getting information that's inconsistent with what's in the FDD, or you see that all franchisees are required to sign these types of confidentiality agreements, these are red flags. And, again, the prospective franchisee has the choice to proceed or not to proceed.

**CHRISTINE
TODARO:** OK. I would like to jump to a new topic outside of mandatory FPRs, because the NASAA FPR commentary, which Susan had mentioned earlier-- Dale, NASAA noted in its 2019 comment that the FTC should consider incorporating the NASAA FPR commentary into the franchise rule. Why would this be helpful?

**DALE
CANTONE:** The FPR commentary-- well, actually the FPR commentary that NASAA did, the original impetus was to correct a misconception about the use of affiliate data. And that stemmed from an unfortunate footnote in the clients' guide of 2008 that

suggested that franchisors, if they have adequate operating experience of their own, should not use affiliate data. But, in fact, affiliate often are the owners of company-owned outlets.

So the original impetus was clarify the use of company-owned outlet data. I may be biased, but I have, in the last couple of years, it seems to me that the NASAA FPR commentary has been very well accepted in the industry. It's used extensively. It has not been a very controversial, for the most part, guidance issued by NASAA.

And it does address a lot of issues that needed to be addressed that were open. The use of affiliate data, subsets, and it's been working extremely well in the state regulatory environment. That's my perception, but people on the panel can share their opinions of it as well. There really would be a benefit to have the guidance that is at the state level incorporated at the federal level.

CHRISTINE TODARO: Susan, do you have a sense of how likely franchisors are to comply with the commentary in non-registration states?

SUSAN GRUENEBERG: Yeah. I'm actually a little bit surprised at the question, because I think there is a view to comply with the commentary. And also, with the more recent guidance that NASAA provided about FPR disclosure in the middle of the COVID-19 pandemic.

In fact, I would also echo Dale's suggestion that it be incorporated. In fact, I think there's an appetite for more commentary and more guidance about Item 19 out there on all levels. Because the commentary is great as far as it goes, but it certainly doesn't address every issue that comes up.

And there are constantly new ones. And this kind of guidance is very helpful to us in preparing FPRs with the assurance that we're more likely to achieve that elusive, reasonable basis, which nobody seems to be able to define exactly. So I would definitely support it. And I do think there's widespread, or there should be widespread compliance with it in states that don't have their own state franchise laws regulating the offer and sale of franchises.

CHRISTINE TODARO: Dale, is there a follow up that you want to add?

DALE Yeah. I just wanted to add that if there is a concern about the fact that the

CANTONE: commentary might be impacting negatively the FPRs, I have data from my state. The year before the FPR commentary was adopted our records show that 60.87 of franchisors registered in my state made some type of FPR. The year after the NASAA FPR commentary was adopted, the number actually increased. So it did not negatively impact franchisors making FPRs. Just not how [INAUDIBLE].

CHRISTINE TODARO: OK. And Justin, just a follow-up on what Susan said. In your practice, do you see that franchisors in non-registration states are following NASAA commentary?

JUSTIN KLEIN: Yeah. No, I agree with both Dale and Susan on their ultimate conclusions. Again, my fear goes back to not only the franchisees who can't hire lawyers who are qualified, but franchisors who can't hire lawyers who are qualified. And my bigger concern is whether or not folks are actually complying with the regulations that are out there.

So I think the more information that can be-- the more guidance that can be given, the better it is. But, again, our biggest fear is garbage in, garbage out. And I think I must there's some enforcement perspective to what the requirements are, then I'm not really sure what the value of any of it is.

CHRISTINE TODARO: And Sandy, do you have a follow-up on that?

SANDY WALL: Yeah. Again, I think the FPR commentary has provided terrific guidance in many areas. The only caution I would mention at this point is the whole issue of disclaimers and providing factual information that explains what the FPRs covers and what it doesn't cover. that's still an ongoing discussion that franchisors and state regulators have.

And I just would want there to be caution there that, again, while some of the language in commentary is absolutely clear, what you can and cannot do, there are certain sections in there which are open to interpretation. And therefore, I guess I'd be more for presumption that the FPR-- if you don't comply with the commentary, you're in compliance with the FTC rule, rather than just saying, absolutely comply. Because I'm not sure in some instances it is 100% clear what you need to do to comply with the commentary.

CHRISTINE OK. Thank you. Just on the final point, I want to note, Susan, you touched on this

TODARO: which is reasonable basis. And I think, Dale, you did as well. Is there confusion in the industry about what a reasonable basis is?

And this will be our final point because we are at the end of our panel. So I'll turn it over to Dale.

DALE
CANTONE: I think there is. I mean, first of all, it's not defined anywhere. Under the rule, franchisors have the burden to show they have a reasonable basis. So in some ways, that's kind of unfair to franchisors.

But I can tell you from our experience-- somebody mentioned the NASAA franchise project group's guidance on making an FPR during the pandemic. I cannot tell you how many franchisors, in response to questions from state regulators, who are under the impression that all you need to have is historically accurate information. I don't think that is entirely the reasonable basis. So the fact that many legitimately represented franchisors had that impression, I think, leads me to believe there is some confusion about what exactly is a reasonable basis, at least in the context of historical FPRs.

CHRISTINE [INAUDIBLE]. Sandy, do you agree with that?

TODARO:

SANDY WALL: Again, I think taking the view that it's historical isn't really the full analysis that you have to engage in here. You look at the FTC rule and Section 436.7(d), a franchisor's obligated to notify the prospective franchisee of material changes that the seller knows or should have known occurred in the information contained in the FPR. And I think that clearly addresses an obligation to be looking at your FPRs constantly to make sure that the reasonable basis that you had when it was prepared still exists today.

Again, also franchisees, prospective franchisees, have the right to request substantiation of the information in the FPR. And, again, I think that's something that's not used as much as you would think in the industry. So while a reasonable basis isn't defined, I'm not sure you could ever properly define it. I think it's a question of fact that the franchisor is responsible for determining and would have to prove in a court of law if necessary.

CHRISTINE OK. And with that, I want to thank each of the panelists for participating today. We've
TODARO: just run slightly over time, but thanks for bearing with us. I think this is a very interesting and informative discussion, so thank you very much.

JUSTIN KLEIN: Thank you.

KEITH MILLER: Thank you, Christine

SUSAN Thank you.

GRUENEBERG: