

NASAA MODEL FRANCHISE EXEMPTIONS

Adopted September 9, 2012

TEXT OF PROPOSED STATUTE GRANTING GENERAL AUTHORITY TO EXEMPT [If Required]

The [administrator] may, by regulation or order, and subject to any conditions [the administrator] requires, exempt any offer or sale, including transfer, of a franchise from any or all of the provisions of [the subtitle] if the [administrator] finds that the requirement is not within the purpose of [the subtitle] and not necessary or appropriate in the public interest or for the protection of prospective franchisees.

MODEL EXEMPTIONS

1. Fractional Franchise Exemption

(a) The registration and disclosure provisions of [the subtitle] shall not apply to any offer or sale, including transfer, of a franchise that satisfies the following criteria when the relationship is created:

(i) The franchisee, any of the franchisee's current directors or officers, or any current directors or officers of an affiliate, has more than 2 years of experience in the same type of business; and

(ii) The parties have a reasonable basis to anticipate that the sales arising from the relationship will not exceed 20% of the franchisee's total dollar volume in sales during the first year of operation.

(b) The exemption set forth in §1(a) of this (regulation)(statute) may be claimed only if the franchisor:

(i) Files a Notice of Exemption in the form prescribed by the [administrator]:

A. Not less than 14 calendar days before the offer or sale of any franchise in this State subject to this exemption, which Notice of Exemption shall expire after a period of one year; and

B. If the franchisor intends to offer or sell for an additional period annually after the expiration of an initial Notice of Exemption, at least 14 calendar days before the expiration of the previously filed Notice of Exemption;

(ii) Files a Consent to Service of Process naming the [administrator] as the franchisor's agent to receive process in this state; and

(ii) Pays the fee provided under this [subtitle] for filing an exemption.

(c) When interpreting the phrase “same type of business” contained in §1(a)(i), the required experience may be in the same business selling competitive goods or services, or in a business that a consumer would reasonably expect to sell the type of goods or services to be distributed under the franchise.

(d) A “reasonable basis” exists to anticipate sales volume sufficient to qualify for the exemption when both parties are capable of demonstrating that the franchisee can derive at least 80% of its total dollar volume in sales during the first year of operation independent of the franchise relationship.

(e) By filing a Notice of Exemption under §1(b) of this (regulation)(statute), the franchisor agrees to supply any additional information related to the franchise offering that the [administrator] may from time to time reasonably request.

2. Experienced Franchisor Exemption

(a) The registration provisions of § _____ of [the subtitle] shall not apply to any offer or sale, including transfer, of a franchise when and for as long as the franchisor meets all of the following requirements:

(i) The franchisor has shareholders,’ members’ or partners’ equity of not less than:

(1) \$10,000,000 on a consolidated basis, according to the franchisor’s audited financial statements for the immediately preceding fiscal year; or

(2) \$1,000,000, according to the franchisor’s financial statements for the immediately preceding fiscal year which may be audited or unaudited; and

(i) the franchisor is at least 80 percent owned directly or indirectly by a corporation or entity that has a shareholders,’ members’ or partners’ equity, on a consolidated basis, according to the entity’s audited financial statements for the immediately preceding fiscal year, of not less than \$10,000,000 (the “80 Percent Owner”); and

(ii) if the franchisor does not prepare audited financial statements of its own because its parent prepares consolidated audited financial statements, the franchisor submits a statement under penalty of perjury by an officer confirming that the franchisor has shareholders, members’ or partners’ equity of not less than \$1,000,000 for the immediately preceding fiscal year; and

- (iii) the 80 Percent Owner absolutely and unconditionally guarantees to assume the duties and obligations of the franchisor under the franchise agreement; and

(3) The audited financial statements required under this section shall be accompanied by an auditor's report that: (i) contains an unqualified opinion within the meaning of Statement on Auditing Standards No. 79 issued by The American Institute of Certified Public Accountants and codified at AU §508, as the same may be amended from time to time (or the equivalent provision of standards of the applicable governing body for accounting principles that are permitted for use by the Securities and Exchange Commission), and (ii) does not contain a going concern explanatory paragraph;

(ii) The franchisor or the 80 Percent Owner of the franchisor had at all times during the 5-year period immediately preceding the offer or sale at least 25 operating franchisees conducting substantially the same business as the franchise being offered, each of which was in operation for at least 24 months;

(iii) During the 10-year period immediately preceding the offer or sale, neither the franchisor, a predecessor, an affiliate who induces franchise sales by promising to back the franchisor financially or otherwise guarantees the franchisor's performance, an affiliate who offers franchises under the franchisor's principal trademark nor any of the franchisor's directors, trustees, general partners, principal officers or other individuals who will have management responsibility relating to the sale or operation of franchises was convicted of or pleaded nolo contendere to a felony charge; and

(iv) Neither the franchisor, a predecessor, or an affiliate who induces franchise sales by promising to back the franchisor financially or otherwise guarantees the franchisor's performance, an affiliate who offers franchises under the franchisor's principal trademark nor any of the franchisor's directors, trustees, general partners, principal officers or other individuals who will have management responsibility relating to the sale or operation of franchises is:

(1) subject to any currently effective order of the Securities and Exchange Commission or the securities administrator of any state denying registration to or revoking or suspending the registration of the person as a securities broker or dealer or investment advisor or is subject to any currently effective order of any national securities association or national securities exchange (as defined in the Securities and Exchange Act of 1934) suspending or expelling the person from membership in the association or exchange; or

(2) subject to a currently effective injunctive or restrictive order, decree or judgment issued during the 10-year period immediately preceding the offer or sale resulting from a pending or concluded action brought by any federal or state public agency or department and relating to the franchise or to a Federal, State, or Canadian franchise, securities, antitrust, trade regulation, or trade practice law.

(b) the exemption set forth in §2(a) of this (regulation)(statute) may be claimed only if the franchisor:

(i) Files a Notice of Exemption in the form prescribed by the [administrator] not less than 14 calendar days before the offer or sale of any franchise in this State subject to this exemption;

(ii) Files a Consent to Service of Process naming the [administrator] as the franchisor's agent to receive process in this state;

(iii) Pays the fee required under this [subtitle] for filing an exemption;

(iv) Submits financial statements demonstrating compliance with the conditions set forth in §2(a)(i) of this (regulation)(statute);

(v) Submits a written certification that the franchisor meets all of the conditions set forth in §2 (a)(ii) - (iv) of this (regulation)(statute); and

(vi) Files with the [administrator], in the format the [administrator] prescribes, one copy of the franchisor's current franchise disclosure document prepared under the Federal Trade Commission Franchise Rule, 16 C.F.R. Part 436 (the "FTC Franchise Rule") or the Franchise Registration and Disclosure law of a state.

(c) By filing a Notice of Exemption under §2(a) of this (regulation) (statute), the franchisor agrees to supply any additional information related to the franchise offering that the [administrator] may from time to time reasonably request.

(d) The [administrator] may, by order or written notice, summarily deny, suspend, or revoke an exemption claimed under this (regulation) (statute) or condition the exemption on additional requirements if, in the [administrator]'s discretion, granting the exemption does not serve the public interest or adequately protect prospective franchisees. The [administrator]'s summary denial, suspension or revocation of an exemption under §2(d) of this (regulation) (statute) does not act to summarily deny, suspend, or revoke a franchisor's registration filed under §___ of [the subtitle].

(e) The Notice of Exemption filed under §2(b) of this (regulation) (statute) shall expire after a period of one year. If the franchisor intends to offer or sell under this exemption for additional one year periods, the franchisor shall file a Notice of Exemption and all other documents required under §2(b), and pay the fee required under this [subtitle] for filing an exemption, not less than 14 calendar days before the expiration of each previously filed Notice of Exemption.

3. Sophisticated Purchaser Exemptions

(a) Existing Franchisee

(i) The registration provisions of § _____ of [the subtitle] shall not apply to any offer or sale, including transfer, of a franchise that meets all of the following requirements:

(1) The offer or sale is of an additional franchise (i) to an existing franchisee of the same franchisor, or (ii) to an entity of which one or more of its officers, directors, managing agents or owners has at least a 50 percent interest in an existing franchisee of the same franchisor;

(2) For twenty-four (24) months or more the franchisee, or an officer, director, managing agent or owner with at least a 50 percent interest in the franchisee, has been engaged in a business offering products or services substantially similar to those to be offered by the franchise being sold;

(3) The existing franchisee purchases the franchise from the franchisor in order to operate the business and not for the purpose of resale;

(4) The first sale to the existing franchisee was lawful at the time of the sale; and

(5) The sale under this exemption involves the execution of a franchise agreement that is substantially similar to the first franchise agreement between the franchisor and the existing franchisee.

(ii) The exemption set forth in §3(a)(i) of this (regulation)(statute) may be claimed only if the franchisor:

(1) Reports the sale to the [administrator] on the Notice of Exemption in the form prescribed by the [administrator] within 14 calendar days following the sale;

(2) Obtains from the prospective franchisee a signed acknowledgement verifying the grounds for the exemption;

(3) Files a Consent to Service of Process naming the [administrator] as the franchisor's agent to receive process in this state;

(4) Pays the fee required under this [subtitle] for filing an exemption; and

(5) Delivers to the prospective franchisee at least 14 calendar days before the sale of the franchise a Franchise Disclosure Document prepared under the FTC Franchise Rule or the Franchise Registration and Disclosure law of a state.

(iii) The exemption set forth in §3(a)(i) of this (regulation)(statute) applies only to the registration provisions, and not the disclosure provisions, of the [subtitle].

(iv) By filing a Notice of Exemption under §3(a)(ii) of this (regulation) (statute), the franchisor agrees to supply any additional information related to the franchise offering that the [administrator] may from time to time reasonably request.

(b) **Franchisor Insider**

(i) The registration and disclosure provisions of § _____ of [the subtitle] shall not apply to any offer, sale, including transfer, of a franchise that meets all of the following requirements:

(1) The offer, sale, or other transfer is made to one or more purchasers having at least a 50% ownership interest in the franchise who, within 60 days of the sale, has been, for at least two years, (i) an officer, director, general partner, or individual with management responsibility for the offer and sale or the operation of the franchisor's franchises; or (ii) an owner of at least a 25% interest in the franchisor; and

(2) The purchase of the franchise is in order to operate the business and not for the purpose of resale.

(ii) The exemption set forth in §3(b)(i) of this (regulation)(statute) may be claimed only if the franchisor:

(1) Reports the sale to the [administrator] on the Notice of Exemption form prescribed by the [administrator] within 14 calendar days following the sale;

(2) Obtains from the prospective franchisee a signed acknowledgement verifying the grounds for the exemption;

(3) Files a Consent to Service of Process naming the [administrator] as the franchisor's agent to receive process in this state; and

(4) Pays the fee required under this [subtitle] for filing an exemption.

(iii) The exemption set forth in §3(b)(i) of this (regulation)(statute) applies to both the registration and disclosure provisions of [the subtitle].

(iv) By filing a Notice of Exemption under §3(b)(ii) of this (regulation) (statute), the franchisor agrees to supply any additional information related to the franchise offering that the [administrator] may from time to time reasonably request.

(c) **Sophisticated Franchisee (Accredited Investor)**

(i) The registration provisions of § _____ of [the subtitle] shall not apply to any offer or sale, including transfer, of a franchise that meets all of the following requirements:

(1) Each and every purchaser of the franchise is one of the following:

a. A High Net Worth Individual, defined as a person whose net worth, or joint net worth with that person's spouse, exceeds three million dollars (\$3,000,000) at the time of his or her purchase of the franchise, excluding the value of that person's personal residence, any and all retirement or pension plan accounts or benefits, home furnishings, and automobiles;

b. A High Income Individual, defined as a person whose gross income exceeds five hundred thousand dollars (\$500,000) per year in each of the two most recent years, or whose joint gross income with that person's spouse exceeds seven hundred fifty thousand dollars (\$750,000) per year in each of those years, and who reasonably expects to reach the same income level in the year following the purchase of the franchise;

c. Any entity with shareholders,' members' or partners' equity exceeding five million dollars (\$5,000,000) according to its most recent financial statements and which has been in business for not less than five (5) years prior to the sale;

d. A trust with total assets exceeding five million dollars (\$5,000,000) according to its most recent financial statements and which has been in operation for not less than five (5) years prior to the sale; or

e. Any other entity or a trust in which all of the equity owners are High Net Worth Individuals or High Income Individuals;

(2) [optional] The prospective franchisee is represented by legal counsel in the transaction; and

(3) The franchisor reasonably believes immediately before making the offer or sale that the prospective franchisee, either alone or with the prospective franchisee's representative, has sufficient knowledge and experience in the type of business operated under the franchise such that the prospective franchisee is capable of evaluating the merits and risks of the prospective franchise investment.

(ii) The exemption set forth in §3(c)(i) of this (regulation)(statute) may be claimed only if the franchisor:

(1) Reports the sale to the [administrator] on the Notice of Exemption in the form prescribed by the [administrator] within 14 calendar days following the sale;

(2) Obtains from the prospective franchisee a signed certification verifying the grounds for the exemption;

(3) Files a Consent to Service of Process naming the [administrator] as the franchisor's agent to receive process in this state;

(4) Pays the fee required under this [subtitle] for filing an exemption; and

(5) Delivers to the prospective franchisee at least 14 calendar days before the sale a Franchise Disclosure Document prepared under the FTC Franchise Rule or the Franchise Registration and Disclosure law of a state.

(iii) The exemption set forth in §3(c)(i) of this (regulation)(statute) applies only to the registration provisions, and not the disclosure provisions, of [the subtitle].

(iv) By filing a Notice of Exemption under §3(c)(i) of this (regulation) (statute), the franchisor agrees to supply any additional information related to the franchise offering that the [administrator] may from time to time reasonably request.

(d) **Substantial Investment**

(i) The registration provisions of § _____ of the [subtitle] shall not apply to any offer or sale, including transfer, of a franchise that meets all of the following requirements:

(1) The offer or sale is of a single unit franchise in which the actual minimum initial investment is in excess of two million dollars (\$2,000,000) and does not exceed 20% of the franchisee's net worth, excluding the franchisee's principal residence, furnishings and automobiles for personal use;

(2) The prospective franchisee is represented by legal counsel in the transaction; and

(3) The franchisor reasonably believes immediately before making the offer or sale that the prospective franchisee, either alone or with the prospective franchisee's representative, has sufficient knowledge and experience in the type of business operated under the franchise such that the prospective franchisee is capable of evaluating the merits and risks of the prospective franchise investment.

(ii) The exemption set forth in §3(d)(i) of this (regulation)(statute) may be claimed only if the franchisor:

(1) Reports the sale to the state [administrator] on the Notice of Exemption in the form prescribed by the [administrator] within 14 calendar days following the sale;

(2) Obtains from the prospective franchisee a signed certification verifying the grounds for the exemption;

(3) Files a Consent to Service of Process naming the [administrator] as the franchisor's agent to receive process in this state;

(4) Pays the fee required under this [subtitle] for filing an exemption; and

(5) Delivers to the prospective franchisee at least 14 calendar days before the sale a Franchise Disclosure Document prepared under the FTC Franchise Rule or the Franchise Registration and Disclosure law of a state.

(iii) The exemption set forth in §3(d)(i) of this (regulation)(statute) applies only to the registration provisions, and not the disclosure provisions, of [the subtitle].

(iv) By filing a Notice of Exemption under §3(d)(i) of this (regulation) (statute), the franchisor agrees to supply any additional information related to the franchise offering that the [administrator] may from time to time reasonably request.

4. Discretionary Exemption

(a) The [registration, or registration and disclosure] provisions of § _____ of [the subtitle] shall not apply to any offer or sale, including transfer, of a franchise when [the administrator], by order or written notice, finds that the offer sale, or other transfer is not one within the purpose of [the subtitle], and that registration of that offer, sale or other transfer is not necessary or appropriate in the public interest or for the protection of prospective investors;

(b) The exemption set forth in §4 of this (regulation)(statute) may be claimed only if the franchisor:

(i) Prior to the filing of a Notice of Exemption, has made a written request to [administrator] setting forth the basis for the exemption in the form the [administrator] prescribes;

(ii) Submits a copy of the [administrator's] signed order of exemption;

(iii) Files a Notice of Exemption in the form prescribed by the [administrator] not less than 14 calendar days before the offer or sale of any franchise in this State subject to this exemption;

(iv) Files a Consent to Service of Process naming the administrator as the franchisor's agent to receive process in this state;

(v) Pays the fee required under this [subtitle] for filing an exemption;
and

(vi) If required under the Order of Exemption, files with the [administrator], in the format the [administrator] prescribes, one copy of the franchisor's current franchise disclosure document prepared under the FTC Franchise Rule or the Franchise Registration and Disclosure law of a state.

(c) By filing a Notice of Exemption under §4(b) of this (regulation) (statute), the franchisor agrees to supply any additional information related to the franchise offering that the [administrator] may from time to time reasonably request.