



## Understanding the UFOC and Franchising Laws

### **Overview of U.S. Franchising Regulations**

The offer and sale of a franchise is regulated at both the federal and state level. At the federal level, the Federal Trade Commission (FTC) in 1979 adopted its trade regulation rule 436 (the "FTC Rule") which specifies the minimum amount of disclosure that must be made to a prospective franchisee in any of the fifty states. In addition to the FTC Rule, over a dozen states have adopted their own rules and regulations for the offer and sale of franchises within their borders. Known as the registration states, they include most of the nation's largest commercial marketplaces, such as California, New York, and Illinois. These states generally follow a more detailed disclosure format, known as the Uniform Franchise Offering Circular (the UFOC).

The UFOC was originally developed by the Midwest Securities Commissioners Association in 1975. The monitoring of and revisions to the UFOC are now under the authority of the North American Securities Administrators Association (NASAA). Each of the registration states has developed and adopted its own statutory version of the UFOC. The differences among the states should be checked carefully by both current and prospective franchisors and their counsel, as well as individuals considering the purchase of a franchise opportunity.

A new version of the UFOC was adopted by NASAA in April of 1993 and approved by the FTC in December of 1993. As of January 1, 1995, the registration states had approved the new UFOC and mandated its use for filings in their states. The new UFOC Guidelines ("Guidelines") require that the offering circular be written in plain English. Disclosures must be made "clearly, concisely and in a narrative form that is understandable by a person unfamiliar with the franchise business" and should not contain technical language, repetitive phrases or "legal antiques."

### **Brief History of Franchise Registration**

The laws governing the offer and sale of franchises began in 1970, when the state of California adopted its Franchise Investment Law. Shortly thereafter, the FTC commenced its hearings to begin the development of the federal law governing franchising. After seven years of public comment and debate, the FTC adopted its trade regulation rule that is formally titled "Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Venture" on December 21, 1978, to be effective October 21, 1979. Many states followed the lead of California, and there are now fifteen states that regulate franchise offers and sales.

The states that require full registration of a franchise offering prior to the "offering" or selling of a franchise are *California, Illinois, Indiana, Maryland, Minnesota, New York, North Dakota, Rhode Island, South Dakota, Virginia, and Washington.*

Other states that regulate franchise offers include *Hawaii*, which requires filing of an offering circular with the state authorities and delivery of an offering circular to prospective franchisees; *Michigan and Wisconsin*, which require filing of a “Notice of Intent to Offer and Sell Franchises;” *Oregon*, which requires only that pre-sale disclosure be delivered to prospective investors; and *Texas*, which requires the filing of a notice of exemption with the appropriate state authorities under the Texas Business Opportunity Act.”

Among other things, the FTC Rule requires that every franchisor offering franchises in the United States deliver an offering circular (containing certain specified disclosure items) to all prospective franchisees (within certain specified time requirements). The FTC has adopted and enforced its rule pursuant to its power and authority to regulate unfair and deceptive trade practices. The FTC Rule sets forth the minimum level of protection that shall be afforded to prospective franchisees. To the extent that a “registration state” offers its citizens a greater level of protection, the FTC Rule will not preempt state law. There is no private right of action under the FTC Rule; however, the FTC itself may bring an enforcement action against a franchisor that does not meet its requirements. Penalties for noncompliance have included asset impoundments, cease and desist orders, injunctions, consent orders, mandated rescission or restitution for injured franchisees, and civil fines of up to \$10,000 per violation.

The FTC Rule regulates two types of offerings: (1) package and product franchises and (2) business opportunity ventures. The first type involves three characteristics: (i) the franchisee sells goods or services that meet the franchisor’s quality standards (in cases where the franchisee operates under the franchisor’s trademark, service mark, trade name, advertising, or other commercial symbol designating the franchisor (“mark”)) that are identified by the franchisor’s Mark, (ii) the franchisor exercises significant assistance in the franchisee’s method of operation, and (iii) the franchisee is required to make payment of \$500 or more to the franchisor or a person affiliated with the franchisor at any time before to within six months after the business opens.

Business Opportunity Ventures also involve three characteristics : (i) the franchisee sells goods or services that are supplied by the franchisor or a person affiliated with the franchisor; (ii) the franchisor assists the franchisee in any way with respect to securing accounts for the franchisee, or securing locations or sites for vending machines or rack displays, or providing the services of a person able to do either; and (iii) the franchisee is required to make payment of \$500 or more to the franchisor or a person affiliated with the franchisor at any time before to within six months after the business opens.

Relationships covered by the FTC Rule include those within the definition of a “franchise” and those represented as being within the definition when the relationship is entered into, regardless of whether, in fact, they are within the definition. The FTC Rule exempts 1) fractional franchises, 2) leased department arrangements, and 3) purely verbal agreements. The FTC Rule excludes 1)

relationships between employer/employees and among general business partners, 2) membership in retailer-owned cooperatives, 3) certification and testing services, and 4) single trademark licenses.

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The information must be current as of the completion of the franchisor's most recent fiscal year. In addition, a revision to the document must be promptly prepared whenever there has been a material change in the information contained in the document. The FTC Rule requires that the disclosure document must be given to a prospective franchisee at the earlier of either 1) the prospective franchisee's first personal meeting with the franchisor; or 2) ten business days prior to the execution of a contract; or 3) ten business days before the payment of money relating to the franchise relationship. In addition to the disclosure document, the franchisee must receive a copy of all agreements that it will be asked to sign at least five business days prior to the execution of the agreements. A business day is any day other than Saturday, Sunday, or the following national holidays: New Year's Day, Washington's Birthday, Memorial Day, Independence Day, Labor Day, Columbus Day, Veteran's Day, Thanksgiving, and Christmas.

The timing requirements described above apply nationwide and preempt any lesser timing requirements contained in state laws. The ten-day and five-day disclosure periods may run concurrently, and sales contacts with the prospective franchisee may continue during those periods.

It is an unfair or deceptive act or practice within the meaning of Section 5 of the FTC Act for any franchisor or franchise broker:

1. To fail to furnish prospective franchisees, within the time frame established by the Rule, with a disclosure document containing information on twenty different subjects relating to the franchisor, the franchise business, and the terms of the franchise agreement
2. To make any representations about the actual or potential sales, income, or profits of existing or prospective franchisees except in the manner set forth in the rule

3. To fail to furnish prospective franchisees, within the time frame established by the rule, with copies of the franchisor's standard form of franchise agreement and copies of the final agreements to be signed by the parties
4. To fail to return to prospective franchisees any funds or deposits (such as down payments) identified as refundable in the disclosure document

### **State Franchise Laws**

The goal of the FTC Rule is to create a minimum federal standard of disclosure applicable to all franchisor offerings and to permit states to provide additional protection as they see fit. Thus, while the FTC Rule has the force and effect of federal law and, like other federal substantive regulations, preempts state and local laws to the extent that these laws conflict, the FTC has determined that the rule will not preempt state or local laws and regulations that either are consistent with the rule or, even if inconsistent, would provide protection to prospective franchisees equal to or greater than that imposed by the rule.

Examples of state laws or regulations that would not be preempted by the Rule include state provisions requiring the registration of franchisors and franchise salespersons, state requirements for escrow or bonding arrangements, and state-required disclosure obligations set forth in the Rule. Moreover, the Rule does not affect state laws or regulations that regulate the franchisor/franchisee relationship, such as termination practices, contract provisions, and financing arrangements.

#### ***Definitions Under State Law***

Each state franchise disclosure statute has its own definition of a "franchise," which is similar to, but not the same as, the definition set forth in the FTC Rule. If the proposed relationship meets this definition, then the franchisor must comply with the applicable registration and disclosure laws.

There are three major types of state definitions of a franchise or business opportunity. They consist of:

- A. Majority State Definition. In the states of California, Illinois, Indiana, Maryland, Michigan, North Dakota, Oregon, Rhode Island, and Wisconsin, a franchise is defined as having three essential elements:
  1. A franchisee is granted the right to engage in the business of offering, selling, or distributing goods or services under a marketing plan or system prescribed in substantial part by a franchisor.

2. The operation of the franchisee's business . . . is substantially associated with the franchisor's trademark or other commercial symbol designating the franchisor or its affiliate.

3. The franchisee is required to pay a fee.

B. Minority State Definition. The states of Hawaii, Minnesota, South Dakota, and Washington have adopted a somewhat broader definition of *franchise*. In these states, a franchise is defined as having the following three essential elements:

1. A franchisee is granted the right to engage in the business of offering or distributing goods or services using the franchisor's trade name or other commercial symbol or related characteristics.

2. The franchisor and franchisee have a common interest in the marketing of goods or services.

3. The franchisee pays a fee.

C. New York Definition. The state of New York has a unique definition. Under its law a franchisee is defined by these guidelines:

1. The franchisor is paid a fee by the franchisee.

2. Either essentially associated with the franchisor's trademark or the franchisee operates under a marketing plan or system prescribed in substantial part by the franchisor.

D. Virginia Definition. The Commonwealth of Virginia also has its own definition of a franchise, which stipulates that:

1. A franchisee is granted the right to engage in the business of offering or distributing goods or services at retail under a marketing plan or system prescribed in substantial part by a franchisor.

2. The franchisee's business is substantially associated with the franchisor's trademark.

Virginia and New York have definitions that are broad in certain respects. Virginia does not have a "fee" element to its definition. New York requires a fee, but specifies *either* association with franchisor's trademark *or* a marketing plan prescribed by the franchisor. Therefore, in New York no

trademark license is required for a franchise relationship to exist. However, the regulations in New York exclude from the definition of a franchise any relationship in which a franchisor does not provide significant assistance to or exert significant controls over a franchisee.

### **Understanding the UFOC Disclosure Document**

The UFOC format of franchise disclosure consists of 23 categories of information that must be provided by the franchisor to the prospective franchisee at least ten business days prior to the execution of the franchise agreement. Because this format has been adopted by many states as a matter of law, franchisors may not change the order in which information is presented, nor may any of the disclosure items be omitted in the document. In addition, many sections of the UFOC must be a mirror image of the actual franchise agreement (and related documents) that the franchisee will be expected to sign. There should be no factual or legal inconsistencies between the UFOC and the franchise agreement.

## Preparing the Disclosure Document Under UFOC Guidelines

The UFOC format of franchise disclosure consists of 23 categories of information that must be provided by the franchisor to the prospective franchisee at least ten business days prior to the execution of the franchise agreement. Because this format has been adopted by many states as a matter of law, franchisors may not change the order in which information is presented, nor may any of the disclosure items be omitted in the document. In addition, many sections of the UFOC must be a mirror image of the actual franchise agreement (and related documents) that the franchisee will be expected to sign. There should be no factual or legal inconsistencies between the UFOC and the franchise agreement.

A description of the information required by each disclosure item of the UFOC is as follows:

- Cover Page: NASAA has sought to create a generic cover page by moving state-specific information to Item 23 (Receipt) or to exhibits to the offering circular. Information moved off of the cover page includes state-mandated language regarding offering circular delivery requirements and related disclaimers, addresses of administrators and the list of registered agents, subfranchisors and franchise brokers. The Guidelines mandate disclosure of certain risk factors. A franchisor must use prescribed language to disclose as a risk that its franchise agreement includes an out-of-state form and/or choice of law provision. Additional risk factor disclosures may be required by state regulators.
- Item 1: THE FRANCHISOR, ITS PREDECESSORS AND AFFILIATES. Franchisors must identify themselves by using “we,” initials or two words of reference. “Franchisor” and “Franchisee” are not be used. The entities for which disclosure must be made are expanded to include franchisor’s affiliates. The number of years of the franchisor’s predecessors is reduced from 15 to 10. Agents for service of process may be disclosed in Item 1, Item 23 (Receipt) or an exhibit to the offering circular. In addition, franchisors must disclose, in general terms, “any regulations specific to the industry in which the franchise business operates.” Regulations which are applicable to businesses generally need not be disclosed.
- Item 2: BUSINESS EXPERIENCE. This section requires disclosure of the identity of each director, trustee, general partner (where applicable) and officer or manager of the franchisor who will have significant responsibility in connection with the operation of the franchisor’s business or in the support services to be provided to franchisees. The principal occupation of each person listed in Item 2 for the past five years must be disclosed, including dates of employment, nature of the position, and the identity of the employer. The identity and background of each franchise broker (if any) authorized to represent the franchisor must also be disclosed in this Item.
- Item 3: LITIGATION. A full and frank discussion of any litigation, arbitration, or administrative hearings affecting the franchisor, its officers, directors, or sales representatives over the past ten years should be included in this section. The formal case name, location of the dispute, nature of the claim, and the current status of each action must be disclosed. Item 3 does not require disclosure of all types of litigation but rather focuses on specific allegations and

proceedings that would be of particular concern to the prospective franchisee. “Ordinary routine litigation incidental to the business” is not to be considered material. Litigation is deemed “ordinary routine” if it “ordinarily results from the business and does not depart from the normal kind of actions in the business.”

Item 4: BANKRUPTCY. This section requires the franchisor to disclose whether the company or any of its predecessors, officers, or general partners, have during the past ten years been adjudged bankrupt or reorganized due to insolvency. The court in which the bankruptcy or reorganization proceeding occurred, the formal case title, and any material facts and circumstances surrounding the proceeding must be disclosed.

Item 5: INITIAL FRANCHISE FEE. The initial franchise fee and related payments to the franchisor prior to opening the franchise must be disclosed in this section. The manner in which the payments are made, the use of the proceeds by the franchisor, and whether or not the fee is refundable in whole or in part must be disclosed. If the initial franchise fee is not uniform, the franchisor must disclose the formula or range of initial fees received by it in the most recent fiscal year prior to the application date.

Item 6: OTHER FEES. A tabular form of any other initial or recurring fee payable by the franchisee to the franchisor or any affiliate must be disclosed and the nature of each fee fully discussed, including but not limited to, royalty payments, training fees, audit fees, public offering review fees, advertising contributions, mandatory insurance requirements, transfer fees, renewal fees, lease negotiation fees, and any consulting fees charged by the franchisor or an affiliate for special services. The amount, time of the payment, and refundability of each type of payment should be disclosed. A “remarks” column or footnotes may be used to elaborate on the information about the fees disclosed in the table. In addition, if fees are paid to a franchisee cooperative, the franchisor must disclose the voting power of its outlets in the cooperative. Further, the range of any fees imposed by that cooperative must be disclosed if the franchisor’s outlets have controlling voting power.

Item 7: INITIAL INVESTMENT. Each component of the franchisee’s initial investment that the franchisee is required to expend in order to open the franchised business must be estimated in this section, in a prescribed tabular form, regardless of whether such payments are made directly to the franchisor. Real estate, equipment, fixtures, security deposits, inventory, construction costs, working capital, accounting and legal fees, license and permit fees, and any other costs and expenditures should be disclosed. The disclosure should include to whom such payments are made, under what general terms and conditions, and what portion, if any, is refundable. A payment must be disclosed if it is required to be paid during the “initial phase” of the business. The Guidelines instruct that “[a] reasonable time for the initial phase of the business is at least three months or a reasonable period for the industry.” The Guidelines also require disclosure of additional funds required during the initial phase and the factors, basis and experience upon which the franchisor bases its calculation.

Item 8: RESTRICTIONS ON SERVICES OF PRODUCTS AND SERVICES. Any obligation of the franchisee to purchase goods, services, supplies, fixtures, equipment, or inventory that relates to the establishment or operation of the franchised business from a source designated by the franchisor should be disclosed. The terms of the purchase or lease as well as any minimum-volume purchasing requirements must be disclosed. If the franchisor will or may derive

direct or indirect income based on these purchases from required sources, then the nature and amount of such income must be fully disclosed. Remember that such obligations must be able to withstand the scrutiny of U.S. antitrust laws. In addition to disclosing whether the franchisor or its affiliates will or may derive revenue or material consideration as a result of franchisees' required purchases or leases, the franchisor must also disclose the estimated proportion of these required purchases and leases to all purchases and leases by the franchisee of goods and services necessary to establish and operate the franchise. The franchisor must disclose whether there are any purchasing or distribution cooperatives serving its system. The franchisor must disclose, based on immediately preceding years' financial statements, its: 1) total revenues; 2) revenues derived from required purchases and leases of products and services; and 3) the percentage of its total revenues from such required purchases and leases. If the franchisor's affiliates also sell or lease products or services to franchisees, the franchisor must also disclose the percentage of the affiliates revenues derived from these sales or leases. Any fees required for approval of a new supplier must also be disclosed. In addition, the franchisor must disclose whether it offers franchisees inducements, such as renewal or additional franchises, for purchasing goods or products from designated or approved sources.

Item 9: FRANCHISEES' OBLIGATIONS Franchisors must set forth the franchisees' obligations in a prescribed tabular form with regard to 24 specific categories. The table must cite the relevant sections of both the franchise agreement and offering circular.

Item 10: FINANCING. In this section, the franchisor must disclose the terms and conditions of any financing arrangements offered to franchisees either by the franchisor or any of its affiliates. The exact terms of any direct or indirect debt financing, equipment or real estate leasing programs, operating lines of credit, or inventory financing must be disclosed. If any of these financing programs is offered by an affiliate, then the exact relationship between the franchisor and the affiliate must be disclosed. Terms that may be detrimental to the franchisee upon default, such as a confession of judgment, waiver of defenses, or acceleration clauses, must be disclosed in this Item of the UFOC. The terms and conditions of "indirect offers of financing" made to franchisees must be disclosed. An "indirect offer of financing" includes: 1) a written arrangement between the franchisor, or its affiliate, and a lender for the lender to offer financing to franchisees; 2) an arrangement in which the franchisor or its affiliate receives benefits from a lender for franchisee financing; and 3) the franchisor's guarantee of a note, lease or obligation of the franchisee. Franchisors are permitted, but not required, to make disclosure in tabular form. Franchisors must disclose the annual percentage rate of interest ("APR") charged for financing, computed in accordance with Sections 106-107 of the Consumer Protection Credit Act, 15 U.S.C. (sections) 106-107. If the APR varies depending on when the financing is issued, franchisor must disclose the APR as of a disclosed recent date. Franchisor must disclose to the franchisee the consequences of any default of its obligations, including operation of any cross-default provisions, acceleration of amounts due, and payment of court costs and attorneys' fees. In addition, Franchisors must include in the offering circular specimen copies of any financing documents.

Item 11: FRANCHISOR'S OBLIGATIONS. This section is one of the most important to the prospective franchisee because it discusses the initial and ongoing support and services provided by the

franchisor. Franchisors must disclose only those pre-opening obligations which they are contractually required to provide to franchisees. Pre-opening assistance that the franchisor intends to provide, but to which it is not contractually bound to provide, may not be included. Accordingly, this disclosure must begin with the following sentence: “[e]xcept as listed below, (franchisor) need not provide any assistance to you.” Franchisors must make comprehensive disclosures regarding advertising, including: 1) the type of media in which the advertising may be distributed; 2) whether the media coverage is local, regional or national in scope; 3) the source of the advertising (e.g., in-house or advertising agency); 4) the conditions under which franchisees are permitted to use their own advertising; and 5) if applicable, the manner in which the franchisee advertising council operates and advises the franchisor. Franchisors must make specific disclosures regarding local or regional advertising cooperatives, including: 1) how the area and/or membership of the cooperative is defined; 2) how franchisees’ contributions to the cooperative are calculated; 3) who is responsible for administration of the cooperative; 4) whether cooperatives must operate from written governing documents and whether the documents are available for review by franchisees; 5) whether cooperatives must prepare annual or periodic financial statements and whether such statements are available for review by franchisees; and 6) whether the franchisor has the power to form, change, dissolve or merge cooperatives. Franchisors must disclose information about advertising funds they administer, including: 1) the basis upon which franchisor-owned outlets contribute to the fund; 2) whether franchisees contribute at a uniform rate; and 3) the percentages of the fund spent on production, media placement, administrative and other expenses. Franchisor must also disclose whether they are obligated to advertise in the area in which the franchise is to be located and the percentage of funds used for advertising that is principally a solicitation for the sale of franchises. Franchisors are required to disclose whether franchisees must buy or use electronic cash registers or computer systems. If there is such a requirement, the franchisor must describe in non-technical language: 1) the hardware components; 2) the software program; and 3) whether such hardware and software are proprietary property of the franchisor, an affiliate or a third party. If the hardware or software is not proprietary, the franchisor must disclose: 1) whether the franchisee has any contractual obligation to upgrade or update the equipment, and if so, any limitations on the frequency and cost of such obligation; 2) how it will be used in the franchise; and 3) whether the franchisor has any independent access to information or data in the system. The new Guidelines expand disclosure regarding site selection procedures to include the factors considered by the franchisor in site selection or approval. In addition, a copy of the table of contents of the franchise Operating Manual must be included in the offering circular unless the prospective franchisee will view the manual before purchasing the franchise.

Item 12: **TERRITORY.** The exact territory or exclusive area, if any, to be granted by the franchisor to the franchisee should be disclosed, as well as the right to adjust the size of this territory in the event that certain contractual conditions are not met, such as the failure to achieve certain performance quotas. The right of the franchisor to establish company-owned units or to grant franchises to others within the territory must be disclosed. A detailed description and/or map of the franchisee’s territory should be included as an exhibit to the franchise agreement. In addition to disclosing whether it has established or may establish additional

franchised or company-owned outlets which may compete with franchisees' outlets, the franchisor must disclose whether it has established or may establish "other channels of distribution" under its mark. The franchisor must disclose the conditions under which it will approve the relocation of a franchise or the establishment of additional franchises. In addition, a franchisor must disclose whether it or an affiliate operates or has plans to operate another chain or channel of distribution under a different trademark to sell goods or services which are similar to those offered by the franchise. If the franchisor operates competing systems, it must also disclose the methods it will use to resolve conflicts between them regarding territory, customers and franchisor support. If the principal business address of the competing system is the same as franchisor's, it must also disclose whether it maintains separate offices and training facilities.

- Item 13: TRADEMARKS. Franchisors need only disclose the principal trademarks, rather than all trademarks, to be licensed to the franchisee. If a principal trademark is not federally registered, franchisors must include a statement that "[b]y not having a Principal Register federal registration for (trademark), franchisor does not have certain presumptive legal rights granted by a registration."
- Item 14: PATENTS, COPYRIGHTS AND PROPRIETARY INFORMATION. If the franchisor claims proprietary rights in confidential information or trade secrets, it must disclose the general subject matter of its proprietary rights and the terms and conditions under which they may be used by the franchisee.
- Item 15: OBLIGATION TO PARTICIPATE IN THE ACTUAL OPERATION OF THE FRANCHISED BUSINESS. Franchisors are required to disclose obligations arising from its practices, personal guarantees, and confidentiality or non-competition agreements.
- Item 16: RESTRICTIONS ON WHAT THE FRANCHISEE MAY SELL. In this section the franchisor must disclose any special contractual provisions or other circumstances that limit either the types of products and services the franchisee may offer or the types or location of the customers to whom the products and services may be offered.
- Item 17: RENEWAL, TERMINATION, TRANSFER AND DISPUTE RESOLUTION. The disclosures must be presented in a prescribed tabular form. The table must contain abbreviated summaries regarding 23 specific categories with references to relevant sections of the franchise agreement. Preceding the table, the offering circular must state: "[t]his table lists important provisions of the franchise and related agreements. You should read these provisions in the agreements attached to this offering circular."
- Item 18: PUBLIC FIGURES. Any compensation or benefit given to a public figure in return for an endorsement of the franchise and/or products and services offered by the franchisee must be disclosed. The extent to which the public figure owns or is involved in the management of the franchisor must also be disclosed. The disclosure is only required if a public figure endorses or recommends an investment in the franchise to prospective franchisees. Consequently, franchisors need not disclose franchisees' rights to use the names of public figures who are featured in consumer advertising or other promotional efforts.
- Item 19: EARNINGS CLAIMS. If the franchisor is willing to provide the prospective franchisee with sample earnings claims or projections, they must be discussed in Item 19.

- Item 20: **LIST OF FRANCHISE OUTLETS.** A full summary of the number of franchises sold, number of operational units, and number of company-owned units, including an estimate of franchise sales for the upcoming fiscal year broken down by state. The names, addresses, and telephone numbers of franchisees should be included in this Item. With the exception of the list of franchise names, addresses, and telephone numbers, franchisors must disclose all information required by this Item in tabular form. The franchisor must disclose the number of franchised and company-owned outlets sold, opened and closed in its system as of the close of each of its last three fiscal years. Operational outlets must be listed separately from those not opened, and disclosure must be provided on a state-by-state basis. The franchisor may limit its disclosure of the franchisees' names, addresses and telephone numbers to those franchised outlets in the state in which the franchise offering is made if there are 100 outlets in such state. If there are fewer than 100 in the state, the franchisor must disclose the names, addresses and telephone numbers of franchised outlets from contiguous states and, if necessary, the next closest states until at least 100 are listed. For the three-year period immediately before the close of its most recent fiscal year, the franchisor must disclose the number of franchised outlets which have: 1) had a change in "controlling ownership interest;" 2) been canceled or terminated; 3) not been renewed; 4) been re-acquired by the franchisor; or 5) otherwise ceased to do business in the system. The franchisor must disclose the last known home address of every franchisee who has had an outlet terminated, canceled, not renewed, or who otherwise voluntarily or involuntarily ceased to do business under the franchise agreement during the most recently completed fiscal year end or who has not communicated with the franchisor within ten weeks of the application date. In addition, the franchisor must disclose information about company-owned outlets that are substantially similar to its franchised outlets. The same table may be used for both franchised and company-owned outlets so long as the data regarding each is set out in a distinct manner.
- Item 21: **FINANCIAL STATEMENTS.** The franchisor must include its audited balance sheet for the last two fiscal years. Audited statements of operations, stockholder's equity and cash flow are required for the franchisor's last three fiscal years. If the most recent balance sheet and statement of operations are as of a date more than 90 days before the application date, the franchisor must also include an unaudited balance sheet and statement of operations for a period falling within 90 days of the application. If the franchisor does not have audited financial statements for its last three fiscal years, it may provide either 1) an audited financial statement for its last fiscal year and, if the audit is not within 90 days of the application date, an unaudited balance sheet and income statement for a period falling within 90 days of application; or 2) an unaudited balance sheet as of the date within 90 days of the application and an audited income statement from the start of its fiscal year through the date of the audited balance sheet.
- Item 22: **CONTRACTS.** A copy of the franchise agreement as well as any other related documents to be signed by the franchisee in connection with the ownership and operation of the franchised business must be attached as exhibits to the UFOC.
- Item 23: **RECEIPT.** Franchisors are required to provide two copies of the Receipt in the offering circular, one to be kept by the prospective franchisee and the other to be returned to the franchisor. The franchisor must disclose the name, principal business address and telephone

number of any subfranchisor or franchise broker offering the franchise in the state. The Receipt must contain an itemized listing of all exhibits to the offering circular. If not previously disclosed in Item 1, the franchisor must disclose the name(s) and address(es) of its agent(s) authorized to receive service of process.

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## **ABOUT THE PRESENTER**

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