



July 13, 2018

**VIA EMAIL**

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**Re: Comments to Proposed New State Cover Sheets to Franchise Disclosure Documents**

Dear Messrs. Cantone, Staley, Beatty, and Stewart:

Cheng Cohen LLC submits comments to NASAA's Franchise Project Group's ("NASAA") Notice of Request for Public Comments Regarding Proposed New State Cover Sheets to Franchise Disclosure Documents ("Notice"). We understand and support many of NASAA's proposals, but hope our comments are constructive and shed light on the challenges faced by franchisors and franchisees alike with respect to the issues raised in the Notice.

**Sample Page – How to Use This Franchise Disclosure Document**

The purpose of a Franchise Disclosure Document (FDD) is to provide prospective franchisees with all of the information the FTC believes relevant to the prospect's ability to make an informed decision about the purchase of a franchise. The encompassing nature of the FDD and the importance of all of the information in it are evident from the FTC's cover page that instructs the prospect to "*Read this Disclosure Document and all accompanying agreements carefully*" and to "*Show your contract and this Disclosure Document to an advisor, like a lawyer or an accountant.*" To reinforce the importance of reading the entire document, franchisors are prohibited from providing prospects with stand-alone FDD Receipts, forcing them to download the entire document, not just parts of it—in other words, not making it easy for the prospect to gloss over sections of the FDD that don't address questions like "How much will I earn?" The proposed "How to Use this Disclosure Document" page

works against that notion by emphasizing and directing prospects' attention to certain sections of the FDD and certain types of information over others. Every section of the FDD, not just certain highlighted sections, deserves the full attention of prospective franchisees and their advisors.

Further, the first question on the page ("How much will I earn?") directs prospective franchisees to Item 19. However, this instruction unfairly discriminates against franchisors that elect not to include an Item 19 disclosure. In fact, many (if not a majority) of franchisors disclose in Item 19 something other than "earnings." Especially in predominantly franchised systems, many Item 19 disclosures focus on "revenue" rather than "earnings." Directing the prospect, in every case, to Item 19 for an answer to "How much will I earn?" can be overtly misleading if what's disclosed in Item 19 is something other than the answer to that question.

We're also concerned that the tone of the questions not be unduly negative. For example:

- The fourth question on the page ("Is the franchise system stable and growing or shrinking?") unfairly suggests that if a franchise system is not "growing" then it isn't "stable." It also suggests that a shrinking system is not stable, which might not always be the case, especially when the amount of "shrink" that might indicate something other than stability isn't specified (for example, having a negative net number of 1 unit in a 400-unit system would reflect a system that has "shrunk," but it's certainly not necessarily an indication of instability). In fact, the word "shrinking" in this context can have an unjustified negative connotation. It might be more appropriate to ask, "Is the system growing?"
- The sixth question on the page ("Does the franchisor have a troubled legal history?") unfairly suggests that all franchisors that disclose litigation in Item 3 have a "troubled" history. Most franchise systems, in particular larger franchise systems, will have some amount of litigation to disclose for the preceding 10 years. Such disputes are not always an indicator of "trouble" in the system, and they shouldn't be labeled as such. To the contrary, often litigation that gets disclosed in Item 3 arises from the franchisor's efforts to enforce system standards, and doing so benefits those franchisees who are working hard to build the brand by working within the system and in accordance with their franchise agreements.

Ultimately, if this proposed page is not jettisoned altogether, we would strongly encourage you to draft the questions in a neutral tone that does not reflect unfairly on the health of the system.

### Sample Page – What You Need to Know About Franchising *Generally*

The underlying assumption for this page is that the issues are uniform across all franchise programs. This is simply not the case—not all franchise programs are alike. To the extent the information does not apply to certain franchise programs, this proposed page may cause confusion for prospective franchisees. There is already a resource for prospective franchisees to review if they have questions about franchising in general—"A Consumer's Guide to Buying a Franchise"—and this resource is highlighted on the FTC's cover page.



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We appreciate being provided the opportunity to submit our comments. If you would like additional clarifications or explanations of our comments, please feel free to contact Amy Cheng or Michael Daigle at 312.243.1701.

Very truly yours,

CHENG COHEN LLC

*Cheng Cohen LLC*