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Re: Proposed Model Franchise Exemptions

Gentlemen:

Hilton Worldwide, Inc. ("HWI") offers the comments set forth herein on behalf of its franchisor subsidiaries, Conrad Franchise LLC, Doubletree Franchise LLC, Embassy Suites Franchise LLC, Hampton Inns Franchise LLC, Hilton Franchise LLC, Hilton Garden Inns Franchise LLC, Homewood Suites Franchise LLC, HLT ESP Franchise LLC and Waldorf Astoria Franchise LLC (collectively, the "Brands"). As of December 31, 2010, we and our affiliates have approximately 3,200 franchised lodging facilities open and operating worldwide under the Brands. As experienced franchisors, each of the Brands lauds the underlying purpose of pre-sale disclosure laws and agrees that it is important that the investing public have a complete understanding of the franchise offering prior to making an investment. However, not all franchise concepts, and not all franchise candidates, are similarly situated. The prospective franchisee that is purchasing a home cleaning franchise or other low capital investment franchise is not the same type of institutional investor that is investing in building hotels and restaurants. We submit that these institutional, or sophisticated, investors are not the type of investor that the franchise laws are designed to protect, and that the franchise disclosure document is not necessary in order for this type of prospective franchisee to make an informed investing decision. With the characteristics of the prospective exempt franchisee in mind, we offer specific comments relating to the Fractional Franchise Exemption ("FFE"); the Experienced Franchisor Exemption ("Experienced Franchisor"); the Sophisticated Purchaser Exemption for Existing Franchisees ("Existing Franchisee"); and the Sophisticated Purchaser Exemption for Substantial Investments ("Substantial Investment") (collectively, the "Exemptions") that will harmonize the state and Federal approach to disclosure.

Exemptions from Registration and Disclosure

The Existing Franchisee and Sophisticated Investor exemptions are from registration and not from disclosure. Please note that our proposal to have certain transactions exempt from the franchise sales disclosure laws is not an effort to avoid the registration process. Given the number of states with franchise statutes that permit pure notice filings, the variety of exemptions that are available in California, New York, and most recently, Illinois, there are few states doing any substantive review of franchise disclosure documents. From a legal perspective, going through the annual registration process is actually a relatively straight-forward and painless process for a prepared franchisor. It is not our desire to avoid regulatory review that is the issue, but rather: (1) a desire to eliminate the preparation of costly franchise disclosure documents that are not necessary given the nature of our franchisee candidate; and (2) to facilitate the transfer of an existing franchised business to another franchisee without being subject to the 14-day waiting period. To use the Brands as an example, approximately 75% of new franchises that are sold each year within the Hilton portfolio are sold to existing franchisees. While the investment per brand varies, we estimate it costs between $53,000,000 and $90,000,000 to construct a Hilton full-service hotel. When one considers franchise sales in the hotel context, the purchase of the franchise is tangential to the purchase of the hotel and the franchisor is, at the outset, engaging in a franchise sale with an owner who has the financial wherewithal to either build or purchase a multi-million dollar hotel. This type of business transaction is not conducted with the mom and pop type franchisee candidates that the franchise registration and disclosure laws are designed to protect. We submit that an owner sophisticated enough to engage in a real estate transaction that results in the purchase of a multi-million dollar asset is sophisticated enough to select a franchise for that asset without reviewing a franchise disclosure document. We find it particularly ironic that existing franchisees are subject to this requirement since, by virtue of already being a system franchisee, they have received the ultimate disclosure. Accordingly, we propose the deletion of the obligation to disclose in the Existing Franchisee and Sophisticated Investor exemption, or failing that, the elimination of the 14-day waiting period.

The Fractional Franchise Exemption

We would suggest two modifications to the FFE exemption: (1) clarification that the exemption applies to the parties' "business" relationship; and (2) clarification that the 20% rule may be satisfied by the franchisee's affiliates. We suggest this change because many franchisees create special purpose entities to hold the franchise agreement for tax planning and liability issues. As a result, many franchisees cannot meet the requirement of Section 1(a)(ii) that sales arising from "the relationship" will not exceed 20% of the

franchisee's total dollar volume during the first year of operation. The relationship, as set forth in the model exemption, would appear to refer to the franchise relationship between franchisor and franchisee relating to the franchised outlet at issue. Given that the creation of the SPE is a corporate construct, we would propose that the language state that "sales arising from the operation of the franchised business will not exceed 20% of the franchisee's (or its parent and affiliates') total gross sales during the first year of operation."

The Experienced Franchisor Exemption

Most franchise companies that sell multi-unit concepts create separate franchise companies to sell franchises under the brand, for a variety of corporate reasons. When a franchisor creates a new brand, or simply creates a new franchise company to reflect a new ownership structure as the result of a merger or acquisition, the franchisor is not eligible for an exemption. Using the example of brand creation, you may have a franchisor with multiple brands that qualify for an exemption while having a new brand, owned by the same parent, having to go through the registration process for a five-year period. Accordingly, we would propose that Section 2(a)(ii) be modified to permit the "tacking" of the experience of the parents and affiliates to that of the franchisor.

The Existing Franchisee Exemption

We further propose the deletion of Section 3(a)(i)(5), which requires the form of franchise agreement to be "substantially similar to the first franchise agreement between the franchisor and the existing franchisee." Franchise agreements are long-term agreements. The requirement that they be "substantially similar" is vague to the point that the net result will be the franchisor's decision not to use the exemption because the judgment call it requires is so vast. Existing franchisees are in the position to understand their current agreement and to evaluate the new form of agreement prior to making a purchasing decision.

The Substantial Investment Exemption

Section 3(d)(i)(2) requires all prospective franchisees to be "represented by legal counsel in the transaction." We would propose eliminating the requirement that a franchisor require a franchisee to employ an attorney to close a transaction and submit that investors should be able to determine what advisors, if any, are necessary. Since the franchisee is required to certify the grounds for the exemption as it is, we think this additional layer is unnecessary. We further propose the deletion of Section 3(d)(i)(3), requiring the franchisor to have an opinion as to whether "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." One would have to assume that the franchisor evaluates prospective franchise candidates as part of the application process. However, it would appear that the remedy for franchising with an unqualified candidate would be to simply give that candidate a disclosure document. The focus of this exemption is transactions in excess of Two Million Dollars. Requiring the franchisor to make this judgment, which simply will have the effect of ensuring the exemption is not used by careful franchisors, does not further the purpose of the franchise registration or disclosure laws or the creation of a uniform set of exemptions.

Discretionary Exemptions

We appreciate the recommendation that all registration states provide the opportunity for granting Discretionary Exemptions. Our only suggestion with regard to this exemption as drafted is to permit it to be granted on less than 14-days notice. It has been our experience that most circumstances in which an exemption is needed are those in which the franchisee has a business need to close a transaction before the expiration of required time periods for disclosure. When properly presented and documented, these applications for exemption should be granted on less than 14-days notice.

The Process of Claiming Exemptions

Aside from the substantive provisions of the Exemptions, we would like to comment on the process and requirements surrounding utilizing Exemptions. The FFE exemption requires the franchisor to file a Notice of Exemption no less than 14 calendar days before the offer or sale of any franchise in the state. The Existing Franchisee and Substantial Investment exemptions require that the notice of exemption be filed within 14 days following the sale of a franchise. Given that three of the four exemptions are based upon characteristics of the franchisee, it would appear that the notice filing requirement is on a per-deal basis, and is not intended to be an annual filing. First, it is difficult to predict with any degree of certainty whether or not any given deal will actually result in a franchise sale. Second, imposing a 14-day waiting period will unnecessarily delay the transfer of franchised outlets as part of real estate transactions. Accordingly, we would request that notice of exemptions, and any fees due therewith, be required 14 days after the franchise sale takes place for all exemptions that are not intended to be annual in nature. We would further appreciate clarification that the requirements relating to the filing of a Consent to Service of Process, financial statements and certifications of compliance are meant to be filed on an annual and not per-deal basis. Given that these

documents are filed with the state, and not given to the franchisee, it would not seem to serve any purpose for the state to receive copies of identical documents on a per-deal basis, especially from franchisors that sell hundreds of franchised outlets per year.

We appreciate your consideration of our comments.

Very truly yours,

Karen Boring Satterlee
Vice-President & Senior Counsel
Global Franchise Development

cc: John Dent, Esq.