JOSH DOAN: Good afternoon or good morning, as the case may be. My name is Josh Doan, and I'm an Attorney in the FTC's Division of Marketing Practices. This panel will explore some of the comments the FTC received last year about the use of disclaimers, waivers of reliance, and questionnaires in connection with franchise disclosure documents and franchise agreements.

If we have time, I will try to incorporate questions we receive from our virtual audience. Please submit those questions to franchiserule@ftc.gov. We have a lot to cover. But first, I'd like to briefly introduce our distinguished panelists. Their bios are available on the event page if you would like to learn more about their impressive work.

Howard Bundy is a Seattle, Washington Attorney who represents franchisors in dispute resolution and also works-- I'm sorry, represents franchisees in dispute resolution and also works with franchisors in preparing contracts and disclosure.

Amy Cheng is a Partner at Chicago's Cheng Cohen LLC, where she represents franchisors on structuring and operation of their franchise programs through all phases of domestic and international development.

Theresa Leets is the Assistant Chief Counsel of the Securities Regulation Unit of the California Department of Financial Protection and Innovations Legal Division, where she supervises programs under the state's Corporate Securities Law of 1968 and franchise investment law.

Brandon Moore is a resident of Northern Virginia and a former franchisee who will bring a nonlawyer's perspective to today's panel.

And Lee Plave is a partner at Reston, Virginia's PlaveKoch PLC, where he counsels franchisors and distributors, drafts and negotiates agreements for international and domestic transactions, and advises clients on all aspects of franchise and distribution law.

And so as we get started, I would like to say on behalf of myself and the panelists, the views we express today are our own and do not necessarily reflect the views of

the Federal Trade Commission or any other particular organization, law firm, or company. And so with that, let's get started by talking about disclaimers.

The franchise rule prohibits disclaimers and representations made in the franchise disclosure document or in its exhibits or amendments. So I'd like to start by asking Howard Bundy, are franchisors still making disclaimers in their disclosure documents despite that prohibition, and if so, in which items?

HOWARD BUNDY: Josh, yes, they are. They continue to make them. If anything, we've seen an increase in the use of what I would generally characterize as disclaimers since 2007. Disclaimers come in three forms. There are outright disclaimers. There are waivers of reliance or statements of nonreliance or their acknowledgments that appear to be benign, but are not, at the end of the day.

So yes, we see an increase. I think it is approaching the point now where for an attorney doing compliance work for a franchisor, if you do not include all of those, you probably are exposed to a legal malpractice and service. And is that always-- that [? much ?] always present that we see those.

You also hear back from franchisor clients who are going through the process that everybody else has these disclaimers. They have read on the internet or heard in seminars how valuable the disclaimers are. And they want them too.

So in my view, this is the most important of the issues before the FTC today because unless the Commission or the states get a handle on the disclaimer issues, the remainder of the disclosure is basically wasted. Everything else contained in the rule, all the other issues the FTC is looking at, get superseded and rendered essentially meaningless if the franchisor can go outside of the vacuum, the outside of the FDD, and say whatever they want to say in order to make a sale and then hide behind the waiver disclaimer to avoid liability in the end.

And yes, I wish it were not true, but particularly the federal courts and arbitrators broadly enforce waivers and disclaimers against franchisees. Maybe we can talk later about what the franchisee thinks he or she is signing when they sign these waivers and disclaimers. But I'll leave that for later.

In terms of where these are found, they're found, number one, in item 19 they're

found in item 11. And they're found in a separate section of the FDD that has become [? on ?] the [? present ?] that usually follows [INAUDIBLE] just the head of the receipt pages, but it [? flows ?] around in there somewhere in the exhibits portion. It's usually a one- to three-page document with a series of questions that the franchisee is required to answer yes or no. And those get presented by the transactional lawyers and by the franchisors as necessary to police potentially problematic salespeople, rogue salesperson defense.

But the minute the franchisee makes a claim later that they were lied to or misled, that disclaimer, that questionnaire, comes in as exhibit A from the defense side. And [INAUDIBLE]--

JOSH DOAN: Thank you, Howard. And we are sorry. And we are going to get into the questionnaires and acknowledgments a bit. And there is a lot in your response. I just want to follow up on that a bit.

One of the items that you mentioned where you report continuing to see disclaimers is in item 19. And item 19 was the subject of the first panel today. And as we left off, I believe Sandy Wall, one of the panelists, was touching on attention that maybe we can explore a bit here between adequately explaining from a franchisor's perspective the reasonable basis for financial performance representation and an impermissible disclaimer.

So, Lee Plave, do you want to take that up?

LEE PLAVE: I'm happy to. Thank you for having us on this discussion. It's very interesting and very useful. There's a big difference between explaining and disclaiming. And a disclaimer is flat-out prohibited under 436.9(h) in any case. So a disclaimer that's been made in the context of the FDD is, by definition of the rule, ineffective.

So I leave it at that. I think it would be very helpful, though. And to pick up on a point that the first panel discussed, if your goal is to see more FPRs and more fulsome information, then allow people to give some explanation and some context, particularly in a year like this one where there is so much context that's needed. It is a difficult year in which to try to provide details without providing some explanation.

Now, that's not to say that it's a disclaimer. It's an explanation. I don't think anyone

would have an objection if the Commission were to take the rule that currently exists which says, no disclaimers. And just make it more obvious as to what they mean by that and to make it more clear that no disclaimers means that anything that's a disclaimer is ineffective.

I think most franchise lawyers, most franchisor side lawyers, work from that presumption to begin with. So I'll answer your specific question with that specific answer. I don't think we need to overturn things. We already have a clause in the rule that says disclaimers are ineffective. You're don't have to go any further.

JOSH DOAN: Amy Cheng, I see you nodding along. Is there anything you'd like to say to supplement or complement Lee's response?

AMY CHENG: As well, I absolutely agree with Lee in that item 19-- there's also already a required disclaimer, right? The FTC says you've got to include an admonition, right, that a new franchisee's results may differ from the information that's contained in the [? FDD. ?] And I think that's sufficient in terms of the disclaimer.

But as we said, especially during these times, unprecedented times, we're including information in item 19 to provide as up-to-date information as possible to prospective franchisees. But that does require some unusual explanation. And it's not only because of 2020 and the pandemic. But as franchisors provide up-to-date information, [? they ?] provide more detailed information, it's important to allow franchisors to include as much information as possible so that they have-- they're disclosing the material basis on which they're including the information.

So to conclude that that explanation is a disclaimer, I think, would be an inaccurate conclusion.

JOSH DOAN: Theresa Leets, would you like to jump in and provide the perspective of a state regulator from a registration's take?

THERESA LEETS: I would. And I want to thank you for inviting me here today and for joining this fantastic panel. My first comment on disclaimers is that I think it would be helpful if the FTC added a definition of disclaimer to the rule to create clarity, right? So I think if everyone was working under the same definition, there would be less uncertainty in this space.

I understand the term to mean any language that mitigates, contradicts, or disavows the information presented in an FDD. But to the point about after the admonition, especially during uncertain times that we're living in today, regulators here all the time-- sometimes franchisors add an helpful explanation, and it's not a disclaimer. But if the explanation applies to all businesses generally, most regulators view it as a disclaimer because, again, it mitigates, contradicts, or disavows the FPR, meaning it has no reasonable basis.

However, if a franchisor adds language to explain a circumstance or condition specific to a business model, like a size of territory, or seasonal demand for the product, and explains how that might cause results to vary, that would be allowed. But regulators generally find if a franchisor adds a disclaimer to an FPR, it implies the FPR is not representative, or it's not accurate, and it's likely to mislead.

Also, I want to add that if a franchisor knows key factors that cause results to vary, and they don't include it, that is likely to be a material omission, and, I would argue, a deceptive sales practice under both state and federal law. So I'm on board with explanations when they're specific and certainly not when they're general.

JOSH DOAN: OK, one of the things that you mentioned, Theresa, was-- and I believe it was mentioned by others-- is the item 19 admonition. So under the franchise rule, and a franchisor who makes a financial performance representation under item 19 must include a clear and conspicuous admonition that a new franchisee's individual financial results may differ from the results stated in that financial performance representation.

The North American Security Administrators Association, which is sometimes referred to as NASAA, has issued commentary on what those admonitions may say. So should the FTC consider adopting the NASAA commentary on those admonitions? Howard, do you have a perspective on that?

HOWARD BUNDY: Josh, I am of two minds on the issue. And I apologize to everyone in advance for the fact that I have a split personality on that [? end. ?] On one level, I would not advocate for adoption because NASAA is more agile than the FTC can ever be. And one of the beauties of the commentary process is that it allows for a living document that changes as the world changes, that responds as problems occur.

So at that level, I would not like to see it adopted in a static form. If there is a way to adopt it in a nonstatic form so it can be a living, breathing, developing document, I would love that. So split personality today.

JOSH DOAN: Amy, you are a franchisor or attorney working in a registration, but non-NASAA states. So let me ask you, are franchisors tending to follow the NASAA guidelines on admonitions in both, I guess, registration non-NASAA member states and nationally, even a non-registration states?

AMY CHENG: I would say yes. For most part, my clients-- I would advise them to follow the NASAA guidelines in preparing the item 19 disclaimer because, one, you don't know if the franchisor is going to expand into a registration state or not that may need to comply with the NASAA guidelines. And second, frankly, I don't see any issue with the NASAA guidelines. And I think it's a clear admonition-- Theresa's agreeing with me for once, I think. And it helps franchisors all have a level playing field for everyone to say the same thing.

So now the question is, should the FTC adopt it? I don't have concerns with FTC adopting it. However, I'm not sure it's absolutely necessary because I think [? it's ?] complying with the guidelines are complying with the FTC requirement itself. So not sure that if we're going to recommend for FTC to revise the rule. This would be, from my perspective, an important focus that the FTC would want to deal with right now.

JOSH DOAN: OK, thank you. Lee, was there anything you wanted to add?

LEE PLAVE: Only that most franchisors try to have an FDD that applies throughout the country. And to echo Amy's point, if you're going to prepare an FDD, you don't prepare one for some states and others for other states in the most part. As a consequence, you typically prepare it so that you're satisfying the requirements in all of the states.

I would add, though, that the NASAA guidelines, which are perfectly well intentioned and are not that difficult to deal with, at least on paper, didn't go through the same kind of rigorous review, comment, analysis, and thorough rulemaking that the Federal Trade Commission typically adopts under the APA and the Magnuson-Moss Warranty Act. So it's a bit of a different animal in terms of how that is developed

and how it has become a part of the regulatory climate. I'm not sure that you would end up in the same place as you started if you went through that analysis.

JOSH DOAN: And are you speaking to the admonition provisions of the NASAA guidance in particular? Or do you feel the same way about NASAA guidance on financial performance representations [? generally? ?]

LEE PLAVE: No, the admonitions don't bother me. It strikes me that we can all agree on what the appropriate boilerplate should be. And it will end up in the right spot. It's things like an absolute prohibition or ban on company-owned unit information being applied if a franchisor has any franchise units in its network.

I'll give you an example. We have many clients that are fairly innovative, and they come up with a different design for the units they've already got. Under those circumstances, we've been told that the examiners will not permit the use of company-owned data without franchise data. But the franchise data is [? quite ?] literally a different concept, different format of a unit.

In the last 15 or 20 years, what has been previously called nontraditional has actually become traditional because people are constantly innovating and trying to fit the needs of the market. So if a franchisor comes up with a different format of a unit, whether it's a kiosk, a cart, a small format, a large format, a store within a store-- whatever the innovation is, they may have company-owned stores where they've tried it out and given it an opportunity to play out. And they've got some results.

But they don't have franchisees who have yet adopted that new format, that new model, and the like. Being able to provide information about those units is really useful. But under the NASAA guidelines, it's [? bad ?] because if you have any franchise units, you must give that information as well. And that information has nothing to do with the kind of format of units that they're offering at the present time.

So there are tensions that need to be addressed. I suspect with some rational approaches to handling those things, that could be done. But that's just one of the examples of why I think it would be really useful to have a more formal vetting of that with commentary and with responses to the comments and full analysis that I

know is typical of an FTC rulemaking.

JOSH DOAN: [? --you ?] Lee. Unless anybody else has anything on disclaimers, I'd like to move to a related topic, which is waivers of reliance. So under the franchise rule, franchisors may not require franchisees to waive reliance on representations in the franchise disclosure document or its exhibits or attachments. The rule does allow franchisors to use integration clauses so long as the clause does not purport disclaim liability for statements authorized by franchisors in their disclosure document.

So my first question is, do waivers and integration clauses remain a problem in 2020? Brandon Moore, do you have a perspective on this?

BRANDON MOORE: I do. Absolutely, I think these clauses are a problem. Essentially, they give any person involved in the sales process a license to stretch the truth in order to make a sale. And obviously, FPRs are the most hotly discussed issue when it comes to this. So I don't think that we need to discuss them too heavily.

But during the due diligence process, franchisees are asking dozens of questions and reviewing marketing materials surrounding the opportunity. Some of them might relate to the actual business model of the services that they'll be able to offer, what product lines they gain access to. Even what level of support or service they can expect as part of the royalties, or even the experience necessary to survive in the franchise.

The answer to these questions and marketing materials are then used as part of their decision-making process. They repeat it to their business partners, their family, their friends. And then they're taken to perform competition analysis. They study the proposed territory, their location. They build a business plan and even construct a pro forma based off of these representations.

In some cases, the time comes when the franchisee realizes that the opportunity wasn't necessarily as described, and perhaps the discrepancy was with the representation that was material to their purchase decision. By this time, it's frequently too late, and they've already signed a franchise agreement with an integration clause. And they cannot afford a multi-year legal battle with bills going into the hundreds of thousands of dollars.

Instead, they likely go on to fail as a business owner, and they file bankruptcy, and all of the negative things that come with that. And this does happen because the franchisor knew that they could say whatever was necessary to make the franchisee comfortable signing it, whether or not it was accurate, and then hide behind the integration clause. And at that point, there's really no other options left for the franchisee except to hope for regulatory intervention.

JOSH DOAN: Thank you, Brandon. Howard, is your experience representing clients the same as Brandon's?

HOWARD BUNDY: I think Brandon pretty much said it all, that it's not even the existence of the integration clause. [INAUDIBLE] [? the ?] [? big ?] issue is how it's used. An integration clause in its pure sense is nothing but telling the parties that there are no agreements outside of the document. Where it becomes a problem is when it's presented as a defense to fraud and inducement or deceit and inducement.

And so there needs to be a way to limit the reach of the integration clauses and related waivers of reliance to just the contract issues, no problem with that. But if we could limit it so that it doesn't reach out and become a defense to fraud and inducement, then I think we could find some common ground. And I think that would be extremely beneficial to franchisees who are investing billions of dollars in these franchises and often losing it with no remedy available except, as Brandon said, to file for bankruptcy.

[? You know, ?] ideally, the franchise industry is not here [INAUDIBLE] to enrich bankruptcy lawyers and to make money out of US Treasury because much of the financing for franchisees comes directly out of the Small Business Administration, and thus, out of taxpayers' pockets. It's billions of dollars a year in losses to taxpayers that results because of it, and in large part because of these waivers and integration clauses improperly applied. So yes.

JOSH DOAN: All right, Lee Plave, do you have any reaction to that? Is the issue with allowing the inclusion of integration clauses? Is the problem the way courts look to them after there is a contract dispute? Where do you come down on this?

LEE PLAVE: Well, you just hit the nail on the head. You refer to a franchise agreement as a contract. And its hornbook, black letter law that in the contract, parties have the

right, if not the need, to say this is the contract. Look at *Corbin on Contracts,* California's Supreme Court, Ninth Circuit, Second Circuit, all of the circuits. A contract with an integration clause is part of-- that is part of American jurisprudence.

It's not to say that-- again, to go back to the previous portion of our discussion, it's not to say that there is anyone disclaiming what's in the FDD. But it is entirely reasonable for parties to say, our contract is what's in this document, and nothing else. It's no different than the world of franchising than it is in the world of buying a car or signing a lease or commercial real estate, buying a home, or any other transaction.

An integration clause is fully understood and accepted throughout the American legal jurisprudence. Changing that here wouldn't make any sense at all. The issue is really being able to read and understand the contract. And if a franchisee has an issue with that, and I can certainly understand why that would be the case. They need to engage counsel, experienced, competent, counsel, to assist them.

If they choose not to spend the money on counsel when they're making an investment of this nature, then I feel badly for them, but that's not the smart decision to make. You would no sooner buy a home without some lawyer involved to help you understand the provisions than you would sign a contract of this magnitude without having a qualified and experienced lawyer. I think that's the right way to go.

JOSH DOAN: Theresa, do you have a perspective on this as a regulator? Or do you [? view ?] [? this as ?] more a dispute between parties to the contract?

THERESA LEETS: Oh no, it goes so much further. I think the-- and I agree with it. Technically, as an attorney, I agree with what Lee is saying. But I think it's only part of the story. And I think Brandon spoke to the other part.

Integration clauses illustrate the power and information imbalance in the franchise relationship that favors and franchisor. And these clauses circumvent investor protection. If the public policy is to prevent false and deceptive sales practices, then we need to modify these integration clauses, right? And they need to have language that don't allow the franchisor to prevent a franchisee from bringing a claim for

false and deceptive sales practices, right?

And these clauses should also allow franchisees to rely on representations made by former and existing franchisees. The rule recognizes that franchise existing and former franchisees offer material information about the franchisor, the franchise system and the relationship. But these integration clauses say, look, if it's not in the FDD, you can't rely on it. And you're not relying on any representations made.

And yet, they don't have to make FPRs. So a lot of information that people need to make an informed decision are not in the contract. They're not in the FDD. And these integration clauses circumvent the franchisee's ability to bring a lawsuit if they even have the money to bring a lawsuit.

So I think fairness requires disputes over false and deceptive sales practices should be determined by a trier of fact and not by an integration clause because when allegations of fraud are proven, it allows industry to identify, remove, or rehabilitate bad actors. And it's necessary for investor protection.

So transparency, accountability in the sales process-- it preserves the integrity of the franchise channel of commerce. So yes, integration clauses are a normal part of contract law. But the franchisee relationship is a very different creature. And I think we have to recognize the power and information imbalance favors the franchisor.

JOSH DOAN: Amy Cheng, I couldn't tell whether you were agreeing with Theresa there and suspected you might not be.

THERESA LEETS: I would not.

JOSH DOAN: Is there anything you'd like to add?

THERESA LEETS: I'm not.

AMY CHENG: Not fully in this instance. So a couple of points, but I absolutely agree with Lee that you're taking away one of the basic principles of contract law if you take away the integration clause. And I don't see why this relationship is any different than any

other relationships that are governed by a contract.

But also, if you look at it from a franchisee's perspective, if I'm a franchisee, would I want to know which contract-- what the terms of my relationship? I would want to know as well. So I'm not sure that taking away the integration clause protects the franchisee from that perspective as well.

The franchisee is entitled-- two parties are entitled to know the terms of their relationship. And without documenting it on a piece of written agreement, I don't know how anybody would ever be able to guess their obligations, future obligations, during the relationship, right?

And two, I don't agree that taking away the integration clause is the way to go so that franchisees cannot sue franchisors for fraud. There are many claims that I think franchisees have successfully brought under state false and deceptive trade practice acts, and where franchisees have prevailed, right?

And we have gone many years now with integration clauses in most of these contracts where franchisees have prevailed or their circumstances are correct for them to do so. So I'm not sure taking the integration clause really would-- well, having the integration clause would prevent the franchisees from bringing those lawsuits. I think franchisees will be able to bring those lawsuits and will continue to be able to prevail. The circumstances are there.

And third, if you take away the integration clause, and now we don't have the agreement in writing, what happens if a franchisee or a franchisor transfers the agreement? Franchisees and franchisors assign franchise agreements all the time. Franchisees sell their businesses. Some buyers assume existing contracts, while others may sign a new contract.

It takes away the ability, frankly, for a franchisee to be able to do that and for a franchisor to be able to assign a contract. Who would spend money to purchase a contract when they don't understand and they cannot rely that the terms of the contract will continue going forward?

THERESA LEETS: Can I respond to that, Josh?

JOSH DOAN: Sure, and then let me go to Howard--

THERESA LEETS: Real quickly.

JOSH DOAN: --and Lee after that.

THERESA LEETS: Yeah, I agree with what Amy is saying in that certain integration clauses are OK. It's that part of the integration clause that says that the franchisee did not rely on or have any representations outside the FDD. That's the problem part, and that's the part that has to be removed or limited. And that's the part that prevents franchisees from bringing lawsuits. Not the standard integration clause saying this is the intent of the parties-- absolutely, that should be in the agreement.

JOSH DOAN: OK, Howard, do you have something you'd like add?

HOWARD BUNDY: Thank you. I wanted to take issue with something that Lee said that also came up in the first workshop this morning. And that is the statement that franchisees before they invest, should consult with someone like me before they invest. The reality is somewhere different from that.

Franchisees, prospective franchisees, tend to come to the table with a mixed bag of experience out of large corporations. They're retired teachers. They're young couples, almost never having business experience. Their first thought is not to talk with lawyers.

They are talking with the sales rep or the franchise executive that's trying to sell them the franchise. And throughout that process, they are being told both directly and through more subtle means that they should not waste their money on lawyers because this document's been reviewed and approved by the government, and it's a safe investment because of that. And besides, we don't negotiate anything. We won't change anything.

That results in franchisees, prospective franchisees, saying, well, if they won't change anything, if they won't negotiate anything, why should I spend a few thousand dollars having a lawyer look at it? And yes, that is a wrong decision. But that is the decision that's being driven by the sales process. And believe it or not,

even that set of misrepresentations that leads to those bad decisions to not hire counsel is wiped out by these clauses that we're here to talk about today.

JOSH DOAN: Lee Plave, what'll your response be?

LEE PLAVE: Yeah, it'll come as virtually no surprise that I disagree with virtually everything that Howard just said. But I'm not going to refer to him the way that Vincent Laguardia Gambini might have or might have responded. But the reality is, what you've described, Howard, and to a degree or another, what Theresa described, was an information imbalance. And that's precisely what disclosure is intended to address.

I'm not aware of the instances that you're talking about. And I'm sure that when the rulemaking record opens up, you'll put in copious evidence of that. I'm not aware of franchisors that discourage franchisees, prospective franchisees, from talking to lawyers, precisely the opposite.

But to address that imbalance, the easiest thing to do would be to have the FTC require a boilerplate that says, this is a serious investment. We recommend strongly that you seek out counsel with experience in this area and an auditor with experience in this area.

I was part of the FTC's team that regulated used cars and funerals years ago. Expensive as those are, they pale in comparison to the costs of buying a franchise. Buying a franchise is an investment that runs somewhere between $50,000 on the low end and over well north of a million on the high end.

It's just inconceivable to me that somebody would make a judgment of that nature and elect not to hire counsel because it's too expensive. If you're going to spend that kind of money, you make, the choice of hiring counsel. And if you choose not to, that's not a choice that's attributable to the other side of the equation.

The FTC, however, can address that imbalance by adding a disclaimer-- not a disclaimer, sorry-- a statement that-- yeah, a disclaimer-- a statement that would tell the franchisee, go out and find a lawyer. Go out and find an accountant. I think that would be a really useful thing to achieve the public policy goal of encouraging people to hire folks like Howard or talking to Brandon or talking to others of their colleagues who know what they're talking about. And even if they don't get changes

in the agreements, get an assessment of what the contract is that you're signing. It's a critical thing.

And the notion that you can rely on anything that somebody said is really interesting. We've seen franchisees as well make statements about their own experience, their past. It's got to, at some point or another, say, OK, we're done. That's the parol evidence rule. Centuries of jurisprudence suggest that that's the way to go. I don't see how the franchise world is much different.

However, if you do believe that there is an information imbalance, as Theresa suggests, well, I don't know specifically what information that is or how you deal with that. I'd suggest that additional disclosure or additional mandatory boilerplate language to explain, you cannot rely on things that were told to you before you signed this contract.

Read this contract. This is the entire ball of wax. If you have statements to that effect, you put somebody on notice through the regulatory process, that what they might have heard earlier just doesn't have any bearing on what goes forward from here on out. I think that's the better way to proceed.

JOSH DOAN: Amy, I couldn't tell whether there was something you wanted to add. Or did Lee cover it all?

AMY CHENG: I think Lee covered most of it. But I think there is a misconception that franchisors don't want franchisees to read the FDD and read the agreement. I can tell you that most of my clients not only want them to, but they actually spend a lot of time walking franchisees through these documents to explain.

Because as a franchisor, frankly, you don't want to get in a relationship with somebody who has not read the contract You know, I tell my clients all the time, you rather sell a franchise to somebody who has read the contract and understand the terms of the relationship than somebody who goes in there with their eyes closed.

So franchisees, also-- they do have a responsibility to do so if they're going to spend half a million dollars. It's amazing how many people will spend half a million dollars and not spend the money to have an advisor to advise them regarding the contract if necessary.

JOSH DOAN: Thank you, Amy. Let's talk about the questionnaires and acknowledgments, then, if we can move on. My understanding is that some franchisors use questionnaires or acknowledgments during the sales process. How prevalent is the use of those documents? And how and at what stage of the negotiation or discussion of a potential franchise relationship are the questionnaires or acknowledgments presented to franchisees? Brandon Moore, do you have a view on that?

BRANDON MOORE: Yeah. Oops, there's an echo. Typically, this document's presented on the tail end of signing the agreement as kind of a follow up-- oh, one last item. We just need you to sign this. Typically, franchisors may say, I need you to answer favorably towards the franchisor for all of these questions or else you may not be able to get the franchise. I've only heard of one instance where somebody documented this, [? or ?] that they did receive something-- they did answer unfavorably towards the franchisor.

But also, too, what's curious about this is that if you have any questions about some of the definitions of the things that you're asking about the questions, such as, what is an FPR, in the same breath that they're asking you to fill out this form, they're also going to tell you, oh, well don't worry about what an FPR is. You've never seen one because we don't make them. And so there is a little bit of a-- kind of an issue with defining things.

You know, and this goes back to what Mr. Plave was stating. You know, I think an attorney might help in this scenario. But at the same time, I think it's an interesting point of debate.

JOSH DOAN: Thank you, Brandon. Howard, is Brandon's description also your experience working with these questionnaires and acknowledgments on behalf of franchisees?

HOWARD BUNDY: Yes, it is, [? Justin, ?] very much the same experience. We've seen hundreds of prospective franchisees over time. And I don't think I've ever seen a questionnaire-- trying to remember here on the spot. But I don't think I've ever seen a questionnaire filled out by a franchisee where there was other than the desired answer provided where the franchisee actually became a franchisee.

I've seen a couple of instances where, under pressure from certain attorneys, the

franchisee told what I would characterize as the truth, yes, I did get FPRs, or yes, I did get these outside statements. But those people never became franchisees. Can I tell you why that happened? No. But there's an interesting coincidence that of all of the franchisees that we've seen over the years with the almost ubiquitous presence of those questionnaires, we've never seen one where the franchisee had answered, yes, I got impermissible information, and here it is.

JOSH DOAN: Amy Cheng, let me ask you this. Is there a benefit to franchisees in having a franchisor provide them with the questionnaire and acknowledgement document? Or does it strictly benefit the franchisor?

AMY CHENG: No, I think it absolutely may benefit the franchisee as well. I mean, so contrary to the way Howard would describe this document would be a disclaimer, I don't think this document is a disclaimer in any way. It is a questionnaire. It literally is a set of questions, right? So if a franchisee answers questions for-- let me give you an example.

One of the many questions, probably typically, is, have you received any financial information from any franchisor representative other than what's contained in item 19 of the FDD? Now, a franchisee may answer yes, and they write down, so-and-so told me this information, right? Well, if the franchisor receives that document, what I have seen actually is that the so-and-so is another existing franchisee who provided this prospective franchisee with all kinds of financial information.

And the franchisor was able to sit down with the prospective franchisee and explain, you obtained the information from our existing franchisee, right? But you have to understand that this information did not come from us, right? There is not information that you should be relying on or [INAUDIBLE] information coming from the franchisor.

Another example is a franchisee may understand that they're buying a business. And they're getting-- a franchisee will fill it out and say, well, I got information from the seller of an existing franchise business that I'm buying. Again, as the franchisor, you can explain where they got the information on and explain that the information is not from the franchisor. So they have an obligation to do their own due diligence, right? A franchisor cannot verify the financial information that they received. And

they will tell the prospective franchisee, make sure that you do your due diligence.

So as a prospective franchisee, I do think you may benefit from getting that information. And there have been many circumstances over the years where these examples I'm giving have happened, [? and ?] they're real-life examples, where the franchisee did go back to the person from whom they received the information and was able to verify the information and do their own due diligence.

JOSH DOAN: Lee, I think you had something you'd like to add.

LEE PLAVE: I think Amy makes some cogent points here. And I would simply say this-- the questionnaire that asks, did you get any information about gross revenues other than what's in the FDD-- there's no disclaimer in that. You're not saying, we don't stand behind our item 19, or we say that everything we said in the item 19 is not true, or we stand back from it. It's asking a simple question-- did you get information that was any different than what you got in the FDD?

I have seen people who answered that yes. The franchisor then takes it, looks seriously at it, determines what went on. Amy gave some examples of that. I've seen others. It actually also serves an additional point and an additional process. The point of public policy is to get people to comply with the law. And whatever the law is, that's the point of public policy.

If you have the accountability of a sales team that knows it's about to be discovered, if it made some sort of an illegal FPR, because as soon as the franchise agreement is submitted to be signed, then the questionnaire is there, the information is going to be laid bare. Why, then, at that point the salesperson is a whole lot less likely to do something for which they will be held accountable?

Now, Howard suggests that franchisors routinely have their sales team telling people to sign it, no matter what, whether it's true or not. The document says, and usually concludes with, we're relying on your answers. Please be honest and truthful and complete. Again, if somebody can't answer questions on an honest basis, then there is a problem.

I can tell you in my own experience, I have seen that questionnaire used. It is quite prevalently used. And ironically, it was the instigation of the Maryland examiner

roughly 20 years ago that suggested it would be a great way to handle things other than using disclaimers. And that suggestion seems to have led to the use of these questionnaires.

But I have seen the questionnaire used. I have seen a franchisee who asked its counsel to call us up and threaten one of our clients with a lawsuit. And we sent the franchisee's questionnaire to his counsel. It revealed, among other things, the three or four different things that he had told his counsel that were not true. His counsel didn't take the case. There were other pieces to it as well.

The point is, not everybody remembers everything with clarity in the years to come. If you have the opportunity to memorialize what took place just now-- did you get any of this information? Do you understand the information that you got? If not, would you like some more information, some more explanation? That serves a useful purpose, and it's consistent with public policy.

JOSH DOAN: Howard, did you want to respond to that?

HOWARD BUNDY: Yes. I think it needs to be clear that I do not oppose, and I don't think most franchisees oppose, a checklist of facts as to what they did or did not do in the due diligence process. I think there could be a benefit to both franchisees and franchisors in having a formalized checklist.

Again, my problem, as I alluded earlier, is not so much in what the surface of the document says, but in how it gets used in the defense of claims by franchisees. All of a sudden, that sentence that says, I did not receive any inconsistent information, becomes, I waive any claims made because I received information that I didn't understand to be inconsistent. It simply gets applied on the defense of claims in a way that is not consistent with the FTC's goal in creating a level playing field of information and of remedies, potential remedies, for franchisees who get misled in the process.

LEE PLAVE: Could I just say one thing on that?

JOSH DOAN: Sure, briefly, and then I know Amy wants to add something too, [? so. ?]

LEE PLAVE: Oh, sure. I'm sorry. I'll just be brief on this. Howard raises a fair point, which is that if you don't understand the question, then the answer is somewhat more murky than

it should be. But if the question is properly posed, then the answer is honestly given. Then at that point, the only thing that's foreclosed is lying in the future. But if you ask the wrong question, then you're going to get a murky answer. And I think that's why people should be asking the questions the right way. Forgive me.

JOSH DOAN: Sure. Amy, did you have anything you wanted to add to that?

AMY CHENG: Yeah, a couple of things. One is the timing of the document. I don't think it's correct that this document is slipped in at the last minute to a franchisee when they're about to sign the franchise agreement. It does come with the execution of the agreement. However, it is attached as an exhibit to the FDD. So the franchisee has had the opportunity to review this document along with all the other documents.

Under item 22 of the FTC rule, you're required to attach all documents that the franchisee must execute in connection with the purchase of the franchise. So if a franchisor is including this document, it should be attaching it as an exhibit to the FDD.

And second, I don't think that the answer, no, I did not receive any financial information, necessarily precludes in all instances, that Howard alluded to, a franchisee from bringing a claim. And in fact, there have been many lawsuits, I think, over the years, if you read some of these decisions, where a franchisee has executed a questionnaire, [? has ?] [? answered ?] the question that they did not receive.

However, their attorney was able to bring in sufficient evidence that that was incorrect. And there was information provided outside of item 19 where a franchisee was able to prevail. So I don't think that it is-- just because the franchisee answers no, it immediately precludes them. And it's not-- again, this is not a waiver. This is not a waiver of claims. It's very different. It's simply a questionnaire.

JOSH DOAN: Theresa, is there something you'd like to add?

THERESA LEETS: Yes, I definitely have a regulatory perspective on this that might be a little bit different. I question how this questionnaire got into this document. It definitely didn't go through a rulemaking process and was less vetted than the NASAA FPR

commentary, for instance. But it is, I think, very helpful for a regulator to see the questionnaire flags areas that it appears that the franchisees commonly failed to understand in the franchise relationship.

And this goes back to the power imbalance. And it does have the impact of preventing franchisees from being able to bring lawsuits. And a lot of the information in that questionnaire is not in the FDD. And let me give you a quick example. I'll give you three examples.

One of the things a franchisee is commonly required to agree is that they read and understood the FDD, right? But the rule doesn't say anything about whether the franchisee is literate, whether they can read English, whether the FDD was disclosed in language that was suitable to their education reading comprehension level. So we're making a lot of assumptions that may not be true that they understood a very complex and long document.

Second, franchisees are required to do their due diligence, their independent investigation of market conditions and competitive factors. Yet, the franchisor is usually the number one source of that information. And they don't have to disclose that in item 1. So if you're going to ask that on the tail end in a questionnaire that's not expressly authorized, you'd better be amending the rule to make sure that they're disclosing in the FDD information about competition and market conditions.

Last example, another one that the franchisees have to agree to is that their business abilities and efforts are vital to success. Again, many people recruited and told they don't have to have any business experience. Yet, in item 15 of the FDD, the only thing the franchisor has to disclose is whether or not the franchisee has to participate in the business.

Item 15 has to be amended if we're going to include that language in the questionnaire to add a disclosure about business abilities, skills, knowledge, and time commitment needed to run the business being offered. Otherwise, we have a disconnect between what's in the FDD and what's in the questionnaire and what people need to know to make an informed business decision. This is about a relationship. And I think you have to have a better transfer of information if we're going to have a better outcome in this channel of commerce.

JOSH DOAN: Howard is there something you'd like to add to the discussion on that point?

HOWARD BUNDY: I would second what Theresa said. The point that I wanted to make-- and I'll try to make it quickly-- is that the-- I think part of what the Commission needs to understand is that not all franchisors out there are McDonald's or the big names that we hear in franchising all the time that have very sophisticated, qualified counsel guiding them to make sure that they do a good job. There are some good franchisors who've been at it long time, and they figured out how to hire Lee or Amy to do a good job for them.

The franchisors that I see, the franchisors that Theresa sees to a large extent, are much less sophisticated, much less experienced, and frankly, much less honest. They don't care as much about being sure that their franchisees understand. What they care about is that the franchisee can fog a mirror and sign a check.

And that is not the qualifications that the franchisor should be looking for. But that's what they're looking for, because they're trying to hit the bottom line. And that's very true of a lot of young franchisors. It's also true of some of the larger ones.

Recently, [? you ?] had a case involving a franchisor that has 2,000 or 3,000 franchises worldwide. And they were having a fire sale of franchises, selling them in five packs. And the tales they were telling about how well these franchisees were going to do, the spreadsheets that they were putting up on webinars, like what we're doing today, were very impressive. I mean, were I not in the role that I am, it would have been tempting to me to buy a pack of those franchises. They failed in droves.

So I think that we create traffic laws for the person who is careless and runs a stop sign and hits a child. But that same traffic law also impacts the person who's very, very careful, who's never had an accident. That doesn't mean we don't need the traffic laws.

And we need them to be strong and firm, and in this case, to make sure that the franchisee, A, has access to really solid, reliable information, complete and truthful information, and that, at the end, their remedy is not taken away from them through terms hidden in contracts and then suddenly become the billboard the minute a claim is made.

JOSH DOAN: Thank you, Howard. I did want to add one point addressing some of the discussion earlier about the franchise rule and recommending that franchisees have counsel or an accountant to help them review the franchise disclosure document. I did just want to point out that under the franchise rule as currently written-- I believe it's 16 CFR 436.3(e)(3)-- the franchise disclosure document must state on the first page that the terms of the contract will govern your franchise relationship.

Don't rely on the disclosure document alone to understand your contract. Read all of your contract carefully. Show your contract and this disclosure document to an advisor like a lawyer or an accountant. So I did just want to point out that the FTC already has included language to this effect in the rule [? and ?] [? requires ?] in the document.

I think we only have about-- well, my clock just actually turned, so I think we're out of time, for better or worse. I know it's been a great discussion. I want to thank you all for being such lively panelists. And thanks for appearing. And I believe we have a 10-minute break before the next panel. Thank you all.

HOWARD BUNDY: Thank you, Joshua.

AMY CHENG: Thank you [INAUDIBLE].

LEE PLAVE: Thank you. Thank you all.